HYMANS ROBERTSON

London Borough of Havering Pension Fund

Infrastructure allocation

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This report includes information relating to the financial or business affairs of investment managers being considered for investment.

Executive Summary

Introduction

- This paper is addressed to the Pensions Committee (“the Committee”) of the London Borough of Havering Pension Fund (“the Fund”).
- The purpose of this paper is to follow up on the ‘Investment Strategy Update Considerations’ paper presented at the 21 March 2023 Pensions Committee meeting and provide considerations and recommendations for the agreed additional 2.5% allocation to infrastructure assets.
- This paper should not be released or otherwise disclosed to any third party except as required by law or regulatory obligation without our prior written consent. We accept no liability where this note is used by, or released or otherwise disclosed to, a third party unless we have expressly accepted such liability in writing. Where this is permitted, the note may only be released or otherwise disclosed in a complete form which fully discloses our advice and the basis on which it is given.

Summary of Recommendations

Within this paper, we make the following recommendations regarding the previously agreed 2.5% increase to the Fund’s infrastructure allocation:

1. An additional 1.5% allocation to the target allocation to the JP Morgan Infrastructure Investments Fund
2. An additional 1.0% allocation to the target allocation to the LCIV Renewable Infrastructure Fund.

Based on current capital commitments, we expect that will require a c£13m investment to be made in the JP Morgan Fund. We expect that existing capital commitments will broadly deliver the overall target allocation at this time although propose that this be revisited in 12 months.

Current allocations

As at 31 March 2023	Actual	Current Target
JP Morgan	4.1%	4.0%
Stafford	4.1%	3.5%
LCIV Renewables	1.3%	2.5%
Total	**9.5%**	**10.0%**

- Committee has previously agreed to allocate a further 2.5% (c.£22.4m as at 31 March 2023) to infrastructure, increasing the target allocation to 12.5%.
- As at 31 March 2023, the Fund was slightly below target allocation although there are undrawn commitments to both Stafford and LCIV of c£11m and c£17m respectively. Based on current valuations, the immediate drawing of these amounts would be equivalent to increasing the actual allocation to c12.5% (Stafford increasing to 5.1% and LCIV to 3.2%).
- Whilst capital continues to be drawn gradually, we anticipate the outstanding Stafford commitment to be full during 2023 and the LCIV allocation to be fully drawn during 2024. We also note that Stafford will continue to return capital over this time for reinvestment and hence the allocation is likely to reduce.
- Based on the latest cashflow forecasts provided by Stafford, the current target allocation is expected to be broadly retained over the next 12 months.

- In order to determine how to implement the target strategy, the Committee needs to consider two steps:
    - First, what the target underlying split between the three infrastructure managers should be, recognising that the existing managers offer diversification between sectors and investment approach. As agreed with Committee, we have not considered a further mandate.
    - Second, based on the agreed target split and the current and expected allocations, consider what additional investments may need to be made in order to achieve the target allocations.
- Stafford invest in secondary market funds whilst both LCIV and JP Morgan are making direct/primary investments in infrastructure. The nature of the JP Morgan and LCIV funds are also ‘evergreen’ so will allow the investments to be broadly retained over time, rather than requiring continual re-commitments.
- The JP Morgan and LCIV allocations both facilitate pooling, the former through a specific LGPS fee arrangement and the latter directly through the pooling company. Stafford are not included within a pooling arrangement at present.
- We believe there is merit in retaining an allocation to Stafford to obtain diversification but that there are also merits in gaining more direct exposure to infrastructure assets. Accordingly, we have focused on the to directly invested mandates and consider their respective characteristics overleaf.

Key characteristics comparison

	JP Morgan Infrastructure Investments Fund	LCIV Renewable Infrastructure Fund
NAV	$29,488m	£353.3m
Main Regions (Top 3)	Europe (45.3%), US (38.6%), UK (8.3%)	UK (23.0%), Europe (14.0%), Asia Pacific (13.0%)
Main Sectors (Top 3)	Renewable Energy (38.9%), Utilities (34.5%), Aviation/Maritime (26.6%)	Onshore Wind (14.0%), Solar PV (8.0%), Offshore Wind (7.0%)
Number of Investors	1,217	13
Number of Investments	20 portfolio companies (810 underlying assets)	5 funds, each with several underlying investments
Fund inception	1 July 2007	29 March 2021
Cash Yield	6.3%	Still within 4-year ramp up period - performance not yet formally assessed and performance figures not currently produced.
Target Return	8%-12% (Net)	7%-10% (Net)
Fees (p.a.)	0.65%	0.05% LCIV management fee plus management fee for underlying investment managers – these range between 0.9%-1%
Investment Manager	JP Morgan	LCIV
Structure	Open-Ended	Open-Ended
Lock-Up	4 years	5 years

JP Morgan Infrastructure Investments Fund and LCIV Renewable Infrastructure Fund information is as at 31 December 2022..

Comments on fund characteristics

	Comments
Regional	• Both funds are global and primarily invested are developed economies i.e. the UK, US and Europe and Australia. • The benefit of these regions having already established financial regulations and there being a lower risk of political and/or economic instability negatively impacting investments in these regions and subsequent performance.
Sectoral	• Both funds have majority sectoral allocations to renewable energy. • This is expected with the LCIV Renewable Infrastructure Fund's allocation, which, more granularly, includes solar photovoltaics, on/off-shore wind, electric vehicle charging etc. Similarly, the JP Morgan Infrastructure Investments Fund's allocation to renewable energy includes mostly solar energy and on-shore wind.
Diversity of investments	• Although the LCIV fund is concentrated on a specific sector (renewable energy), the fund consists of investment in underlying funds – as at March 2023 there were 5 underlying fund investments. This adds a significant level of diversification • The JP Morgan fund is relatively concentrated for the size of the fund, with only 20 company investments. However, these company investments comprise of a range of underlying assets
Cash yield and target return	• The JP Morgan Infrastructure Investments Fund has been able to report an actual since inception cash yield of 6.3%. However, the LCIV Renewable Infrastructure Fund is in its ramp up period and as such, is not yet formally reporting a cash yield figure • The JP Morgan Infrastructure Investments Fund also has a slightly higher target return, though we would view both funds in the same risk/return region
Liquidity and fund structure	• Both funds have a lock up period – the JP Morgan Infrastructure Investments Fund with 4 years from investment and the LCIV Renewable Infrastructure Fund with 5 years from investment. • Both funds are open-ended and will reinvest capital rather than return this to investors. This means the Fund's allocation will be broadly maintained and is advantageous from a governance/operational perspective

Recommendation

As at 31 March 2023	Actual	Current Target	Proposed Target
JP Morgan	4.1%	4.0%	5.5%
Stafford	4.1%	3.5%	3.5%
LCIV Renewables	1.3%	2.5%	3.5%
Total	**9.5%**	**10.0%**	**12.5%**

- We remain supportive of all the Fund's infrastructure investments and would be comfortable in continuing to allocation to all. We propose increasing the target allocation to JP Morgan by 1.5% and to the LCIV Renewable Fund by 1%.
- We believe there is merit in retaining a degree of diversification in approach, noting that JP Morgan offer exposure to non-renewable infrastructure which are subject to ongoing management action in order to decarbonise activities. This was previously discussed by JP Morgan with Committee.
- We also note that consideration should be given to the pace of capital deployment, with LCIV taking time to draw down whilst capital allocated to JP Morgan is likely to be drawn quickly.
- As noted, both JP Morgan and LCIV allocations provide pooling benefits and increasing the target allocation to these vehicles is thus consistent with the overall pooling objective.
- In the immediate short term, we do not believe it necessary to make a further commitment to the LCIV Renewables Fund as the current committed capital will be largely sufficient to achieve the proposed target.
- Allocations to Stafford are likely to remain temporarily above the proposed target allocation although the return of capital will serve to correct this. We believe it will be appropriate to consider reupping into a future Stafford vehicle during 2024 once drawdowns have been completed.
- In the short-term, a further commitment can be made to the JP Morgan Fund. We propose an allocation of £13m in order to meet the proposed target to be funded from the LCIV DGF. Alongside the proposed commitment to the LCIV Global Bond Fund and existing capital commitments, this will see the DGF allocation reduced to nil in line with expectations.
- We look forward to discussing this with Committee.

Risk Warning

- Please note the value of investments, and income from them, may fall as well as rise. This includes equities, government or corporate bonds, and property, whether held directly or in a pooled or collective investment vehicle. Further, investments in developing or emerging markets may be more volatile and less marketable than in mature markets. Exchange rates may also affect the value of an overseas investment. As a result, an investor may not get back the amount originally invested. Past performance is not necessarily a guide to future performance.