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ISLINGTON

Governance and Human Resources
Town Hall, Upper Street, London, N1 2UD

AGENDA FOR THE PENSIONS SUB COMMITTEE

Members of the Pensions Sub Committee are summoned to a meeting which will be held in Committee Room 4, Islington Town Hall, Upper Street, N1 2UD on **25 March 2019 at 7.30 pm.**

Yinka Owa
Director of Law and Govenance

Enquiries to	:	Mary Green
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Despatched	:	15 March 2019

Membership 2018/19	Substitute Members
Councillor Dave Poyser (Chair)	Councillor Mouna Hamitouche MBE
Councillor Andy Hull (Vice-Chair)	Councillor Jenny Kay
Councillor Sue Lukes	Councillor Angela Picknell
Councillor Michael O'Sullivan	Councillor Flora Williamson

Quorum is 2 members of the Sub-Committee

A. Formal Matters

1. Apologies for absence

2. Declaration of substitutes

3. Declaration of interests

If you have a Disclosable Pecuniary Interest* in an item of business:
- if it is not yet on the council's register, you must declare both the existence and details of it at the start of the meeting or when it becomes apparent;
- you may choose to declare a Disclosable Pecuniary Interest that is already in the register in the interests of openness and transparency.

In both the above cases, you must leave the room without participating in discussion of the item.

If you have a personal interest in an item of business and you intend to speak or vote on the item you must declare both the existence and details of it at the start of the meeting or when it becomes apparent but you may participate in the discussion and vote on the item.

*(a) Employment, etc - Any employment, office, trade, profession or vocation carried on for profit or gain.
(b) Sponsorship - Any payment or other financial benefit in respect of your expenses in carrying out duties as a member, or of your election; including from a trade union.
(c) Contracts - Any current contract for goods, services or works, between you Or your partner (or a body in which one of you has a beneficial interest) and the council.
(d) Land - Any beneficial interest in land which is within the council's area.
(e) Licences- Any licence to occupy land in the council's area for a month or longer.
(f) Corporate tenancies - Any tenancy between the council and a body in which You or your partner have a beneficial interest.
(g) Securities - Any beneficial interest in securities of a body which has a place of business or land in the council's area, if the total nominal value of the securities exceeds £25,000 or one hundredth of the total issued share capital of that body or of any one class of its issued share capital.

This applies to **all** members present at the meeting.

B. Non-exempt items

C. Urgent non-exempt items

Any non-exempt items which the Chair agrees should be considered urgently by reason of special circumstances. The reasons for urgency will be agreed by the Chair and recorded in the minutes.

D. Exclusion of press and public

To consider whether, in view of the nature of the remaining items on the agenda, any of them are likely to involve the disclosure of exempt or confidential information within the terms of Schedule 12A of the Local Government Act 1972 and, if so, whether to exclude the press and public during discussion thereof.

E. Confidential/exempt items

F. Urgent exempt items

Any exempt items which the Chair agrees should be considered urgently by reason of special circumstances. The reasons for urgency will be agreed by the Chair and recorded in the minutes.

The next meeting of the Pensions Sub Committee is scheduled for 17 June 2019

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London Borough of Islington

Pensions Sub Committee - 26 November 2018

Non-confidential minutes of the meeting of the Pensions Sub Committee held at Islington Town Hall, Upper Street, N1 2UD, on 26 November 2018 at 7.30 pm.

Present:	**Councillors:**	David Poyser (Chair), Andy Hull (Vice-Chair), Sue Lukes and Michael O'Sullivan
Also Present:		Maggie Elliott and George Sharkey (Pension Board members and observers) Nikeeta Kumar, Tony English, Peter Tornkvist and Tomi Nummela, Mercer Limited Karen Shackleton – MJ Hudson Allenbridge Paul Middleman and Jonathan Perera, Mercer Limited

Councillor Dave Poyser in the Chair

32 **APOLOGIES FOR ABSENCE (Item A1)**
None received.

33 **DECLARATION OF SUBSTITUTES (Item A2)**
None.

34 **DECLARATION OF INTERESTS (Item A3)**
Councillor Poyser declared a personal interest in agenda item B1, specifically paragraph 3.16.4, as godfather to an employee at Ruffer.

35 **MINUTES OF THE PREVIOUS MEETING (Item A4)**

RESOLVED:
That the minutes of the meeting held on 12 September 2018 be confirmed as a correct record and the Chair be authorised to sign them.

36 **PENSION FUND PERFORMANCE - 1 JULY TO 30 SEPTEMBER 2018 (Item B1)**

RESOLVED:
(a) That the performance of the Fund from 1 July to 30 September 2018, as set out in the BNY Mellon interactive performance report, and detailed in the report of the Interim Corporate Director of Resources, be noted.

(b) That the report by MJ Hudson Allenbridge Advisers on fund managers' quarterly performance, detailed in Appendix 1 to the report and their presentation, be noted.
(c) That exempt Appendix 2 (Mercer's performance analysis of Schroder's Diversified Growth Fund) be noted.
(d) That the position of Hearthstone and Schroder in the Fund be reviewed as part of the June 2019 Investment Strategy Review.

37 TRAINING - ACTUARIAL REVIEW UPDATE (VERBAL) (Item B2)

Jonathan Perera, Mercer, and Paul Middleman, Mercer Fund Actuary, gave a presentation on: the purpose of an Actuarial Valuation, liability calculations, Funding Strategy Statement, 2016 Valuation Recap and what had happened since 2016.

It was noted that there had been a 21% return in real investment returns since March 2016. However, the outlook for future real returns was lower relative to that in 2016. The Fund had implemented an equity protection strategy to protect against equity market price falls and this would impact on the level of prudence that could be considered in the 2019 valuation assumptions. Life expectancy improvements were slowing down, meaning a possible reduction in liabilities/% contributions. Islington was similar to other London boroughs in that contributions were in the middle. There were a number of employees who were currently not in the Fund, who would be re-enrolled in the future. The Pensions Team/Human Resources would need to communicate all the benefits of the Scheme to these employees to encourage them not to opt out in the future.

Also, the public sector pay cap had been removed, meaning that the impact for individual employers would need to be considered. The Actuary would work with the Pension Team on data quality, since good data was important to ensure liabilities were not affected. It was also noted that it was likely that there would be an improvement in benefits/contributions from 2019, leading to an increase in cost for employers. The introduction of Exit Credits for exiting employers from May 2018 would impact on the Fund's policies and employers needed to consider their own commercial arrangements with outsourced contracts. It was thought that guaranteed minimum pension equalisation was unlikely to affect the LGPS, but would affect private schemes.

It was also thought that Brexit would not impact on the Fund's liabilities, but that it could impact on overseas investments.

Jonathan Perera and Paul Middleman were thanked for their presentation.

38 DECARBONISATION POLICY AND DRAFT INVESTMENT STRATEGY STATEMENT (Item B3)

The Chair had agreed that this item be considered as urgent business in order that the policy on decarbonisation could be integrated into Islington Pension Fund's Investment Strategy Statement as soon as possible, in order to ensure that exposure to climate risk and opportunities were taken into account in the selection, non-selection, retention and realisation of investments going forward.

The Chair of the Sub-Committee thanked staff from Mercer for their work in producing a draft Strategy for the Sub-Committee's consideration.

RESOLVED:
(a) That, subject to the following amendments to page 7 of the agenda, comprising Mercer's recommended policies, the draft decarbonisation policy document produced by Mercer, attached as Appendix 1 to the report of the Corporate Director of Resources, be noted:

Second hyphen, line 2 - add the word "April" before "2022" and "or earlier" after "2022", so sentence reads "The Fund seeks to achieve the following targets by April 2022, or earlier"

Recommendation 1), line 4 – replace "XX" with the words "more than half" and delete the words "per cent"

Recommendation 3), line 1 – insert "at least" before the figure "15%"

(b) That the draft decarbonisation policy document be approved and integrated into the draft Investment Strategy Statement, detailed in Appendix 2 to the report.
(c) That the following next steps be implemented:

- The integration of ESG issues, including climate change, in investment policy
- The consideration of positive allocations to sustainable opportunities
- The formulation of a regular monitoring and reporting regime on progress
- The extension of decarbonisation beyond listed equities over the next four years
- The continuation of engagement and collaboration with relevant parties, including the London CIV, on responsible investment

(d) That officers be authorised to update the Investment Strategy Statement (Appendix 2 to the report), in liaison with Mercer, and to publish it on the Council's website.

39 EQUITY PROTECTION STRATEGY - SEMI-ANNUAL MONITORING (Item B4)

RESOLVED:
(a) That the Fund's market to market equity exposure position, as detailed in the report of the Interim Corporate Director of Resources, be noted.
(b) That Mercer's report and presentation highlighting the main features and activities of the strategy to September 2018, detailed in Appendix 1 of the report, be noted.

40 LISTED EQUITY PORTFOLIO REVIEW - LCIV ALLIANZ TRANSFER (Item B5)

RESOLVED:
(a) That the process of reviewing the global equities managers currently available on the LCIV platform, as detailed in the report of the Interim Corporate Director of Resources, be noted.
(b) That the results of the due diligence process, also detailed in the report, be noted.
(c) That Manager A (detailed in exempt appendix E2 of the agenda) be appointed to replace the Allianz sub-fund on the LCIV platform.
(d) That the Interim Corporate Director of Resources, in consultation with the Acting Director of Law and Governance, be authorised to negotiate and agree the following matters with the London CIV:

- The fund management agreement with Manager A
- The appointment of a transition manager to manage the transfer of assets
- The costs associated with the termination of the Allianz sub-fund

41 CONTRACT AWARD FOR INFRASTRUCTURE MANAGER(S) (Item B6)

RESOLVED:
(a) That the outcome of the tender process to procure an infrastructure manager, detailed in the report of the Interim Corporate Director of Resources and the exempt appendix at agenda item E3), be noted.
(b) That Fund Managers A and B (detailed in the exempt appendix at agenda item E3) be appointed as the Islington Pension Fund Infrastructure preferred managers.
(c) That 40% be allocated to Manager A and 60% to Manager B
(d) That Fund Manager C be appointed as the reserve manager for the Islington Pension Fund Infrastructure.
(e) That the Interim Corporate Director of Resources, in consultation with the Acting Director of Law and Governance, be authorised to negotiate and agree the fund management agreement with Fund Managers A and B.

42 LONDON CIV UPDATE (Item B7)

RESOLVED:
(a) That the progress made at the London CIV in launching funds, running of portfolios and reviewing governance and investment structure, from the period August to November 2018, and detailed in the report of the Interim Corporate Director of Resources, be noted.
(b) That a representative from the London CIV be invited to attend a meeting of the Sub-Committee in the near future to address issues around progress and development.

43 **PENSION FUND FORWARD PLAN (Item B8)**

RESOLVED:
That, subject to the addition of the following items to the Forward Plan, the contents of Appendix A to the report of the Interim Corporate Director of Resources, detailing proposed agenda items for future meetings, be noted:

June 2019 – Actuarial valuation results (Mercer)
Date TBA – Update from LCIV representative

44 **PENSION FUND PERFORMANCE - EXEMPT APPENDIX 2 (Item E1)**
Noted.

45 **LISTED EQUITY PORTFOLIO REVIEW - LCIV ALLIANZ TRANSFER - EXEMPT APPENDIX (Item E2)**
Noted.

46 **CONTRACT AWARD FOR INFRASTRUCTURE MANAGER(S) - EXEMPT APPENDIX (Item E3)**
The Sub-Committee noted the contents of the exempt appendix at agenda item B3. They concurred with the views of the shortlisting meeting that the London CIV should not be appointed at this stage as a possible infrastructure manager as their carbon footprint offer was based on a London borough- wide policy and the fact that it could take five years until full deployment.

47 **MEMBER'S REPORT - PENSIONS FOR PURPOSE**
Councillor O'Sullivan reported that he had attended a recent conference on impact investment, run by the organisation "Pensions for Purpose". He commended the work of Pensions for Purpose, suggesting that it made sense to invest in companies, organisations and funds, which had the commercial purpose of solving social or environmental problems, alongside a financial return. He congratulated Karen Shackleton, one of the founder members of Pensions for Purpose.

RESOLVED:
That Islington Pension Fund affiliate to Pensions for Purpose.

The meeting ended at 9.40pm.

CHAIR

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ISLINGTON

Finance Department
7 Newington Barrow Way
London N7 7EP

Report of: Corporate Director of Resources

Meeting of:	Date	Agenda item	Ward(s)
Pensions Sub-Committee	25 March 2019		

Delete as appropriate	~~Exempt~~	Non-exempt

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Subject: PENSION FUND PERFORMANCE 1 OCTOBER TO 31 DECEMBER 2018

1.	**Synopsis**
1.1	This is a quarterly report to the Pensions Sub-Committee to allow the Council as administering authority for the Fund to review the performance of the Fund investments at regular intervals and review the investments made by Fund Managers quarterly.
2.	**Recommendations**
2.1	To note the performance of the Fund from 1 October to 31 December 2018 as per BNY Mellon interactive performance report
2.2	To receive the presentation by MJ Hudsons Allenbridge, our independent investment advisers, on our fund managers' quarterly performance attached as Appendix 1.
2.3	To note LGPS Current issues February 2019 attached as Appendix 2
3.	**Fund Managers Performance for 1 October to December 2018**
3.1	The fund managers' latest quarter net performance figures compared to the benchmark and Mercer ESG ratings is shown in the table below. Mercer's ESG ratings provide an assessment of the integration of ESG issues into the investment process and provides an overall rating – ESG 1 is the highest possible rating and ESG 4 is the lowest possible rating. As such, Mercer has provided the ESG ratings for the Fund's 9 strategies across equities, fixed income, DGFs, property and private equity.

	(table below)

Fund Managers	Asset Allocation	Mandate	*Mercer ESG Rating	Latest Quarter Performance (Oct-Dec'18) Gross of fees		12 Months to Dec' 2018-Performance Gross of fees	
				Portfolio	Benchmark	Portfolio	Bench Mark
LBI-In House	14%	UK equities	N	-8.80%	-10.25%	-7.36%	-9.47%
London CIV Allianz	8%	Global equities	2	-11.4%	-11.24%	-3.11%	-2.50%
LCIV -Newton	16%	Global equities	2	-9.5%	-10.6%	0.42%	-3.27%
Legal & General	11.5%	Global equities	1	-9.62%	-9.72%	-2.75%	-2.46%
Standard Life	15.2%	Corporate bonds	3	-0.08%	0.12%	-1.87%	-1.5%
Aviva (1)	9%	UK property	2	1.20%	2.5% 1.07%	2.7%	0.82% 7.45%
Columbia Threadneedle Investments (TPEN)	6.8%	UK commercial property	2	1.14%	0.89%	6.25%	6.5%
Hearthstone	2%	UK residential property	N	0.42%	1.07%	2.8%	7.45%
Schroders	8.4%	Diversified Growth Fund	4	-5.4%	1.7%	-5.5%	7.7%
BMO Investments-LGM	5.6%	Emerging/ Frontier equities	2	-1.8%	-5.2%	-6.5%	-8.9%

2.5% & 0.82% = original Gilts benchmark; 1.07% and 7.45% are the IPD All property index; for information

3.2 BNY Mellon our new performance monitoring service provider now provides our quarterly interactive performance report. Performance attributions can be generated via their portal if required.

3.3 The combined fund performance and benchmark for the last quarter ending December 2018 is shown in the table below.

	Latest Quarter Performance **Gross** of fees		12 Months to Dec' 2018 Performance Gross of fees	
Combined Fund Performance ex-hedge	Portfolio %	Benchmark %	Portfolio %	Benchmark %
	-5.1	-4.9	-1.3	-2.4

3.4 Copies of the latest quarter fund manager's reports are available to members for information if required.

3.5 **Total Fund Position**
The Islington combined fund absolute performance with the hedge over the 1, 3 and 5 years' period to December 2018 is shown in the table below.

Period	1 year per annum	3 years per annum	5 years per annum
Combined LBI fund performance hedged	-1.25%	7.4%	6.6%
Customised benchmark	-2.4%	6.9%	6.3%

3.6 **AllianzGI (RCM)**

3.6.1 AllianzGI (formerly known as RCM) is the fund's global equity manager and was originally appointed in December 2008. There have been amendments to the mandate, the last being a transfer to the CIV platform.

3.6.2 On 2 December, the portfolio was transferred to the London CIV platform to Allianz sub fund as agreed by Members at the November 2015 meeting. The new benchmark is to outperform the MSCI World Index. The outperformance target is MSCI World +2% per annum over 2 years' net of fees.

3.6.3 This quarter the fund returned -11.4% against a benchmark of -11.2%. Since inception with the London CIV in December 2015, there is a relative over performance of 0.9% whiles since January 2009 the original inception date, relative outperformance is 0.0% per annum. The main drivers for underperformance was due to stock selection and sector weightings. The portfolio holds 50 stocks.

3.6.4 Members agreed in November to replace Allianz with RBC Sustainability fund on the LCIV platform. A full report on progress to date is another agenda item.

3.7 **Newton Investment Management**

3.7.1 Newton is the Fund's other global equity manager with an inception date of 1 December 2008. There have been amendments to the mandate the latest being a transfer to the London CIV platform.

3.7.2 The inception date for the LCIV NW Global Equity Fund was 22 May 2017. The new benchmark is the MSCI All Country World Index Total return. The outperformance target is MSCI All Country Index +1.5% per annum net of fees over rolling three- year periods.

3.7.3 The fund outperformed by returning -9.5% gross of fees against a benchmark of -10.6% for the December quarter. Since inception the fund has delivered an absolute return of 11.35% but relative under performance of -0.07% gross of fees per annum

3.7.4 The out performance this quarter was driven mainly by stock selection in Information Technology and Healthcare sectors in Japan and US regions.

3.8 **In House Tracker**

3.8.1 Since 1992, the UK equities portfolio of the fund has been managed in-house by officers in the Loans and Investment section by passive tracking of the FTSE 350 Index. The mandate was amended as part of the investment strategy review to now track the FTSE All Share Index within a +/- 0.5% range per annum effective from December 2008. After a review of the fund's equities, carbon footprint Members agreed to track the FTSE UK All Share Carbon Optimised Index and this became effective in September 2017.

3.8.2 The fund returned -8.8% against FTSE All Share Index benchmark of -10.2% for the December quarter and a relative over performance of 0.62% over the five- year period. The portfolio is now mirroring the low carbon index and its dividend income is continued to use to supplement cash flow needs of the pension fund bank account, a total of £15m for 2018/19.

3.9	**Standard Life**
3.9.1	Standard Life has been the fund's corporate bond manager since November 2009. Their objective is to outperform the Merrill Lynch UK Non Gilt All Stock Index by 0.8% per annum over a 3 -year rolling period. During the December quarter, the fund returned 0.2% against a benchmark of 0.12.% and an absolute return of 6.5% per annum since inception.
3.9.2	The drivers behind the out performance in this quarter were due to overweight exposure in European securities and strong stock selection. Overweight positions in financials including subordinates was negative .The forward strategy is to move up the credit quality and take advantage of market dislocation.
3.9.3	The agreed infrastructure mandates will be funded from this mandate.
3.10	**Aviva**
3.10.1	Aviva manages the fund's UK High Lease to Value property portfolio. They were appointed in 2004 and the target of the mandate is to outperform their customised gilts benchmark by 1.5% (net of fees) over the long term. The portfolio is High Lease to Value Property managed under the Lime Property Unit Trust Fund.
3.10.2	The fund for this quarter delivered a return of 1.6% against a gilt benchmark of 2.5%. The All Property IPD benchmark returned 1.07% for this quarter. Since inception, the fund has delivered an absolute return of 6.8% net of fees.
3.10.3	This December quarter the fund's unexpired average lease term is now 19.4years. The Fund holds 80 assets with 49 tenants. One sale and 2 student accommodation purchases were completed during the quarter.
3.10.4	The fund also has £510m of investor cash of which £250m is committed to developments and close to completion.
3.11	**Columbia Threadneedle Property Pension Limited (TPEN)**
3.11.1	This is the fund's UK commercial pooled property portfolio that was fully funded on 14 October 2010 with an initial investment of £45 million. The net asset value at the end of December was £88.3million.
3.11.2	The agreed mandate guidelines are as listed below: • Benchmark: AREF/IPD All Balanced Property Fund Index (Weighted Average) since I April 2014. • Target Performance: 1.0% p.a. above the benchmark (net of fees) over three year rolling periods. • Portfolio focus is on income generation with c. 75% of portfolio returns expected to come from income over the long term. • Income yield on the portfolio at investment of c.8.5% p.a. • Focus of portfolio is biased towards secondary property markets with high footfall rather than on prime markets such as Central London. The portfolio may therefore lag in speculative/bubble markets or when the property market is driven by capital growth in prime markets.
3.11.3	The fund returned a relative out performance of 0.2% against its benchmark 0.9% for the December quarter and a 0.14% three - year relative return. The cash balance now stands at 8.6% compared to 7.6% last quarter. During the quarter, there was two acquisitions and 3 purchases. There is a strong asset diversification at portfolio level with a total of 278 properties.

3.11.4	The medium to long term prospects of commercial property post referendum are likely to be a catalyst for moderate capital value declines but the fund is cushioned by its high relative income return and maximum diversification at both portfolio and client level.
3.12 3.12.1	**Passive Hedge** The fund currently targets to hedge 50% of its overseas equities to the major currencies dollar, euro and yen. The passive hedge is run by BNY Mellon our custodian. At the end of the December quarter, the hedged overseas equities were valued at £6.8m.
3.13 3.13.1	**Franklin Templeton** This is the fund's global property manager appointed in 2010 with an initial investment commitment of £25million. Members agreed in September 2014 to re-commit another $40million to Fund II to keep our investments at the same level following return of capital through distributions from Fund I. The agreed mandate guidelines are listed below: • Benchmark: Absolute return • Target Performance: Net of fees internal rate of return of 15%. Preferred rate of return of 10% p.a. with performance fee only applicable to returns above this point. • Bulk of capital expected to be invested between 2 – 4 years following fund close. • Distributions expected from years 6 – 8, with 100% of capital expected to be returned approximately by year 7.
3.13.2	Fund I is now fully committed and drawn down, though $7.1m can be recalled in the future as per business plans. The final portfolio is comprised of nine funds and five co-investments. The funds is well diversified as shown in table below:

Commitments	Region	% of Total Fund
5	Americas	36
4	Europe	26
5	Asia	38

The total distribution received to the end of the December quarter is $53m.

3.13.3	Fund II has made 5 investments to date in Europe, USA and Asia, in the retail and office sector and the projected geographic exposure is 42% Asia, US 26% and 32% Europe. The Admission period to accept new commitments from investors has been extended with our consent through to June 2017. The total capital call to the quarter end was $24.8.m and a distribution of $9.4m.
3.14. 3.14.1	**Legal and General** This is the fund's passive overseas equity index manager. The fund inception date was 8 June 2011 with an initial investment of £67million funded from transfer of assets from AllianzGI (RCM). The funds were managed passively against regional indices to formulate a total FTSE All World Index series. Member agreed restructuring in 2016, that is now complete and the funding of BMO (our emerging market manager and restructuring of the fund to the MSCI World Low Carbon was completed on 3rd July 2017.
3.14.2	The components of the new mandate as at the end of June inception was £132m benchmarked against MSCI World Low Carbon Index and £33m benchmarked against RAFI emerging markets. For the December quarter, the fund totalled £148m with a performance of -9.6% and relative return of -0.1%.

3.15	**Hearthstone**
3.15.1	This is the fund's residential UK property manager. The fund inception date was 23 April 2013, with an initial investment of £20million funded by withdrawals from our equities portfolios. The agreed mandate guidelines are as follows: • Target performance: UK HPI + 3.75% net income. • Target modern housing with low maintenance characteristics, less than 10 years old. • Assets subject to development risk less than 5% of portfolio. • Regional allocation seeks to replicate distribution of UK housing stock based on data from Academics. Approximately 45% London and South East. • 5-6 locations per region are targeted based on qualitative and quantitative assessments and data from Touchstone and Connells. • Preference is for stock which can be let on Assured Shorthold Tenancies (ASTs) or to companies. • Total returns expected to be between 6.75% and 8.75% p.a., with returns split equally between income and capital growth. Net yields after fund costs of 3.75% p.a. • The fund benchmark is the LSL Academetrics House Price Index
3.15.2	For the December, quarter the value of the fund investment was £28.3m and total funds under management is £56million. Performance net of fees was 0.4% compared to the LSL benchmark of 1.1%. The portfolio has 204properties. Average annual occupancy 93.8%. Officers will with its advisors conduct a review of the fund in early 2019.

3.16
3.16.1
	Schroders-
	This is the Fund's diversified growth fund manager. The fund inception date was 1 July 2015, with an initial investment of £100million funded by withdrawals from our equities portfolios. The agreed mandate guidelines are as follows:
	• Target performance: UK RPI+ 5.0% p.a.,
	• Target volatility: two thirds of the volatility of global equities, over a full market cycle (typically 5 years).
	• Aims to invest in a broad range of assets and varies the asset allocation over a market cycle.
	• The portfolio holds internally managed funds, a selection of externally managed products and some derivatives.
	• **Permissible asset class ranges (%):**
	  • 25-75: Equity
	  • 0- 30: Absolute Return
	  • 0- 25: Sovereign Fixed Income, Corporate Bonds, Emerging Market Debt, High Yield Debt, Index-Linked Government Bonds, Cash
	  • 0-20: Commodities, Convertible Bonds
	  • 0- 10: Property, Infrastructure
	  • 0-5: Insurance-Linked Securities, Leveraged Loans, Private Equity.

3.16.2 3.16.3	This is the fourteen quarter since funding and the value of the portfolio is now £108m. The aim is to participate in equity market rallies, while outperforming in falling equity markets. The December quarter performance before fees was -5.35% against the benchmark of 1.73% (inflation+5%). The one -year performance is -5.45% against benchmark of 7.70% before fees. The underperformance was attributed to equity exposure in the US and credit exposure. However, losses were cushioned by gains in alternatives and government bonds.

3.17	**BMO Global Assets Mgt** This is the new emerging and frontier equity manager seeded in July 2017 with a total £74.4m withdrawn from LGIM. The mandate details as follows: • A blended portfolio with 85% invested in emerging market and 15% in frontier markets • Target performance MSCI Emerging Markets Index +3.0% (for the global emerging markets strategy) • Expected target tracking error 4-8% p.a • The strategy is likely to have a persistent bias towards profitability, and invests in high quality companies that pay dividend
3.17.1	The December quarter saw a combined performance of -1.77% against a benchmark of -5.19% before fees. The performance is mainly due to stock selection. The strategy remains to continue to research new companies that we suspect might be worthy of your hard earned capital and continue to have a close communication with our existing investments to push them to higher business and governance standards which we believe will ultimately enhance your long term return.
4.	**Implications**
4.1	**Financial implications:** The fund actuary takes investment performance into account when assessing the employer contributions payable, at the triennial valuation. Fund management and administration fees and related cost are charged to the pension fund.
4.2	**Legal Implications:** As the administering authority for the Fund, the Council must review the performance of the Fund investments at regular intervals and review the investments made by Fund Managers quarterly.
4.3	**Resident Impact Assessment:** The Council must, in the exercise of its functions, have due regard to the need to eliminate discrimination, harassment and victimisation, and to advance equality of opportunity, and foster good relations, between those who share a relevant protected characteristic and those who do not share it (section 149 Equality Act 2010). The Council has a duty to have due regard to the need to remove or minimise disadvantages, take steps to meet needs, in particular steps to take account of disabled persons' disabilities, and encourage people to participate in public life. The Council must have due regard to the need to tackle prejudice and promote understanding". An equalities impact assessment has not been conducted because this report is an update on performance of existing fund managers and there are no equalities issues arising**.**
4.4	**Environmental Implications** None applicable to this report.

5. Conclusion and reasons for recommendations

5.1 Members are asked to note the performance of the fund for the quarter ending December 2018 as part of the regular monitoring of fund performance. Members are also asked to note Appendix 2- LGPS News Issues

Background papers:

1. Quarterly management reports from the Fund Managers to the Pension Fund.

2. Quarterly performance monitoring statistics for the Pension Fund – BNY Mellon

Final report clearance:

Signed by:

	Corporate Director of Resources	Date
Received by:		
	Head of Democratic Services	Date

Report Author: Joana Marfoh
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London Borough of Islington

Report to 31st December 2018

MJ Hudson Allenbridge

FEBRUARY 2019

Table of Contents

Contacts

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Fund Manager Overview

Table 1 provides an overview of the external managers, in accordance with the Committee's terms of reference for monitoring managers.

TABLE 1:

MANAGER	LEAVERS, JOINERS AND DEPARTURE OF KEY INDIVIDUALS	PERFORMANCE	ASSETS UNDER MANAGE-MENT	CHANGE IN STRATEGY /RISK	MANAGER SPECIFIC CONCERNS
London CIV – Allianz (active global equities)	Monitored by London CIV. No changes reported.	Underperformed in the quarter to December 2018, by -0.20%. Outperformed by +0.25% p.a. over three years to end December 2018 but trailing the target of +2.0% p.a.	London CIV sub-fund dropped in value following exits by other member funds. As at end December the sub- fund's value was £106.4 million and was 100% owned by London Borough of Islington.		
London CIV – Newton (active global equities)	Monitored by London CIV. No changes reported.	Outperformed the index by +1.08% in the quarter. Behind the benchmark over three years by -2.12% p.a. but outperforming over the past year by +3.69%.	As at end December the sub- fund's value was £557.3 million. London Borough of Islington owns 36.2% of the sub-fund.		
BMO/LGM (emerging and frontier equities)	Jeff Chowdhry, Director of Emerging Markets Equities, retired in October 2018.	Outperformed the benchmark by +3.42% in the quarter to December 2018. Ahead over one year by +2.46%.	Not reported.		

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MANAGER	LEAVERS, JOINERS AND DEPARTURE OF KEY INDIVIDUALS	PERFORMANCE	ASSETS UNDER MANAGE-MENT	CHANGE IN STRATEGY /RISK	MANAGER SPECIFIC CONCERNS
Standard Life (corporate bonds)	19 joiners, but 42 leavers (including seven from fixed income).	Underperformed the benchmark by -0.20% in Q4 2018. Over three years the fund is 0.55% p.a. ahead of the benchmark return net of fees, but behind the performance target of +0.8% ahead p.a.	Fund value fell to £2,874 million in Q4 2018, a fall of £70 million. London Borough of Islington's holding stood at 6.9% of the fund's value.		
Aviva (UK property)	24 new joiners and 9 leavers across the firm, but no changes to the Lime Fund team.	Underperformed the gilt benchmark by -1.35% for the quarter to December 2018 but outperforming by +0.33% p.a. over three years, net of fees.	Fund was valued at £2.20 billion as at end Q4 2018. London Borough of Islington owns 5.2% of the fund.		
Columbia Threadneedle (UK property)	Four joiners and five leavers in Q4 2018, but no changes to the team managing the Islington portfolio.	Outperformed the benchmark return by +0.25% in Q4 2018 and by +0.13% p.a. over three years. Trailing the target of 1% p.a. outperformance.	Pooled fund has assets of £2.05 billion. London Borough of Islington owns 4.3% of the fund.		
Legal and General (passive equities)	Mark Zinkula announced that he will retire as CEO of LGIM in August 2019.	Funds are tracking as expected.	Assets under management of £985 billion at end June 2018.		

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MANAGER	LEAVERS, JOINERS AND DEPARTURE OF KEY INDIVIDUALS	PERFORMANCE	ASSETS UNDER MANAGE-MENT	CHANGE IN STRATEGY /RISK	MANAGER SPECIFIC CONCERNS
Franklin Templeton (global property)	Two joiners and two leavers in Q4 2018.	Portfolio return over three years was +17.39% p.a., well ahead of the target of 10% p.a.	$717 billion of assets under management as at end September 2018.		
Hearthstone (UK residential property)	One leaver in Q4 2018.	Underperformed the IPD UK All Property Index by -0.59% in Q4. Trailing the IPD benchmark over three years by -3.69% p.a. to end December 2018.	Fund was valued at £56.1m at end Q4 2018. London Borough of Islington owns 50.6% of the fund.		New investor money into the fund is proceeding at a slower pace than expected which reduces crossing opportunities.
Schroders (multi-asset diversified growth)	No changes to the DGF team.	Fund returned -5.35% during the quarter and +3.22 p.a. over 3 years, -4.89% behind the target return.	Total AUM stood at £392.3 billion as at end September 2018.	The volatility of the fund is lower than expected at present.	

Source: MJ Hudson Allenbridge

Minor Concern

Major Concern

Individual Manager Reviews

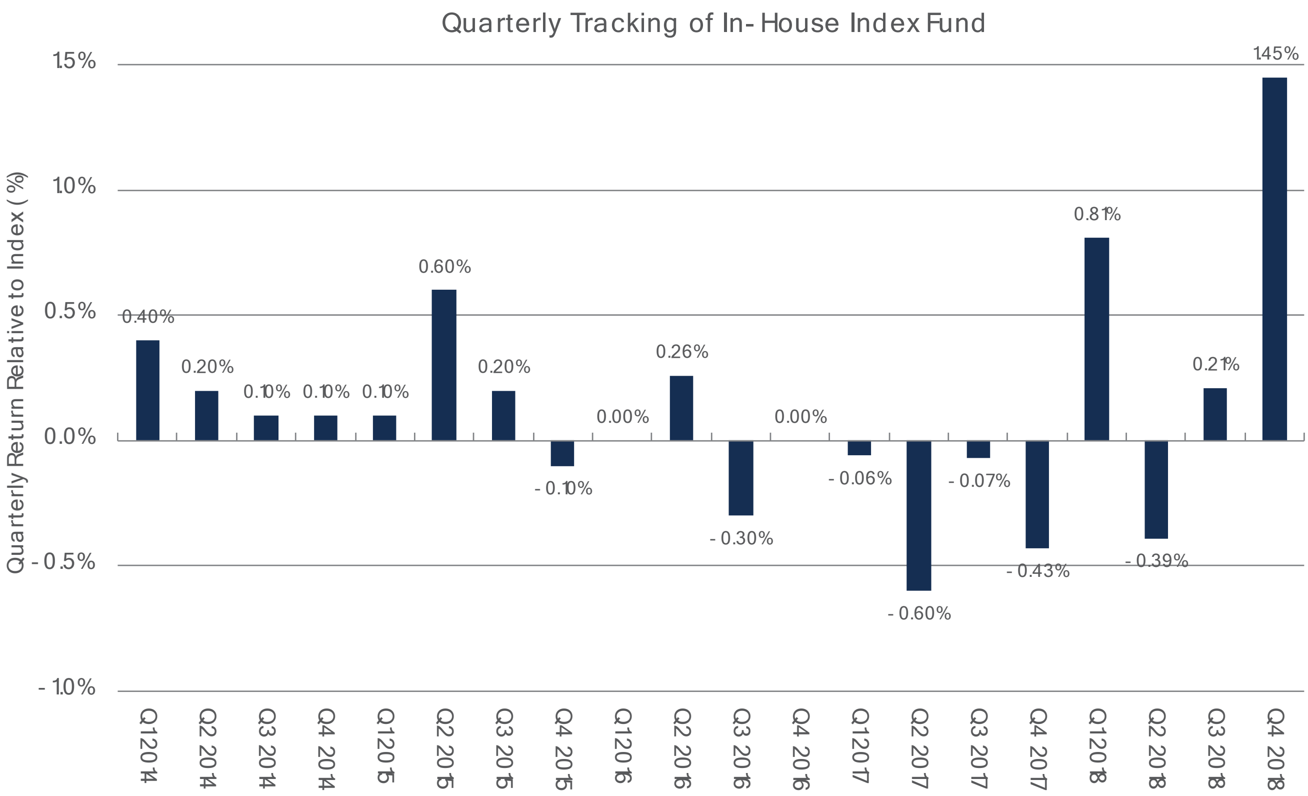
In-house – Passive UK Equities – FTSE UK Low Carbon Optimisation Index

Headline Comments: The portfolio continues to meet its objectives. The fund was ahead of the index benchmark return this quarter and over three years has outperformed the benchmark and delivered a return of +6.54% p.a.

Mandate Summary: A UK equity index fund designed to match the total return on the UK FTSE All-Share Index. In Q3 2017, the fund switched to tracking the FTSE UK Low Carbon Optimisation Index. This Index aims to deliver returns close to the FTSE All-Share Index, over time. The in-house manager uses Barra software to create a sampled portfolio whose risk/return characteristics match those of the low carbon index.

Performance Attribution: Chart 1 shows the quarterly tracking error of the in-house index fund against the FTSE All-Share Index over the last five years. There are no performance issues. Over three years, the portfolio outperformed its three-year benchmark by +0.41%% p.a.

CHART 1:



Source: MJH Allenbridge; BNY Mellon

Portfolio risk: In Q3 2017, the index fund transitioned into a low carbon passive portfolio. As at quarter end, the portfolio had a tracking error of 0.37% against the FTSE UK Low Carbon Optimisation Index.

London CIV – Allianz – Global Equity Alpha Fund

Headline Comments: It was another disappointing quarter for the London CIV – Allianz sub-fund as it underperformed the benchmark in the quarter to December 2018 by -0.2%, amid a wider market fall. Over three years the fund is outperforming the benchmark by +0.25% p.a. but it is disappointing to see it continuing to fall further behind the performance target of +2.0% p.a. over benchmark.

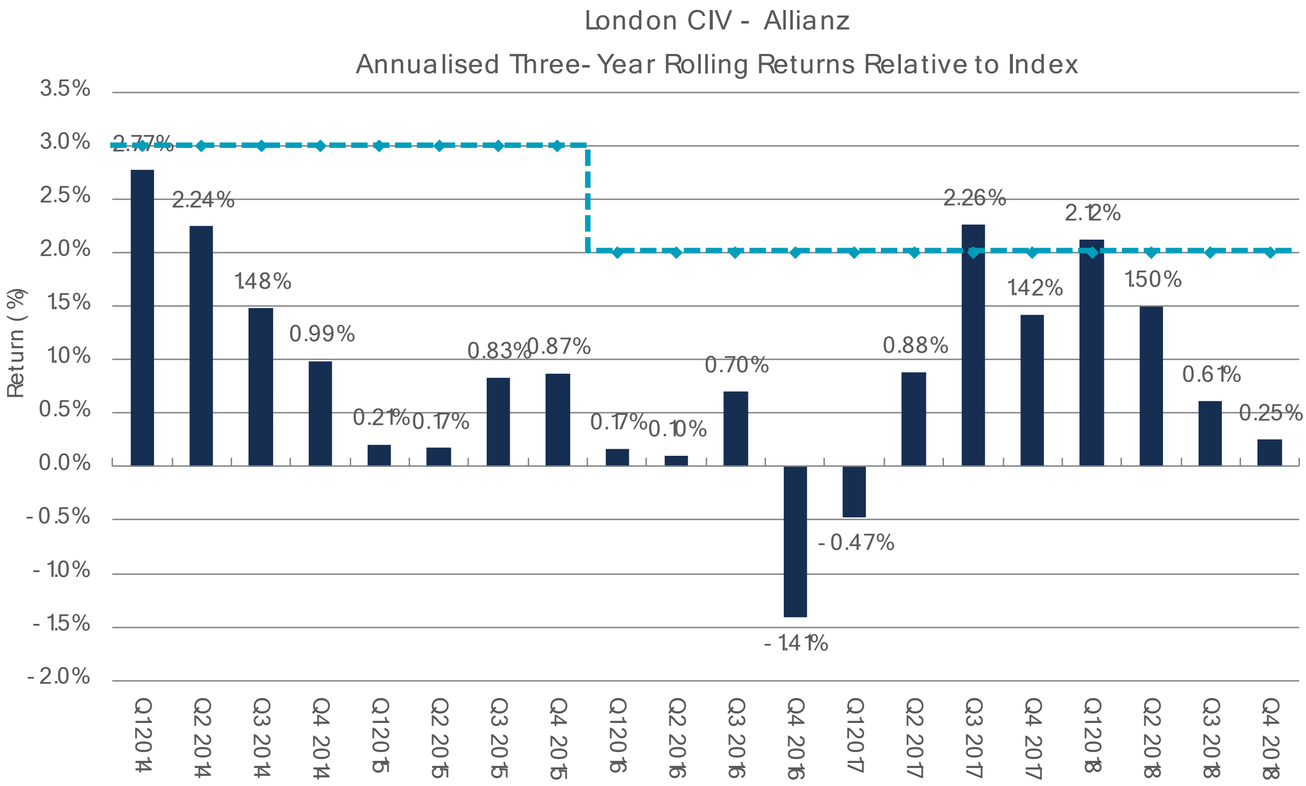
Mandate Summary: An active global equity portfolio, with a bottom-up global stock selection approach. A team of research analysts identifies undervalued stocks in each geographical region (Europe, US, Asia Pacific). A global portfolio team is responsible for constructing the final portfolio. The objective of the fund (since Q4 2015) is to outperform the MSCI World Index by +2.0% p.a. over rolling three-year periods net of fees.

Performance Attribution: For the three years to December 2018, the Allianz portfolio was ahead of the benchmark, but trailing the performance target of +2.0% p.a., shown by the dotted line in Chart 2. Note that the dotted line drops in Q4 2015 when the mandate transferred to the London CIV sub-fund, which has a lower performance objective than when Allianz ran a bespoke mandate for London Borough of Islington.

The portfolio's underperformance, for the quarter to end December 2018, was attributed by the London CIV to poor sector allocation rather than poor stock selection. The market volatility in December saw investors switch to defensive sectors in which the fund is typically underweight due to its long-term growth focus. Holdings in Fresenius SE & Co and Wabtec were the biggest detractors from performance (detracting -0.33% and -0.31% respectively).

The largest contributors to returns came from holdings in Roche (+0.04%), and the Japanese yen (+0.04%). Not allocating to Amazon, Apple or NVidia provided some relative alpha versus the benchmark.

CHART 2:



Source: MJH Allenbridge; BNY Mellon

Portfolio Risk: there remains a concern that London Borough of Islington has become the sole investor in the fund. Cost effective options for transitioning assets to the new manager (LCIV – RBC) are now being explored, although there have been some issues around outstanding withholding tax credits which are still being discussed with the London CIV.

The active risk on the portfolio as at end December was +1.45% and the beta was 1.03 (if the market rises 10%, the fund is expected to rise 10.3%).

Portfolio Characteristics: as at end Q4 2018, the portfolio held 50 stocks (no change from last quarter).

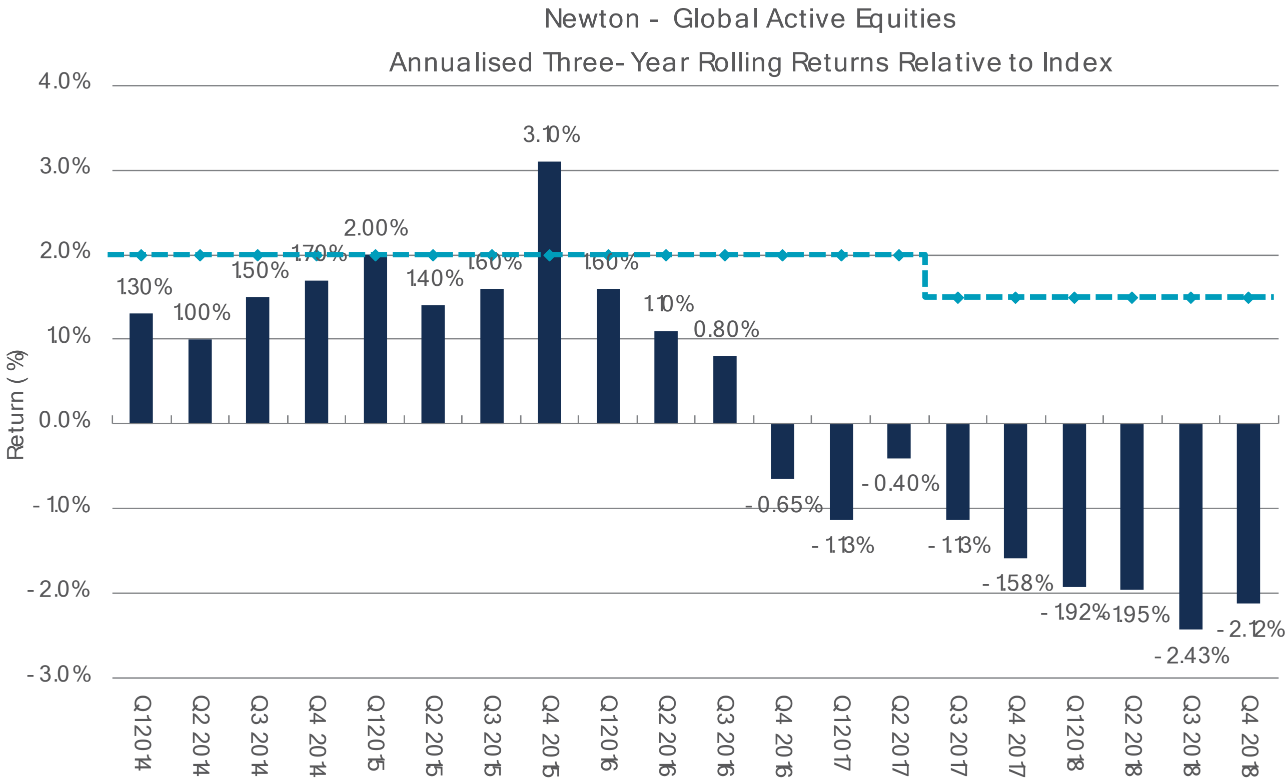
London CIV – Newton – Global Active Equities

Headline Comments: The London CIV – Newton sub-fund outperformed its benchmark during Q4 2018 by +1.08%. Over three years the portfolio has underperformed the benchmark target of +2.0% p.a., however, and remains well below the performance that could be achieved with a passive mandate.

Mandate Summary: An active global equity portfolio. Newton operates a thematic approach based on 12 key themes that impact the economy and industry. Some are broad themes that apply over the longer term; others are cyclical. Stock selection is based on the industry analysts' thematic recommendations. The objective of the fund since 22nd May 2017 is to outperform the FTSE All-World Index by +1.5% p.a. over rolling three-year periods, net of fees.

Performance Attribution: Chart 3 shows the three-year rolling returns of the portfolio relative to the benchmark (the navy bars) and compares this with the performance target, shown by the blue dotted line.

CHART 3:



Source: MJH Allenbridge; BNY Mellon

For the three-year period to the end of Q4 2018, the fund has trailed the benchmark by -2.12% p.a. This means it is trailing the performance objective by -3.62% (the performance objective is shown by the dotted line and dropped in May 2017 when the assets transferred into the London CIV sub-fund).

London CIV attributed the outperformance in the quarter to December 2018 to positive stock selection in consumer staples and utilities. Geographically, the portfolio outperformed in every region, except for the UK, where Brexit uncertainty continues to weigh on returns.

Positive contributions to the total return came from holdings such as Merck & Co (+0.11%) and Suntory Beverage & Food (+0.10%). UK equities were a drag on performance, with Associated British Foods being the biggest detractor (-0.32%) from the fund's quarterly return of -9.49%.

The continued underperformance of this manager over a three-year period remains a concern although it is worth noting that the one-year performance is positive, with a fund return of +0.42% vs the Index return of -3.27%, an outperformance of +3.69%.

Portfolio Risk: the active risk on the portfolio stood at 1.29% as at quarter end. The beta on the portfolio was 0.93 (if the market increases by +10% the portfolio can be expected to rise +9.3%).

At the end of Q4 2018, the London CIV sub-fund's assets under management were £557.3 million, compared with £616.4 million last quarter. London Borough of Islington now owns 36.2% of the sub-fund.

Portfolio Characteristics: The number of stocks in the portfolio stood at 58 as at quarter-end (no change from last quarter). Two positions were added (Verizon and Ecolab) and two were removed (RBS and CA).

Staff Turnover: The London CIV did not report any staff changes during the quarter.

BMO/LGM – Emerging Market Equities

Headline Comments: The total portfolio delivered a return of –1.77% in Q4 2018, compared with the benchmark return of -5.19%, an outperformance of +3.42%. The emerging market component of this portfolio returned -3.09% (source: BMO) compared with the index return of -7.47%. The frontier markets portfolio was also behind the index return of -4.73%, delivering a negative absolute return of -9.33% (source: BMO). Over one year, the total fund is ahead of the benchmark return by +2.46%.

Mandate Summary: the manager invests in a selection of emerging market and frontier market equities, with a quality and value, absolute return approach. The aim is to outperform a combined benchmark of 85% MSCI Emerging Markets Index and 15% MSCI Frontier Markets Index by at least 3% p.a. over a three-to-five-year cycle.

Performance Attribution: during the quarter, the largest positive contributors to performance for the emerging markets portfolio came from Bank Mandiri Persero (+0.9%), which is the largest holding in the portfolio at 5%. ICICI Bank (+0.8%) and British American Tobacco Malaysia (+0.5%) also contributed positively to the total return. Companies which detracted most from performance included Tingyi (-0.9%), Walmart De Mexico (-0.8%) and Universal Robina (-0.5%).

In the frontier market portfolio, positive contributors included Evertec (+0.7%) and British American Tobacco Kenya (+0.3%). Companies which detracted from performance included Delta Corporation (-1.9%), United Bank (-1.1%) and Sonatel (-1.1%).

Portfolio Risk: Within the emerging markets portfolio, 6.2% was allocated to developed or frontier markets, and cash stood at 4.3% as at quarter-end. Turnover for the previous 12 months was 28.8%. The largest overweight country allocation in the emerging markets portfolio remained India (+8.6% overweight). The most underweight country allocation remained South Korea (-13.8%).

Within the frontier markets portfolio, it is worth noting that 64% of the portfolio was invested in countries that are not in the benchmark index, including Egypt, Costa Rica, Peru and Pakistan. The most overweight country allocation remained Egypt (+11.0%) and the most underweight was Argentina (-15.6%).

Portfolio Characteristics: The frontier markets portfolio held 39 stocks as at end December compared with the benchmark which had 113. The emerging markets portfolio held 35 stocks as at end December compared with the benchmark which had 1,125.

Organisation: Jeff Chowdhry, former co-manager of the of the emerging markets fund, retired in October 2018. The fund is now managed by the other co-manager, Sam Mahtani, along with Rishikesh Patel and Gokce Bulut. Two new analysts have been also hired for January 2109.

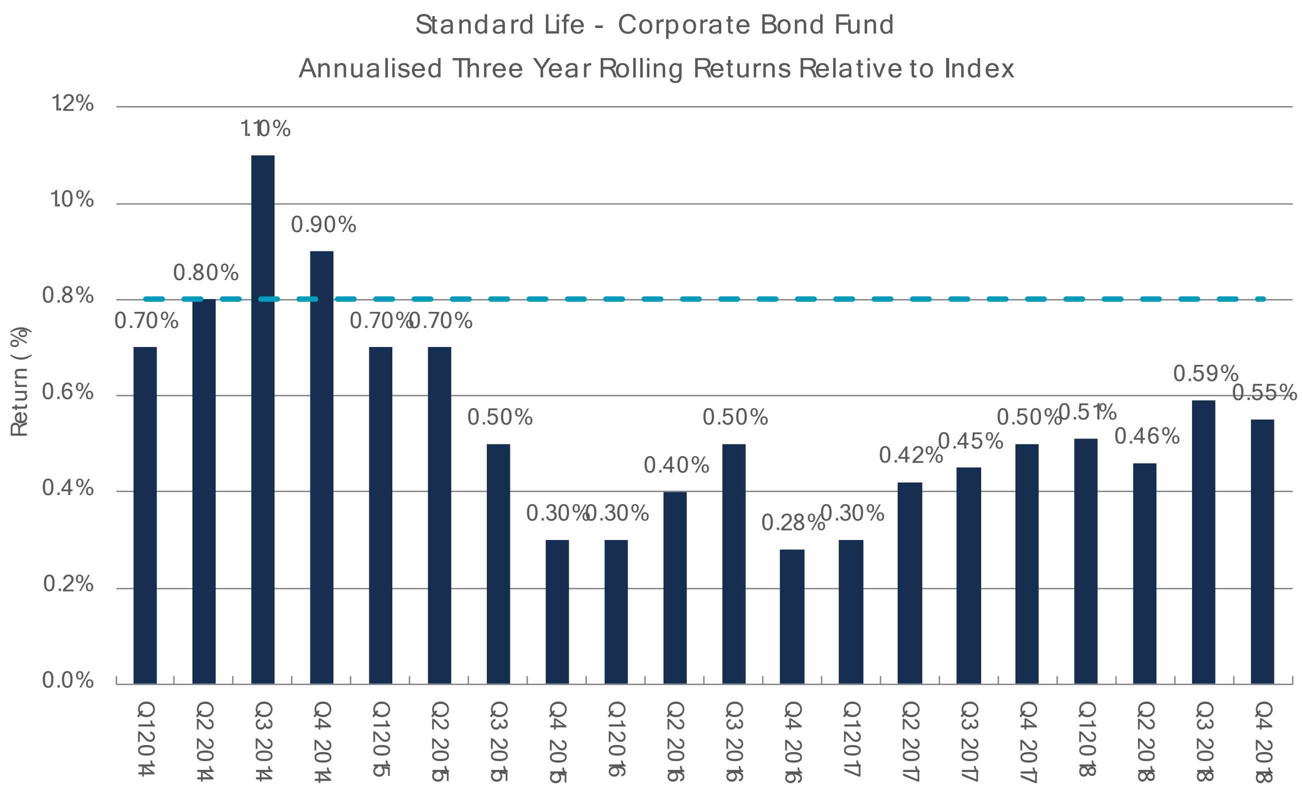
Standard Life – Corporate Bond Fund

Headline Comments: The portfolio was behind the benchmark return during the quarter. Over three years, the fund was ahead of the benchmark return but behind the performance target of +0.8% p.a.

Mandate Summary: The objective of the fund is to outperform the iBoxx Sterling Non-Gilt Index by +0.8% p.a. over rolling three-year periods.

Performance Attribution: Chart 4 shows the three-year performance of the Corporate Bond Fund compared to the Index, over the past five years. This shows the fund is ahead of the benchmark over three years but trailing the performance objective (shown by the dotted line in Chart 4).

CHART 4:



Source: MJH Allenbridge; BNY Mellon

Over three years, the portfolio has returned +4.88% p.a. compared to the benchmark return of +4.33% p.a. Over the past three years, stock selection has added 0.38% value, followed by asset allocation (+0.11%) and curve plays (+0.10%).

Portfolio Risk: The largest holding in the portfolio at quarter-end remained EIB 5.625% 2032 at 1.6% of the portfolio. The largest overweight sector position remained Financials (+5.4%) and the largest underweight position remained sovereigns and sub-sovereigns (-13.7%). Contribution from asset allocation was negative this quarter.

The fund holds 3.4% of the portfolio in non-investment grade (off-benchmark/BB and below) bonds.

Portfolio Characteristics: The value of Standard Life's total pooled fund at end December 2018 stood at £2,874 million, £70.0 million lower than at the end of Q3 2018. London Borough of Islington's holding of £197.6 million stood at 6.9% of the total fund value (compared to 6.7% last quarter).

Staff Turnover: there were 19 joiners, but there were 42 people who left the firm, reflecting the ongoing rationalisation of the merged Aberdeen and Standard Life teams. Of the 42 leavers, seven were from the fixed income team, including three analysts, a manager, an investment director, a manager and an

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assistant portfolio manager. There were no changes to the team managing the London Borough of Islington fund.

Aviva Investors – Property – Lime Property Fund

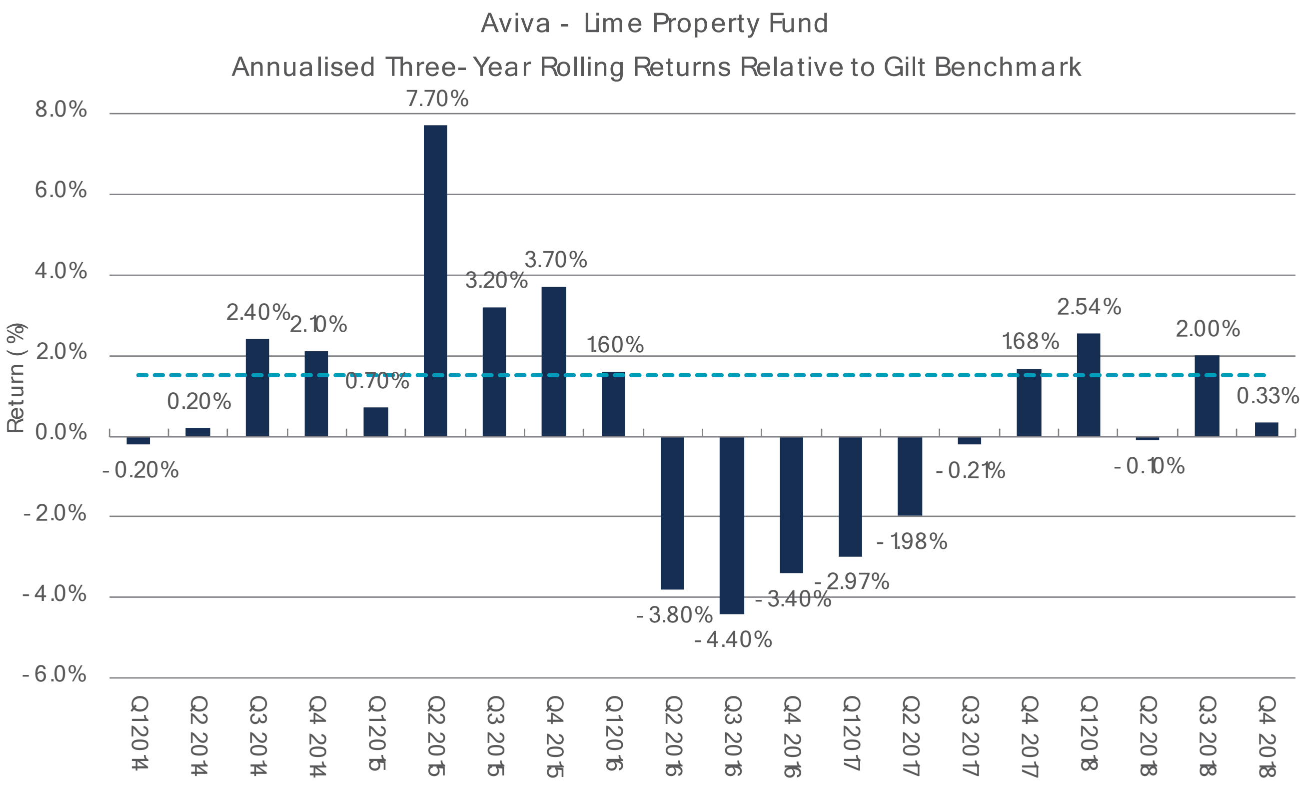
Headline Comments: The Lime Fund delivered another quarter of steady returns though behind the benchmark return. Over three years, the fund is ahead of the gilt benchmark return.

Mandate Summary: An actively managed UK pooled property portfolio, the Lime Fund invests in a range of property assets including healthcare, education, libraries, offices and retail. The objective of the fund is to outperform a UK gilt benchmark, constructed of an equally weighted combination of the FTSE 5-15 Years Gilt Index and the FTSE 15 Years+ Gilt Index, by +1.5% p.a., over three-year rolling periods.

Performance Attribution: The fund's Q4 2018 return was attributed by Aviva to 0.48% capital return and 1.10% income return.

Over three years, the fund has returned +5.66% p.a. ahead of the gilt benchmark of +5.33% p.a. The portfolio is behind its outperformance target of +1.5% p.a., as can be seen in Chart 5.

CHART 5:



Source: MJH Allenbridge; BNY Mellon

Over three years, 60% of the return came from income and 40% from capital gain.

Portfolio Risk: The manager sold another HSBC branch in Kingston in Q4 (following on from one in Norwich in Q3) as part of wider exit strategy from the HSBC portfolio, citing an unfavourable outlook for the investment thesis around this decision. The sale was at a 20% premium above valuation aiding to asset return for the year.

The fund completed purchases of student accommodation in Blackpool and Lincoln, along with a medical centre in Bradford.

The average unexpired lease term was 19.2 years as at end December 2018. 12.1% of the portfolio's lease exposure in properties is in 30-35 year leases, the largest sector exposure remains offices at 28.4%, and the number of assets in the portfolio is now 80 at the end of December. The weighted average unsecured credit rating of the Lime Fund remained A-.

Portfolio Characteristics: As at end December 2018, the Lime Fund was valued at £2.201 billion, an increase of £61.84 million from the previous quarter end. London Borough of Islington's investment represents 5.2% of the total fund. The Fund had 67.6% allocated to inflation-linked rental uplifts as at end December 2018.

Staff Turnover/Organisation: There were 24 new joiners and 9 leavers across the firm during Q4. There were no changes to the Lime Property Fund portfolio management team.

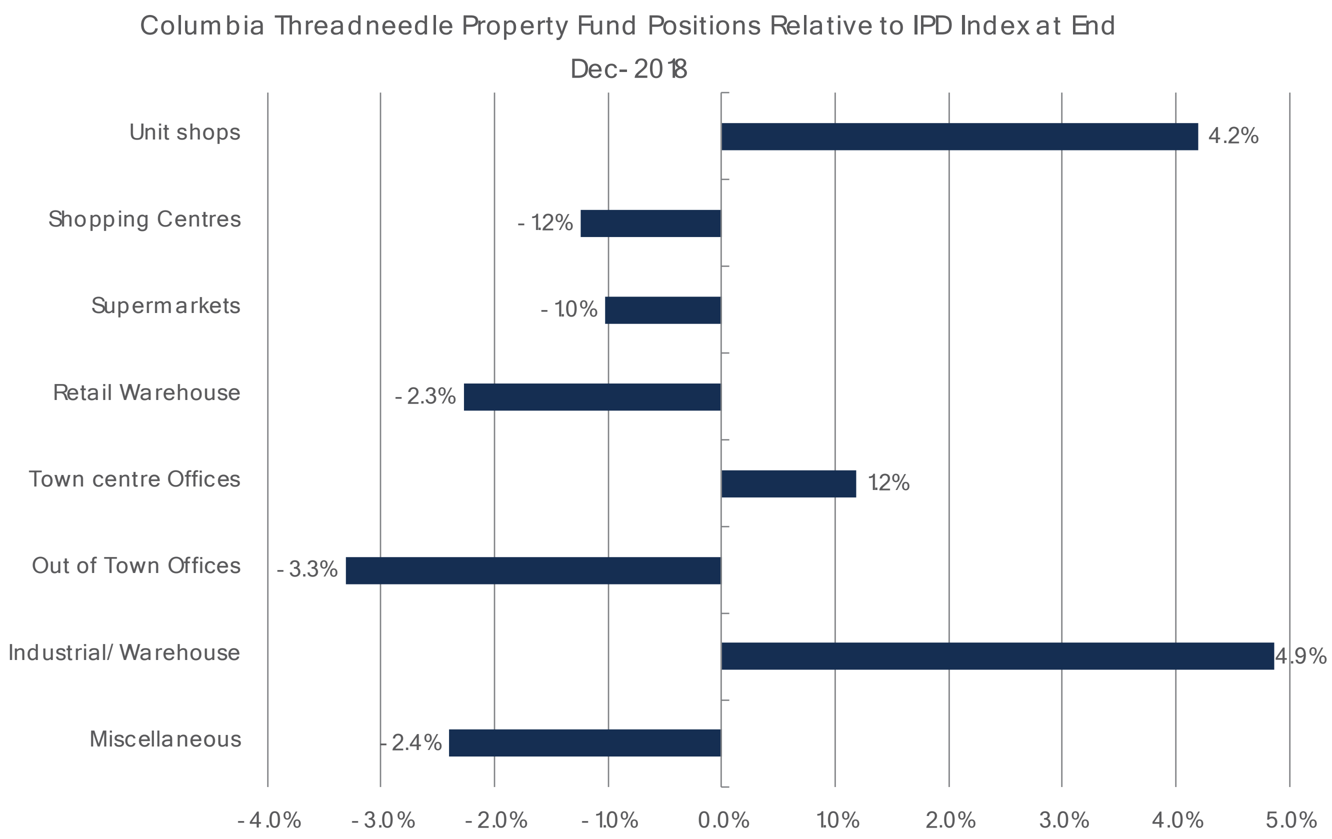
Columbia Threadneedle – Pooled Property Fund

Headline Comments: The fund was ahead of the benchmark return in Q4 2018. Over three years, the Fund has outperformed the benchmark, although this is behind the performance target of 1.0% p.a. above benchmark.

Mandate Summary: An actively managed UK commercial property portfolio, the Columbia Threadneedle Pooled Property Fund invests in a diversified, multi-sector portfolio of UK property assets. Its performance objective is to outperform the AREF/IPD All Balanced – Weighted Average (PPFI) Index by at least 1.0% p.a., net of fees, on a rolling three-year basis.

Portfolio Risk: Chart 6 shows the relative positioning of the fund compared with the benchmark.

CHART 6:



Source: MJH Allenbridge; Columbia Threadneedle

The overweight allocation to unit shops is skewed because IPD (against which the portfolio is measured) classifies two of the largest properties in Columbia Threadneedle's portfolio as retail. These are the Heals building and the South Molton Street property. In fact, based on square footage, these assets are significantly more office than retail.

During the quarter, the fund completed three transactions worth £48.8 million in two industrial estates and one leisure asset (golf driving range) within the Greater London area. The fund also sold an industrial park in Deeside, Wales and a shop in Coleraine, Northern Ireland.

The fund has a slightly higher than benchmark void rate at 10% versus 7.5% but voids have been increasing over the market, generally. The fund has also had a higher cash balance than many peers, and this is creating a drag on performance, but the portfolio does yield 1% more (5.9% versus 4.9%) than the index.

Performance Attribution: The portfolio outperformed the benchmark by +0.25% in Q4 2018, delivering a return of +1.14%. The manager continued to note wide deviation in performance between different sectors. The retail sector, for example, delivered a return of -1.9% in Q4, compared with the industrial sector which returned +3.4%, and the office sector which returned 1.8%.

Over three years, the fund is ahead of its benchmark by +0.13% p.a., with a return of +6.56% p.a., but it is still trailing the performance target of +1.0% p.a.

Portfolio Characteristics: As at 31st December 2018, the fund was valued at £2.051 billion, an increase of £59 million compared with June 2018. London Borough of Islington's investment represented 4.31% of the fund.

The manager is continuing to look to buy smaller units in urban locations where supply is restricted. He is also looking to move the portfolio away from industrial properties in London to other locations.

Staff Turnover: There were four joiners and five leavers across the firm in Q4 2018. No one directly involved with the London Borough of Islington portfolio was in this list. Just after the quarter end, LGIM announced that Michelle Scrimgeour, CEO of Europe, Middle East and Africa (EMEA) for Columbia Threadneedle would be joining LGIM as their new CEO later in the year.

Legal and General Investment Management (LGIM) – Overseas Equity Index Funds

Headline Comments: The two passive index funds were within the expected tracking range when compared with their respective benchmarks. Both index funds marginally underperformed their benchmark indices.

Mandate Summary: Following a change in mandate in June 2017, the London Borough of Islington now invests in two of LGIM's index funds: one is designed to match the total return on the FTSE-RAFI Emerging Markets Equity Index; the second is designed to match the total return on the MSCI World Low Carbon Target Index. The MSCI World Low Carbon Target is based on capitalisation weights but tilting away from companies with a high carbon footprint. The FTSE-RAFI Index is based on fundamental factors.

Performance Attribution: The two index funds both tracked their benchmarks as expected, as shown in Table 2.

TABLE 2:

	Q4 2018 FUND	Q4 2018 INDEX	TRACKING
FTSE-RAFI Emerging Markets	+2.85%	+2.77%	-0.05%
MSCI World Low Carbon Target	-11.25%	-11.23%	-0.02%

Source: LGIM

Portfolio Risk: The tracking errors are all within expected ranges. The allocation of the portfolio, as at quarter end, was 79.4% to the MSCI World Low Carbon Target index fund, and 20.6% allocated to the FTSE RAFI Emerging Markets index fund.

Staff Turnover/Organisation: LGIM's CEO, Mark Zinkula announced that he will retire from LGIM in August 2019. After the quarter end, LGIM announced that Michelle Scrimgeour has been appointed as his replacement. She was previously the chief executive officer for EMEA at Columbia Threadneedle.

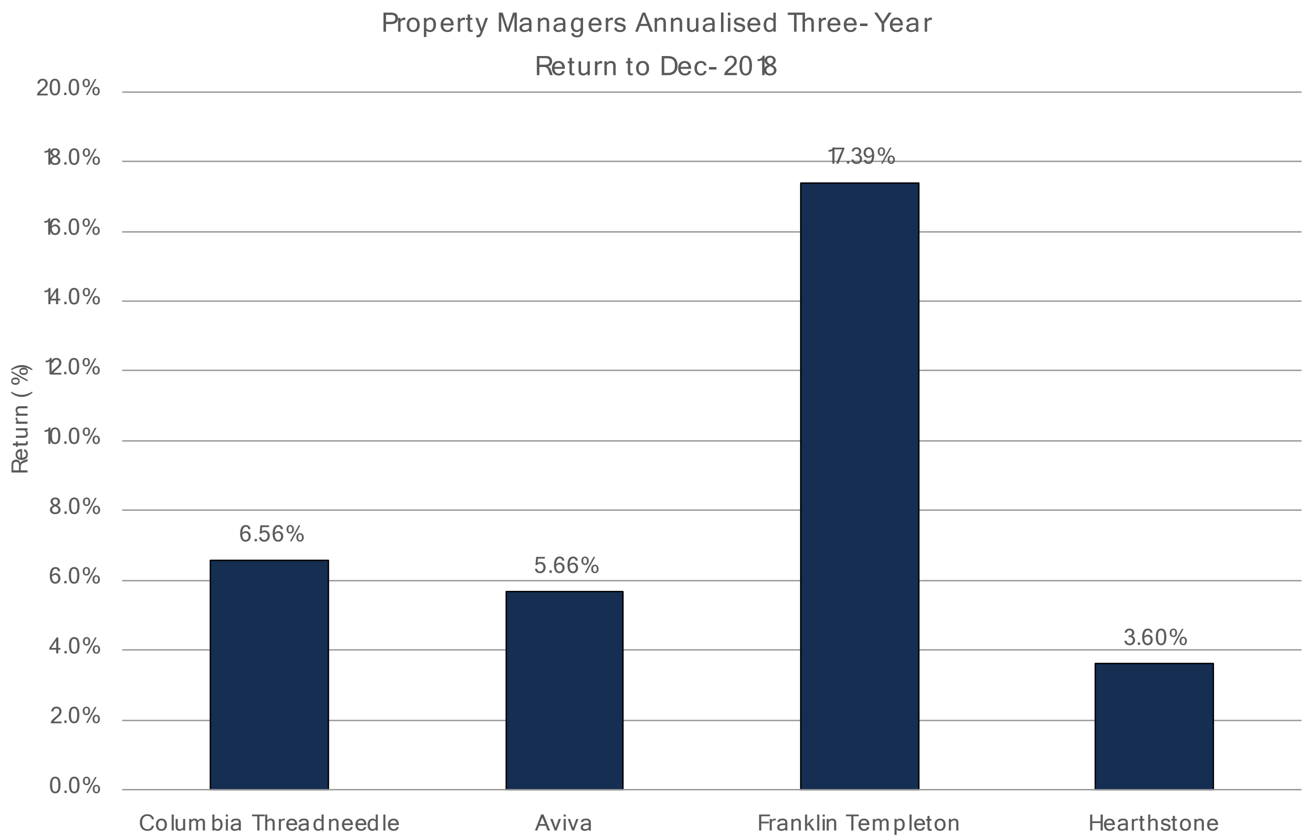
Franklin Templeton – Global Property Fund

Headline Comments: This is a long-term investment and as such a longer-term assessment of performance is recommended. There are two funds in which London Borough of Islington invests. The portfolio in aggregate outperformed the absolute return benchmark of 10% p.a. over three years.

Mandate Summary: Two global private real estate fund of funds investing in sub-funds. The performance objective is an absolute return benchmark over the long term of 10% p.a.

Performance Attribution: Over the three years to December 2018, Franklin Templeton continues to be the best performing fund across all four property managers. Chart 7 compares their annualised three-year performance, net of fees.

CHART 7:



Source: MJH Allenbridge; Columbia Threadneedle

Staff Turnover/Organisation: There were two joiners and two leavers for the real assets team in the quarter. One joined as director of operations in Europe and one as a North American portfolio manager. One left from the Asia investment team and one from the global analytics teams.

Hearthstone – UK Residential Property Fund

Headline Comments: The portfolio underperformed the benchmark for the quarter ending December 2018 and over three years.

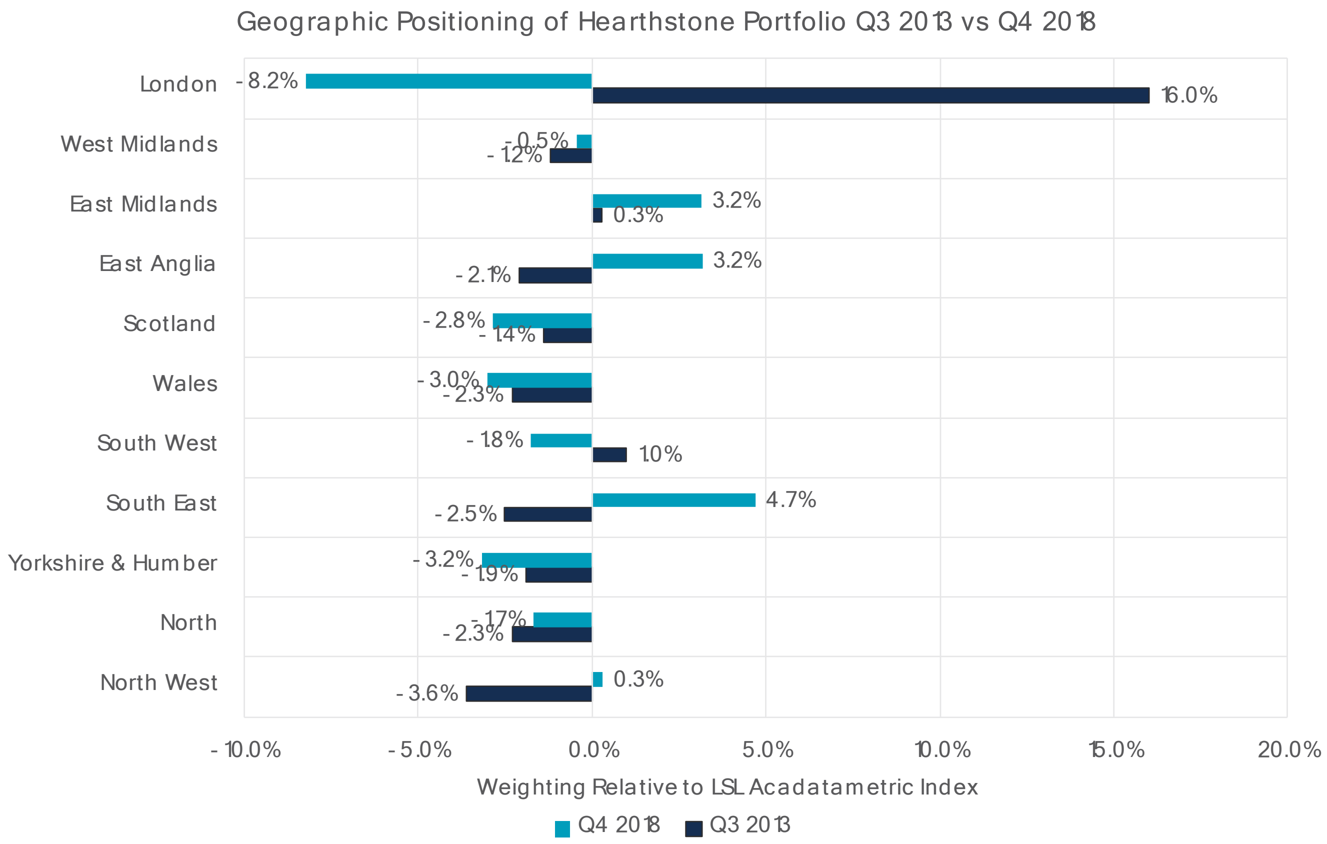
Mandate Summary: The fund invests in private rented sector housing across the UK and aims to outperform the LSL Acadametrics House Price Index (note that this excludes income), as well as providing an additional income return. The benchmark used by BNY Mellon is the IPD UK All Property Monthly Index.

Performance Attribution: The fund underperformed its benchmark over the three years to December 2018 by -2.69% p.a., returning +3.60% p.a. versus the index return of 7.45% p.a. The gross yield on the portfolio as at December 2018 was 4.81%. Adjusting for voids, however, the yield on the portfolio falls to 4.59%.

Portfolio Risk: The cash and liquid instruments on the fund stood at 9.76%.

It remains Hearthstone's long-term intention to run the portfolio on a region-neutral basis. However, they do not wish to be overweight in central London at the present time and are also looking to decrease their overweight allocation to the South East. Chart 8 compares the regional bets in the portfolio in Q4 2018 (turquoise bars) with the regional bets at the start of the mandate, in Q3 2013 (navy bars).

CHART 8:



Source: MJH Allenbridge; Hearthstone

In terms of potential crossing with London Borough of Islington, as they attract new investors, Hearthstone have admitted that they have found this to be a very slow process. They estimate that 90% of new money, that has been set aside to invest in residential property, is not being allocated at this time. The reason for this is uncertainty around Brexit and the potential impact on the housing sector in the UK.

Hearthstone are fully cognisant that their fund might not now be an ideal fit for London Borough of Islington and continue to believe that crossing opportunities may arise in the future, but the slow and steady growth means this has not really been seen to date. If London Borough of Islington wished to liquidate a significant number of units, they would need to swing the price to take account of the costs of selling properties. (The net asset value of a fund is valued at the mid-market prices of the underlying securities which make up the fund's assets. Under a swing price regime, such as that used by Hearthstone, when the fund experiences net redemptions or net subscriptions the price may swing down or up to negate the impact of the expected transaction costs associated with those net flows.) Hearthstone have indicated that they would be prepared to offer in-specie transfers, as an alternative.

Portfolio Characteristics: By value, the fund has a 12% allocation to detached houses, 44% allocated to flats, 24% in terraced accommodation and 21% in semi-detached.

As at end December there were 204 properties in the portfolio and the fund stood at £56.1 million. London Borough of Islington's investment now represents 50.6% of the fund. This compares with 72% at the start of this mandate in 2013.

There have been no changes to the investment process since London Borough of Islington invested. Hearthstone continue to focus on mainstream homes with regional diversification, although they currently have no allocation to prime locations such as central London. A point to note is that Hearthstone does not invest in social housing, or affordable housing, and they have no plans to do this.

In terms of measuring and monitoring the environmental impact of their properties, Hearthstone currently only collects data about the property and not the occupant. They hope to change this going forward so that they can submit ratings to the GRESB survey (GRESB assess the sustainability performance of real estate portfolios). However, at a property level, Hearthstone report that 98% are above average rated on ESG criteria, with the remaining 2% rated "average".

Organisation and Staff Turnover: During the quarter, one investment manager left the team due to current low levels of acquisitions by the fund.

Schroders – Diversified Growth Fund (DGF)

Headline Comments: The DGF delivered a negative return in Q4 2018. Over three years, the fund is behind the target return of RPI plus 5% p.a.

Mandate Summary: The fund invests in a broad mix of growth assets and uses dynamic asset allocation over the full market cycle, with underlying investments in active, passive and external investment, as appropriate. Schroders aim to outperform RPI plus 5% p.a. over a full market cycle, with two-thirds the volatility of equities.

Performance Attribution: The DGF delivered a return of -5.35% in Q4 2018. This is -7.08% behind the RPI plus 5% p.a. target return of +1.73% for Q4. Over three years, the DGF delivered a return of +3.22% p.a. compared with the target return of +8.11% p.a., behind the target by –4.89% p.a. This represents a substantial underperformance, although many DGFs faced similar experiences in Q4 2018 yet are now reporting much improved performance in 2019.

In Q4 2018, equity positions detracted -5.8%, alternatives added +0.2%, credit and government debt was negative at -0.1%, and cash and currency added +0.2% (figures are gross of fees).

The return on global equities was +5.3% for the three years to December 2018 compared with the portfolio return of +3.22% (a 60% capture of the equity return, somewhat lower than expected). Over a full 3-5 year market cycle the portfolio is expected to deliver equity-like returns.

Portfolio Risk: The portfolio is expected to exhibit two-thirds the volatility of equities over a full three to five-year market cycle. Over the past three years, the volatility of the fund was 4.6% compared to the three-year volatility of 9.7% in global equities (i.e. 47% of the volatility) so is less risky than expected.

Portfolio Characteristics: The fund had 27% in internally managed funds (up from last quarter's 24% allocation), 39% in internal bespoke solutions (down from 41% last quarter), 3% in externally managed funds (down from 5%), and 30% in passive funds no change from last quarter's allocation) with a residual balance in cash, as at end December 2018. In terms of asset class exposure, 36.9% was in equities, 28.3% was in alternatives and 32.9% in credit and government debt, with the balance in cash.

Alternative assets include absolute return funds, property, insurance-linked securities, commodities and private equity.

Organisation: During the quarter, there were no changes to the team responsible for the DGF.

Karen Shackleton
Senior Adviser, MJ Hudson Allenbridge
25th February 2019

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LGPS CURRENT ISSUES

NEWS IN BRIEF

IN THIS ISSUE

NEW FAIR DEAL IN THE LGPS

On 10 January the MHCLG published its latest consultation on the "New" Fair Deal, concerning the introduction of greater pensions protection for employees of LGPS employers who are compulsorily transferred to service providers. The consultation closes on Thursday 4 April, and we will be responding in due course as well as setting out our views to clients so that they can frame their own responses.

This latest consultation is long overdue, with the government having issued its New Fair Deal guidance back in 2013 and the MHCLG having had an initial consultation in 2016. As well as covering Fair Deal, it also includes a proposed miscellaneous amendment which will affect some employers who seek to end their participation in the Fund on merger.

We will shortly provide a more detailed view on the implications and practicalities to assist Funds in responding to the consultation. In the meantime, if you have any queries in this area please contact us.

INDEXATION AND EQUALISATION OF GUARANTEED MINIMUM PENSIONS

The consultation discussed in our November issue on indexation and equalisation of GMP in public service pension schemes has concluded. The government has been implementing an "interim solution" on *indexation* between 6 April 2016 and 5 December 2018. The outcome of this consultation is that this solution will be extended for a further two years and four months. i.e. to extend the full indexation window to those reaching state pension age between 6 April 2016 and 5 April 2021. During this period, the government will investigate the possibility of an alternative long-term methodology, known as "conversion". The response paper to the consultation can be found here.

As reported in November, it has been mooted that this may potentially remove the need to consider a separate *equalisation* exercise, as any indexation solution may solve the bulk of the GMP equalisation issue at the same time. We will provide further details once this is known.

UPDATE FROM THE LGPS AVC CLUB – PRUDENTIAL AND EQUITABLE LIFE CHANGES

The AVC landscape continues to change and, during 2019 there will be significant changes at both Prudential and Equitable Life. Prudential will be writing to LGPS Funds shortly to communicate the withdrawal of most of their existing lifestyle strategies. At Equitable Life, all investments are to be transferred to Reliance Life later this year following closure of their With-Profits Fund, and the Equitable Life With-Profits Fund investments are expected to be enhanced by 60%-70%. Hence, from a governance perspective we would recommend that LGPS Funds affected by these changes consider the AVC arrangements they currently have in place and take regulated investment advice.

By participating in the LGPS AVC Club, Funds will be able to better understand the changing AVC landscape, monitor their own AVC arrangements and provide members with the best possible service in a cost-efficient way. Further details can be provided by your usual Mercer consultant.

LGPS COST CAP MECHANISM

On 21 December 2018 the LGPS Scheme Advisory Board (SAB) published its paper on cost management.

The LGPS in England and Wales has a separate cost management process which is completed prior to finalisation of the HMT public sector cost cap calculations.

Under this initial phase, the SAB are proposing an improvement to benefits equating to 0.5% of payroll, taking the cost back up to the long term target of 19.5% of payroll. The proposals are broadly as follows:

- Removal of Tier 3 ill Health
- A minimum lump sum death in service benefit of £75,000 per member (regardless of salary)
- Enhanced early retirement factors for all members who are active on 1st April 2019 in respect of their final salary-linked membership only
- Lower employee contributions for those with salaries at the lower end of the contribution band scale

The HMT cost cap process will be completed once the outcome of the above proposals and subsequent consultation is known.

However, on 30 January 2019 the Government published a written statement which announces a pause in the cost cap process for public service pension schemes pending the outcome of the application to appeal the McCloud case to the Supreme Court. A copy of the judgement can be found here: Judgment

The statement can be found here: Statement

Although the statement gives no timescales for the outcome of this case we understand it could be late 2019 or early 2020 before we know.

The LGPS Advisory Board (SAB) will now consider whether, given this announcement, it should withdraw the benefit change recommendations made to MHCLG as a result of its own cost cap process.

We understand that the LGPS could, if McCloud is upheld, be required to make changes to the underpin (potentially expanding this to cover more members). Such changes would need to be taken into account in a revised SAB cost cap result as this could potentially increase rates materially.

THE BRAND NEW S3 SERIES….MORTALITY TABLES

In December 2018, the CMI (Continuous Mortality Investigation) published a new series of mortality tables - the S3 series.

The S3 series is a set of mortality tables based on the mortality experience of large private ***and*** public sector defined benefit occupational pension schemes between 2009 and 2016. The S3 tables are expected to replace, over time, the S2 tables, which were based on occupational pension scheme experience between 2004 and 2011 (and which excluded data from public sector schemes).

The two sets of tables are not directly comparable because they are based on experience over different periods of time and different schemes. Hence, a straight switch from an S2 table to the corresponding S3 table would not be appropriate. However, if a such a switch was done, without any scheme-specific adjustments, then in general (and depending on the table being used) adopting the S3 tables would result in longer life expectancies and an increase in liabilities of around 1% to 3%. This largely reflects the fact that the pensioner life expectancy in public sector pension schemes is higher than in private sector schemes.

When setting mortality assumptions, standard tables often need to be adjusted, using scheme specific data, to reflect the expected mortality for the scheme. Changing from the S2 to the S3 tables will alter how a scheme's mortality assumption is expressed but, provided the current assumption is up to date, it should not affect estimates of period life expectancies (that is, the experience expected within that scheme at a given point in time). To ensure this, when adopting the S3 tables, consideration will be needed as to what adjustments are required to reflect scheme-specific characteristics and this will be carried out as part of our demographic analysis for the 2019 valuations.

PENSIONS DASHBOARD – A REALITY?

On 3 December 2018, the Department for Work and Pensions (DWP) published 'Pensions Dashboards – working together for the consumer', a feasibility report and consultation which invites views on a range of questions relating to the creation of pensions dashboards. The closing date for the consultation was 28 January 2019.

The DWP's favoured option is, initially, a single, non-commercial, Government sponsored dashboard hosted by the Single Financial Guidance Body (SFGB) and delivered (and largely paid for) by the pensions industry. The SFGB is replacing the Money Advice Service and Pension Wise services and the advice section of the Pensions Advisory Service.

The first dashboard is to include State Pension figures (initially by provision of a link to the www.gov.uk site, 'Check your State Pension'), and will include a Pension Finder Service, with compulsion for pension providers to supply data.

The SFGB will be responsible for delivering the initial Pensions Dashboard, leading a small Steering Group with representatives of the pensions industry, consumer bodies and Government. It is proposed that working groups and stakeholder advisory groups will be used to ensure the best and most up-to-date solutions can be accessed and that the development stays on course. Phased-in delivery is expected, starting in 2019, with Master Trusts and some DC schemes being first. Other arrangements are expected to follow over the next 3-4 years.

The Government is proposing that all ongoing costs (apart from changes to legislation and the provision of State Pension information) will be met by industry via a levy, although it has committed £5 million to help start the project. The consultation paper invites comments on who should pay the levy and how it should be calculated.

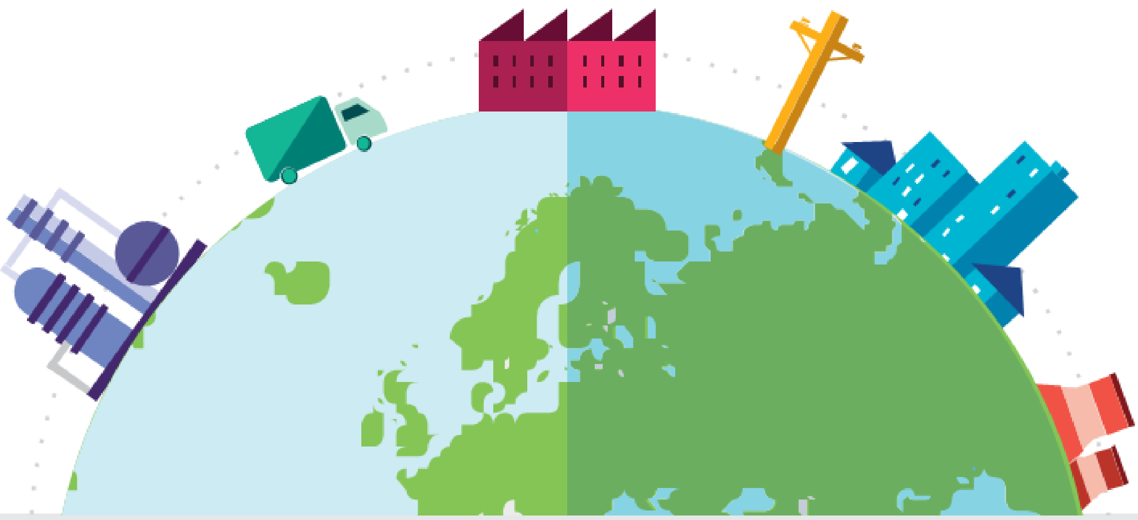
OTHER DEVELOPMENTS ON REGULATIONS AND CONSULTATIONS

TECHNICAL AMENDMENTS TO BENEFITS CONSULTATION

As mentioned in our November issue, the MHCLG issued a small consultation on a number of amendments to the provisions of the LGPS. The three main sections of the consultation were:

- Amendments to benefits payable to same-sex married or civil partners in order for them to receive the same benefits on survival as a widow
- Power to issue statutory guidance to the Secretary of State
- Early access to benefits for deferred members of 1995 Scheme

The consultation has now closed and in December, the MHCLG issued a response to the consultation, with most of the responses being positive. The original consultation and the response paper can be found here.



DATES TO REMEMBER

DATE	ISSUE	THE LATEST
2018/2019	Regulator powers	Consultation on changes to the Pensions Regulator's Funding Code of Practice and strengthening its scheme funding and anti-avoidance powers has now started.
1 January 2019	HMRC brief on VAT and treatment of pension fund management services provided by insurance companies.	Date by which, where an insurance company provides pension fund management and administration services, only the services for schemes classed as "special investment funds" will continue to be treated as VAT exempt.
1 January 2019	Plan Amendment, Curtailment or Settlement (IAS19)	Date after which if a plan amendment, curtailment or settlement occurs, a full remeasurement is mandatory under IAS19.
13 January 2019	IORP II	Date by which member states must adopt the new EU directive covering occupational pensions.
March 2019	Brexit	It is expected that the UK will formally leave the EU by the end of March 2019.
31 March 2019	Actuarial Valuations	For all LGPS Funds in the England and Wales, the next actuarial valuation effective date will be 31 March 2019.
6 April 2019	Auto-enrolment	The minimum contribution rates for auto-enrolment will rise to 3% employer, 5% employee on this date.
6 April 2019	Change in the Lifetime Allowance (LTA)	The LTA for 2019/20 increases from £1,030,000 to £1,055,000
2019	Pensions Dashboard	These are expected to go live some time in 2019

MEET SOME OF THE TEAM

THINGS YOU MAYBE DIDN'T KNOW

Name: Susan Greenwood

Role: Investment Consultant

Joined Mercer: 2007

Place of Birth: Liverpool

Favourite film: The English Patient

How did you spend the holidays?: Chasing kids around

What was your favourite Christmas present? Chocolate

Did you make a New Year's resolution and was it?: No – I can't stick to them!

Name: Will Dunn

Role: Wealth Analyst

Joined Mercer: August 2016

Place of Birth: Douglas, Isle of Man

Favourite film: Inception

How did you spend the holidays?: Stayed in the Lake District for a couple of days

What was your favourite Christmas present? Indoor skydiving tickets

Did you make a New Year's resolution and was it?: Get over my fear of heights

Name: Kieran O'Connor

Role: Wealth Analyst

Joined Mercer: September 2017

Place of Birth: Whiston

Favourite film: The Departed

How did you spend the holidays?: Gorging on festive food

What was your favourite Christmas present? Socks – you can never have enough!

Did you make a New Year's resolution and was it?: Yes, to run a longer distance each week, every week. So far, so good.

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ISLINGTON

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London N7 7EP

Report of: **Corporate Director of Resources**

Meeting of:	**Date**	**Agenda item**	**Ward(s)**
Pensions Sub-Committee	25 March 2019		n/a

Delete as appropriate		Non-exempt

SUBJECT: LGPS STATUTORY GUIDANCE ON ASSET POOLING

1. Synopsis

1.1 This report covers the MHCLG guidance that sets out the requirements on administering authorities in relation to the pooling of LGPS assets, building on previous Ministerial communications and guidance on investment strategies, and taking account of the current state of progress on pooling. It is made under the powers conferred on the Secretary of State by Regulation 7(1) of The Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016 (the 2016 Regulations). Administering authorities are required to act in accordance with it.

2. Recommendation

2.1 To note the LGPS statutory guidance attached as Appendix I

2.2 To consider and submit any comments to the MHCLG by 28th March 2019

3. Background

3.1 The reform of investment management in the Local Government Pension Scheme (LGPS) for England and Wales began in 2015 with the publication of criteria and guidance on pooling of LGPS assets, following extensive consultation with the sector. LGPS administering authorities responded by coming together in groups of their own choosing to form eight asset pools.

3.1.1 This is a considerable achievement in itself, but there is still a long way to go to complete the transition of assets and to deliver the full benefits of scale. In the light of experience to date with pooling and the challenges ahead, authorities have requested guidance on a range of issues. The government believes the time is now right for new guidance to support further progress.

3.1.2 The guidance document –Appendix 1 covers the following

- Introduction

- Definitions
- Structure and scale
- Governance
- Transition of assets to the pool
- Making new investments outside the pool
- Infrastructure investment
- Reporting

3.2 Members are asked to review the draft comments below and agree a final version for submission by the deadline.

Islington's overall view

3.2.1 The Islington fund is part of LCIV and was one of the first London boroughs to pool its assets in 2015. Subsequent to that just under 50% of total portfolio now sits on the LCIV platform. The assets we retain are either closed funds that will have to run until the end of the funds life or asset classes or products determined by our strategic allocation that are not available to our pool. We believe pool fund definition should be widened to recognise where local authorities collaborate to procure an investment (not available in the pool company) with a fund manager and are treated as an LGPS share class to attract reduction in fees. We do not believe the pools have had enough time to prove themselves on selection of managers to achieve optimum performance net of fees and value for money to pay our pensioners and sustain our funds and as such, the mandated 2020 date should be flexible. Governance of the pools is very essential and in its early days some best practise, guidance will be helpful.

3.3. Further detailed comments on the sections are listed below for review by Members:

Section 2 definitions

3.3.1 **Pool company'** *the Financial Conduct Authority (FCA) regulated company which undertakes selection, appointment, dismissal and variation of terms of investment managers, and provides and operates pool vehicles for pool members*.

Comment: we welcome this clarity of what is a pool company

Pool fund' *a regulated unitised fund structure operated by a regulated pool company, such as an Authorised Contractual Scheme (ACS).*

Comment we would welcome the recognition of local authorities collaborating to invest outside ACS defined as pool fund.

Section- Structure and scale

3.3.2 *Regular review of services and procurement*

3.5 Pool governance bodies, working with the pool company, should regularly review the provision of services to the pool, and the process of procurement, to ensure value for money and cost transparency. Where services are procured or shared by pool members, pool members should regularly review the rationale and cost-effectiveness of such arrangements, compared to procurement and management through the pool company. Pool members and pool companies should consider using the national LGPS procurement frameworks www.nationallgpsframeworks.org) where appropriate.

Comment: transition management would be a good example of using the national LGPS procurement framework.

3..3.3 ***Section - Governance***

4.1 Pool members must establish and maintain a pool governance body in order to set the direction of the pool and to hold the pool company to account. Pool governance bodies should be appropriately democratic and sufficiently resourced to provide for effective decision making and oversight.

4.2 Pool members, through their internal governance structures, are responsible for effective governance and for holding pool companies and other service providers to account. Strategic asset

allocation remains the responsibility of pool members, recognising their authority's specific liability and cash-flow forecasts.
Comment: some good practices or guidance to hold pool companies to account will be helpful.

4.8 *Pool members collectively through their pool governance bodies should decide the pool's policy on which aspects of asset allocation are strategic and should remain with the administering authority, and which are tactical and best undertaken by the pool company. Pool governance bodies, when determining where such decisions lie, should be mindful of the trade-off between greater choice and lower costs and should involve the pool company to ensure the debate is fully informed on the opportunities and efficiencies available through greater scale.*

Comment: Whilst accepting that this may be a preference for some pool members , in the LCIV where there are 32 pool members, we believe the governance body is not fully representative and equipped to decide which aspect of asset allocation is tactical and strategic. Perhaps pool members should agree individually with the pool company rather than implementing a general policy that may not meet a pool members objective and accountability to its council tax payers.

3.3.4 ***Section 6- Making new investments outside the pool***
Pool members should normally make all new investments through the pool company in order to maximise the benefits of scale. Following the 2019 valuation, pool members will review their investment strategies and put revised strategies in place from 2020. From 2020, when new investment strategies are in place, pool members should make new investments outside the pool only in very limited circumstances.
A small proportion of a pool member's assets may be invested in local initiatives within the geographical area of the pool member or in products tailored to particular liabilities specific to that pool member. Local assets should:

- *Not normally exceed an aggregate 5% of the value of the pool member's assets at the point of investment.*
- *Be subject to a similar assessment of risk, return and fit with investment strategy as any other investment.*

6.3 Pool members may invest through pool vehicles in a pool other than their own where collaboration across pools or specialisation by pools can deliver improved net returns.

6.4 During the period of transition, while pool governance bodies and pool companies work together to determine and put in place the agreed range of pool vehicles, a pool member may make new investments outside the pool, if following consultation with the pool company, they consider this is essential to deliver their investment strategy. This exemption only applies until the pool vehicles needed to provide the agreed asset allocation are in place:

Comment: Where a pool member should make an investment tailored to particular liabilities specific to that pool member does the cap of 5% apply? I would imagine a fund nearing a fully funded position and de- risking would require more than 5% of total fund to implement such a strategy.
It is very helpful that pool members may invest in a pool other than their own where specialism by a pool can deliver improved net returns over the long term. Is there a criteria of what specialization will mean across all pools?

4. Implications

4.1 Financial implications

None applicable to this report. Financial implications will be included in each report to the Pensions Sub-Committee as necessary.

4.2 **Legal Implications**
None applicable to this report.

4.3 **Environmental Implications**
None applicable to this report. .

4.4 **Resident Impact Assessment**
None applicable to this report. The council must, in the exercise of its functions, have due regard to the need to eliminate discrimination, harassment and victimisation, and to advance equality of opportunity, and foster good relations, between those who share a relevant protected characteristic and those who do not share it (section 149 Equality Act 2010). The council has a duty to have due regard to the need to remove or minimise disadvantages, take steps to meet needs, in particular steps to take account of disabled persons' disabilities, and encourage people to participate in public life. The council must have due regard to the need to tackle prejudice and promote understanding

5. Conclusion and reasons for recommendation

5.1 Members are asked to consider the Asset Pooling Statutory Guidance and review the initial draft comments and make a final submission to MHCLG by 28th March 2019.

Background papers:
None

Final report clearance:

Signed by:

Corporate Director of Resources Date

Received by:

Head of Democratic Services Date

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Local Government Pension Scheme

Statutory guidance on asset pooling

Contents

Foreword

The reform of investment management in the Local Government Pension Scheme (LGPS) for England and Wales began in 2015 with the publication of criteria and guidance on pooling of LGPS assets, following extensive consultation with the sector. LGPS administering authorities responded by coming together in groups of their own choosing to form eight asset pools.

Through the hard work and commitment of people across the scheme, those eight pools are now operational. Their scale makes them significant players at European or global level, and significant annual savings have already been delivered, with the pools forecasting savings of up to £2bn by 2033. Along the way many lessons have been learnt and great progress has been made in developing expertise and capacity, including in private markets and infrastructure investment.

This is a considerable achievement in itself, but there is still a long way to go to complete the transition of assets and to deliver the full benefits of scale. In the light of experience to date with pooling and the challenges ahead, authorities have requested guidance on a range of issues. The time is now right for new guidance to support further progress.

1 Introduction

1.1 This guidance sets out the requirements on administering authorities in relation to the pooling of LGPS assets, building on previous Ministerial communications and guidance on investment strategies, and taking account of the current state of progress on pooling. It is made under the powers conferred on the Secretary of State by Regulation 7(1) of The Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016 (the 2016 Regulations). Administering authorities are required to act in accordance with it.

1.2 This guidance replaces the section at pages 7 to 8 of Part 2 of *Guidance for Preparing and Maintaining an Investment Strategy*, issued in September 2016 and revised in July 2017, which deals with regulation 7(2)(d) of the 2016 Regulations. It also replaces *Local Government Pension Scheme: Investment Reform Criteria and Guidance,* issued in November 2015.

2 Definitions

2.1 This guidance introduces a set of definitions for use in this and future guidance, as follows:

'Pool' the entity comprising all elements of a Local Government Pension Scheme (LGPS) asset pool
'Pool member' an LGPS administering authority which has committed to invest in an LGPS pool and participates in its governance
'Pool governance body' the body used by pool members to oversee the operation of the pool and ensure that the democratic link to pool members is maintained (for example, Joint Committees and officer committees)
'Pool company' the Financial Conduct Authority (FCA) regulated company which undertakes selection, appointment, dismissal and variation of terms of investment managers, and provides and operates pool vehicles for pool members
'Pool fund' a regulated unitised fund structure operated by a regulated pool company, such as an Authorised Contractual Scheme (ACS)
'Pool vehicle' an investment vehicle (including pool funds) made available to pool members by a regulated pool company
'Pooled asset' an investment for which the selection, appointment, dismissal and variation of terms for the investment manager is delegated to a regulated pool company, or an investment held in a pool vehicle
'Retained asset' an existing investment retained by a pool member during the transition period
'Local asset' a new investment by a pool member which is not a pooled asset

3 Structure and scale

3.1 All administering authorities must pool their assets in order to deliver the benefits of scale and collaboration. These include:

- reduced investment costs without affecting gross risk-adjusted returns
- reduced costs for services such as custody, and for procurement
- strengthened governance and stewardship and dissemination of good practice
- greater investment management capacity and capability in the pool companies, including in private markets
- increased transparency on total investment management costs
- diversification of risk through providing access to a wider range of asset classes, including infrastructure investments

3.2 In order to maximise the benefits of scale, pool members must appoint a pool company or companies to implement their investment strategies. This includes:

- the selection, appointment, dismissal and variation of terms of investment managers, whether internal or external

- the management of internally managed investments
- the provision and management of pool vehicles including pool funds

It is for the pool companies to decide which investment managers to use for pool vehicles, including whether to use in-house or external management. Pool members may continue to decide if they wish to invest via in-house or externally managed vehicles.

3.3 Pool companies may be wholly owned by pool members as shareholders or may be procured and appointed by the pool members as clients.

3.4 A pool company must be a company regulated by the Financial Conduct Authority (FCA) with appropriate FCA permissions for regulated activities. This helps ensure the pools comply with financial services legislation, and provides additional assurance to scheme members and employers. Depending on the structure of the pool, appropriate permissions may include permissions for execution, acting as agent, provision of advice, or such other permissions as required by the FCA. Where regulated funds (e.g. in an ACS) are operated by the pool company it should comply with relevant UK legislation.

Regular review of services and procurement

3.5 Pool governance bodies, working with the pool company, should regularly review the provision of services to the pool, and the process of procurement, to ensure value for money and cost transparency. Where services are procured or shared by pool members, pool members should regularly review the rationale and cost-effectiveness of such arrangements, compared to procurement and management through the pool company. Pool members and pool companies should consider using the national LGPS procurement frameworks (www.nationallgpsframeworks.org) where appropriate.

Regular review of active and passive management

3.6 Pool members, working with the pool company, should regularly review the balance between active and passive management in the light of performance net of total costs. They should consider moving from active to passive management where active management has not generated better net performance over a reasonable period. Pool members should also seek to ensure performance by asset class net of total costs is at least comparable with market performance for similar risk profiles.

4 Governance

4.1 Pool members must establish and maintain a pool governance body in order to set the direction of the pool and to hold the pool company to account. Pool governance bodies should be appropriately democratic and sufficiently resourced to provide for effective decision making and oversight.

4.2 Pool members, through their internal governance structures, are responsible for effective governance and for holding pool companies and other service providers to account. Strategic asset allocation remains the responsibility of pool members, recognising their authority's specific liability and cash-flow forecasts.

4.3 Members of Pension Committees are elected representatives with duties both to LGPS employers and members, and to local taxpayers. Those who serve on Pension Committees and equivalent governance bodies in LGPS administering authorities are, in many ways, required to act in the same way as trustees in terms of their duty of care to scheme employers and members, but are subject to a different legal framework, which derives from public law. In particular while they have legal responsibilities for the prudent and effective stewardship of LGPS funds, LGPS benefits are not dependent on their stewardship but are established and paid under statute in force at the time.

4.4 Those who serve on Pension Committees and equivalent governance bodies in pool members should therefore take a long term view of pooling implementation and costs. They should take account of the benefits across the pool and across the scheme as a whole, in the interests of scheme members, employers and local taxpayers, and should not seek simply to minimise costs in the short term.

4.5 Local Pension Boards of pool members have a key role in pool governance, given their responsibilities under the LGPS Regulations 2013 (regulation 106 (1)) for assisting authorities in securing compliance with legislation, and ensuring effective and efficient governance and administration of the LGPS. They can provide additional scrutiny and challenge to strengthen pool governance and reporting, and improve transparency and accountability for both members and employers.

4.6 Local Pension Boards may also provide a group of knowledgeable and experienced people from which observers may be drawn if pool members wish to include observers on pool governance bodies.

Strategic and tactical asset allocation

4.7 Pool members are responsible for deciding their investment strategy and asset allocation, and remain the beneficial owners of their assets, in accordance with *Guidance for Preparing and Maintaining an Investment Strategy.*

4.8 Pool members collectively through their pool governance bodies should decide the pool's policy on which aspects of asset allocation are strategic and should remain with the administering authority, and which are tactical and best undertaken by the pool company. Pool governance bodies, when determining where such decisions lie, should be mindful of the trade-off between greater choice and lower costs and should involve the pool company to ensure the debate is fully informed on the opportunities and efficiencies available through greater scale.

4.9 Providing pool members with asset allocation choices through an excessively wide range of pool vehicles or investment managers will restrict the pool company's ability to use scale to drive up value. On the other hand maximising scale by significantly limiting asset allocation options may not provide all pool members with the diversification needed to meet their particular liability profile and cash flow requirements. Pool members should set out in their Funding Strategy Statement and Investment Strategy Statement how they, through the pool governance body, have balanced these considerations and how they will keep this under regular review.

4.10 Where necessary to deliver the asset allocation required by pool members, pool companies may provide a range of pool vehicles and in addition arrange and manage segregated mandates or access to external specialist funds. Pool governance bodies should ensure that their regulated pool companies have in place the necessary permissions to enable pool vehicles to be made available where appropriate.

4.11 Determining where asset allocation decisions lie will not be a one-off decision as pool member requirements will change over time. Pool governance bodies should ensure that a regular review process, which involves both pool members and pool companies, is in place.

5 Transition of assets to the pool

5.1 Pool members should transition existing assets into the pool as quickly and cost effectively as possible. Transition of listed assets should take place over a relatively short period.

5.2 Pool governance bodies, working with pool companies and, where appointed, external transition managers, should seek to minimise transition costs to pool members while effectively balancing speed, cost and timing, taking into account exit or penalty costs and opportunities for crossing trades.

5.2 The transition process will incur direct or indirect costs which may fall unevenly across pool members. For example, where the selected managers are used by some pool members but not others. In such cases pool members who are already using the selected manager may incur significantly lower (if any) transition costs than those who do not.

5.3 Inter-authority payments (or other transfers of value) may be desirable in order to share these costs equitably between pool members. The Government's view is that such payments are investment costs within Regulation 4(5) of the 2016 Regulations, and payments made by a pool member to meet its agreed share of costs may be charged to the fund of that pool member, whether the payments are made to other pool members, the pool company, or another body by agreement.

Temporary retention of existing assets

5.4 In exceptional cases, some existing investments may be retained by pool members on a temporary basis. If the cost of moving the existing investment to a pool vehicle exceeds the benefits of doing so, it may be appropriate to continue to hold and manage the existing investment to maturity before reinvesting the funds through a pool vehicle.

5.5 In many cases there will be benefits in such retained assets being managed by the pool company in the interim. However pool members may retain the management of existing long term investment contracts where the penalty for early exit or transfer of management would be significant. These may include life insurance contracts ('life funds') accessed by pool members for the purpose of passive equity investment, and some infrastructure investments. Pool members may also retain existing direct property assets where these may be more effectively managed by pool members.

Regular review of retained assets

5.6 Pool members, working with the pool company, should undertake regular reviews (at least every three years) of retained assets and the rationale for keeping these assets outside the pool. They should review whether management by the pool company would deliver benefits. Pool members should consider the long term costs and benefits across the pool, taking account of the guidance on cost-sharing, and the presumption should be in favour of transition to pool vehicles or moving such assets to the management of the pool company.

6 Making new investments outside the pool

6.1 Pool members should normally make all new investments through the pool company in order to maximise the benefits of scale. Following the 2019 valuation, pool members will review their investment strategies and put revised strategies in place from 2020. From 2020, when new investment strategies are in place, pool members should make new investments outside the pool only in very limited circumstances.

6.2 A small proportion of a pool member's assets may be invested in local initiatives within the geographical area of the pool member or in products tailored to particular liabilities specific to that pool member. Local assets should:

- Not normally exceed an aggregate 5% of the value of the pool member's assets at the point of investment.
- Be subject to a similar assessment of risk, return and fit with investment strategy as any other investment.

6.3 Pool members may invest through pool vehicles in a pool other than their own where collaboration across pools or specialisation by pools can deliver improved net returns.

6.4 During the period of transition, while pool governance bodies and pool companies work together to determine and put in place the agreed range of pool vehicles, a pool member may make new investments outside the pool, if following consultation with the pool company, they consider this is essential to deliver their investment strategy. This exemption only applies until the pool vehicles needed to provide the agreed asset allocation are in place.

7 Infrastructure investment

7.1 Infrastructure investment has the potential to provide secure long term returns with a good fit to pension liabilities, and form part of investment strategies of authorities. The establishment of the pools was intended to provide the scale needed for cost-effective investment in infrastructure, and to increase capacity and capability to invest in infrastructure.

7.2 There is no target for infrastructure investment for pool members or pools, but pool members are expected to set an ambition on investment in this area. Pool companies may provide pool vehicles for investment in UK assets, or overseas assets, or both, as required to provide the risk and return profile to meet pool member investment strategies. However the Government expects pool companies to provide the capability and capacity for pools over time to move towards levels of infrastructure investment similar to overseas pension funds of comparable aggregate size.

7.3 Pool companies may provide pool vehicles for investment in existing (brownfield) or new (greenfield) infrastructure, based on an assessment of the benefits and risks in relation to pool member liabilities, and non-financial factors where relevant. Pool members may invest in their own geographic areas but the asset selection and allocation decisions should normally be taken by the pool company in order to manage any potential conflicts of interest effectively, maintain propriety, and ensure robust evaluation of the case for investment.

7.4 For the purpose of producing annual reports, infrastructure assets are defined in the Chartered Institute of Public Finance and Accountancy (CIPFA) guidance *Preparing the Annual Report* as follows:

Infrastructure assets are the facilities and structures needed for the functioning of communities and to support economic development. When considered as an investment asset class, infrastructure investments are normally expected to have most of the following characteristics:

- *Substantially backed by durable physical assets;*
- *Long life and low risk of obsolescence;*
- *Identifiable and reliable cash flow, preferably either explicitly or implicitly inflation-linked;*
- *Revenues largely isolated from the business cycle and competition, for example, through long term contracts, regulated monopolies or high barriers to entry;*
- *Returns to show limited correlation to other asset classes.*

Key sectors for infrastructure include transportation networks, power generation, energy distribution and storage, water supply and distribution, communications networks, health and education facilities, social accommodation and private sector housing.

Conventional commercial property is not normally included, but where it forms part of a broader infrastructure asset, helps urban regeneration or serves societal needs it may be.

7.5 All residential property is included in this definition of infrastructure. It is not restricted to social accommodation or private sector housing.

7.6 A variety of platforms may be required to implement the infrastructure investment strategies of pool members. Pool companies are expected to provide access to a range of options over time including direct and co-investment opportunities.

8 Reporting

8.1 Pool members are required to report total investment costs and performance against benchmarks publicly and transparently in their annual reports, following the CIPFA guidance *Preparing the Annual Report*, with effect from the 2018-19 report.

8.2 In summary, pool member annual reports should include:

- opening and closing value and proportion of pooled assets by asset class
- opening and closing value and proportion of local assets by asset class
- net and gross performance of pooled assets by asset class
- total costs of pooled assets by asset class
- for actively managed listed assets, net performance by asset class net of total costs compared to appropriate passive indices over a one, three and five year period
- net and gross performance of local assets by asset class
- total costs of local assets by asset class
- asset transition during the reporting year
- transition plans for local assets
- pool set-up and transition costs, presented alongside in-year and cumulative savings from pooling
- ongoing investment management costs by type, with a breakdown between pooled assets and local assets

8.3 Investments should be classed as pool assets on the basis of the definition in the CIPFA guidance *Preparing the Annual Report.*

For the purpose of defining those assets which are classed as being within an asset pool, 'pooled assets' are those for which implementation of the investment strategy – i.e. the selection, appointment, dismissal and variation of terms for the investment managers (including internal managers) – has been contractually, transferred to a third party out with the individual pension fund's control.

8.4 Any investment where a pool member retains the day to day management, or the responsibility for selecting or reappointing an external manager, is not a pool asset.

8.5 Pool members should provide a rationale for all assets continuing to be held outside the pool, including the planned end date and performance net of costs including a comparison which costs of any comparable pool vehicles. They should also set out a high level plan for transition of assets.

8.6 The SAB will publish an annual report on the pools based on aggregated data from the pool member annual reports, in the Scheme Annual Report. Pool members should comply with all reasonable requests for any additional data and information from the SAB to enable it to publish a comprehensive report.

8.7 Pool members should ensure that pool companies report in line with the SAB Code of Cost Transparency. They should also ensure that pool companies require their internal and external investment managers to do so.

8.8 Pool members should also ensure that the annual report of the pool company is broadly consistent with the reports of pool members, and with the Scheme Annual Report, in so far as it relates to their investments, and that the report includes a narrative to explain differences. These may arise for example from reporting periods of pool companies which differ from that of the pool member.

8.9 Pool members are required to report any change which results in failure to meet the requirements of this guidance to the LGPS Scheme Advisory Board (SAB) and to MHCLG.

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ISLINGTON

Finance Department
7 Newington Barrow Way
London N7 7EP

Report of: **Corporate Director of Resources**

Meeting of:	Date	Agenda item	Ward(s)
Pensions Sub-Committee	25 March 2019		n/a

Delete as appropriate	Exempt	~~Non-exempt~~

Appendix 1 is exempt and not for publication as it contains the following category of exempt information as specified in Paragraph 3, Schedule 12A of the Local Government Act 1972, namely: Information relating to the financial or business affairs of any particular person (including the authority holding that information)

SUBJECT: LISTED EQUITY PORTFOLIO – UPDATE ON TRANSFER OF ASSETS FROM LCIV ALLIANZ TO LCIV RBC SUSTAINABLE FUND

1. Synopsis

1.1 This report and exempt Appendix 1 provide updated information on implementation of members decision to transfer global equities on LCIV platform from Allianz to RBC Sustainable fund

1.2 MJ Hudsons, our independent investment advisors have also prepared briefing note cataloguing progress to date, proposed options on transition and the proposed timeline attached as exempt Appendix 1)

2. Recommendation

2.1 To note the progress to date with LCIV on the transfer of assets

2.2 To note and consider the issue of withholding tax accrued to the Islington fund only

2.3 To agree to transition the units owned without the withholding tax accrued

2.4 To delegate to the Corporate Director of Resources, in consultation with the Assistant Chief Executive, Governance and HR, authority to negotiate and agree with the LCIV

- Any costs associated with the termination of the Allianz sub fund mandate
- Fair recourse to dealing with the withholding tax accrued

3. Background

Allianz

3.1 The Committee agreed to transfer our global equity assets with Allianz to the LCIV Allianz sub fund as part of the Phase 1 funding in December 2015. We were part of 3 boroughs who completed this transition at the time. As of the 2nd quarter of this year, the other 2 boroughs terminated their mandate with Allianz due to changes in asset allocation and requirements. On the point of termination the fund ownership was 15% Islington, Ealing-53% and Wandsworth 32%.

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3.2 The LCIV in April 2018 gave the fund assurances they will not terminate the Allianz sub fund because asset under management c £120m still makes it viable. In October 2017 all three Boroughs notified the LCIV of our intention to divest from the Allianz sub fund and assurances were given that no one fund will be penalised for leaving at different times and any termination cost will be shared between all the previous unit holders.

3.3 Members then agreed in November 2018 ,after a due diligence process to transfer our assets to LCIV RBC Sustainable fund and delegated authority to Director of Corporate Resources in consultation with the Assistant Chief Executive, Governance and HR, to agree terms with the LCIV and appoint a transition manager if required to implement the transfer.

3.4 **Update on progress on transfer of assets**

The LCIV, was notified after Members' decision in November to initiate the process and terms and conditions to be agreed. As part of the options provided by the LCIV to Islington for the transfer, the issue of accrued withholding tax of £1.5m was raised. This was accrued income for the whole fund not available to invest as the last fund to exit, whilst the other 2 boroughs had been prepaid on exit. The Corporate Director of Resources then agreed to engage an advisor from MJ Hudson Allenbridge to provide oversight and advice to ensure the transfer of assets achieve best value for the Islington Fund.

3.5. The briefing paper prepared by MJ Hudson, attached exempt Appendix1 gives details of the options provided by the LCIV, progress made to date, proposed transition process and a possible timeline.

3.6 Members are asked to receive the briefing, consider our options and agree to transition and seek a fair recourse for Islington from the LCIV on the whole fund accrued withholding tax.

4. Implications

4.1 **Financial implications**

4.1.1 The cost of providing independent investment advice and transition cost is part of fund management and administration fees charged to the pension fund.

4.2 **Legal Implications**

The Council, as the administering authority for the pension fund may appoint investment managers to manage and invest an infrastructure portfolio on its behalf (Regulation 8(1) of the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009 (as amended).

4.2.1 The Council is able to invest fund money in a London CIV fund asset without undertaking a competitive procurement exercise because of the exemption for public contracts between entities in the public sector (regulation 12 of the Public Contracts Regulations 2015). The conditions for the application of this exemption are satisfied as the London authorities exercise control over the CIV similar to that exercised over their own departments and CIV carries out the essential part of its activities (over 80%) with the controlling London boroughs.

4.2.2 The sub- committee must

(i) reasonably believe that the recommended investment manager's ability in and practical experience of financial matters makes them suitably qualified to make investment decisions for the Council

(ii) be satisfied that the fund (or relevant part of it) is managed by an adequate number of investment managers and that where there is more than one investment manager, the value of fund money to be managed by any one of them will not be disproportionate (in their view) in comparison with the value of fund money managed by other investment managers

(iii) have proper regard to the advice of the Interim Corporate Director of Resources and its external advisers, in relation to the proposed appointment

In considering the recommendations in this report, members must take into account the information contained in the Exempt Appendix 1 to this report

4.3 **Environmental Implications**

The environmental impacts were considered as part of the presentations where managers were asked to demonstrate how they took environmental and social governance issues in their portfolio construction. It was identified that the proposals in this report would have no adverse impacts.

4.4 **Resident Impact Assessment**

None applicable to this report. The council must, in the exercise of its functions, have due regard to the need to eliminate discrimination, harassment and victimisation, and to advance equality of opportunity, and foster good relations, between those who share a relevant protected characteristic and those who do not share it (section 149 Equality Act 2010). The council has a duty to have due regard to the need to remove or minimise disadvantages, take steps to meet needs, in particular steps to take account of disabled persons' disabilities, and encourage people to participate in public life. The council must have due regard to the need to tackle prejudice and promote understanding

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5. Conclusion and reasons for recommendation

5.1 Members are asked consider the MJ Hudson briefing attached as Exempt Appendix 1 and agree to transition our asset to LCIV RBC fund without the withholding tax and delegate to the Director of Corporate Resources in consultation with the Assistant Chief Executive, Governance and HR, authority to negotiate and agree with the LCIV any costs associated with the termination of the Allianz sub fund mandate and fair recourse to dealing with the withholding tax accrued.

Background papers:
Exempt Appendix 1 .

Final report clearance:

Signed by:

	Corporate Director of Resources	Date
Received by:		
	Head of Democratic Services	Date

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ISLINGTON

Finance Department
7 Newington Barrow Way
London N7 7EP

Report of: **Corporate Director of Resources**

Meeting of:	**Date**	**Agenda item**	**Ward(s)**
Pensions Sub-Committee	25 March 2019		

Delete as appropriate	Exempt	Non-exempt

Appendix 2 attached is exempt and not for publication as it contains the following category of exempt information as specified in Paragraph 3, Schedule 12A of the Local Government Act 1972, namely: Information relating to the financial or business affairs of any particular person (including the authority holding that information).

SUBJECT: The London CIV Update

1. Synopsis

1.1 This is a report informing the committee of the progress made at the London CIV in launching funds, running of portfolios and reviewing governance and investment structure, over the period December to March 2019.

2. Recommendations

2.1 To note the progress and news to March 2019 including minutes from the shareholder meeting held in January Appendix 1 and the new briefing Collective Voice attached as Appendix 2 (private and confidential)

3. Background

3.1 **Setting up of the London CIV Fund**
Islington is one of 33 London local authorities who have become active participants in the CIV programme. The CIV has been constructed as a FCA regulated UK Authorised Contractual Scheme (ACS). The ACS is composed of two parts: the Operator and the Fund.

3.2 A limited liability company (London LGPS CIV Ltd) has been established, with each participating borough holding a nominal £1 share. The company is based in London Councils' building in Southwark Street. A branding exercise has taken place and the decision was taken to brand the company as 'London CIV.' The London CIV received its ACS authorisation in November 2015.

3.3 **Launching of the CIV**
It was noted that a pragmatic starting point was to analyse which Investment Managers (IM) boroughs were currently invested through, to look for commonality (i.e. more than one borough invested with the same IM in a largely similar mandate), and to discuss with boroughs and IMs which of these 'common' mandates would be most appropriate to transition to the ACS fund for launch. Each mandate would become a separate, ring-fenced, sub-fund within the overall ACS fund. Boroughs would be able to move from one sub-fund to another relatively easily, but ring-fencing would prevent cross contamination between sub-funds.

3.3.1 Further discussions have been held with managers, focussing specifically on what would be achievable for launch, taking into account timing and transition complexities. Four managers have now been identified as offering potential opportunities for the launch of the CIV. These managers would provide the CIV with 9 sub-funds, covering just over £6bn of Borough assets and providing early opportunity to 20 boroughs. The sub-funds will consist of 6 'passive' equity sub-funds covering £4.2bn of assets, 2 Active Global Equity mandates covering £1.6bn and 1 Diversified Growth (or multi-asset) Fund covering just over £300m. Those boroughs that do not have an exact match across for launch are able to invest in these sub-funds from the outset at the reduced AMC rate that the CIV has negotiated with managers.

3.4 The Phase 1 launch was with Allianz our global equity manager and Ealing and Wandsworth are the 2 other boroughs who hold a similar mandate. The benefits of transfer include a reduction in basic fees and possible tax benefits because of the vehicle used. Members agreed to transfer our Allianz portfolio in Phase 1 launch that went ahead on 2 December.

3.5 **Update to March 2019**
3.5.1 The Annual Shareholder meeting was held on 31 Janary 2019 and minutes are attached as Appendix1 some of the major resolutions agreed were:
The Resolution 4
a) That the General Meeting approve the change in the definition of the purpose of the Company set out in Clause 2.1 of the Shareholder Agreement from the Current wording " The business of the Company shall (unless and until otherwise determined in accordance with this Agreement) be confined to acting as the FCA authorised operator of an ACS to provide a collaborative platform through which the Administering Authorities of the LGPS funds can aggregate their pension monies and other investments.
The Company will be branded as "London CIV" to the

Proposed wording " The business of the Company shall (unless and until otherwise determined in accordance with this Agreement) be confined to acting as the FCA1 authorised company to provide a collaborative platform through which the Administering Authorities of the LGPS funds can aggregate their pension monies and other investments. The Company will be branded as "London CIV".and approves the small amendments to the "Definitions" section

3.5.2 The MTFS (medium term finanacial strategy) was agreed and the Objectives and KPI's are listed below:

2019-2020 Objectives and KPIs

Objectives	KPIs
Work in partnership with our shareholders to achieve the company's purpose and vision	Shareholder support of MTFS and change in business purpose
Generate value for LLAs through pooling of their	Generate value for LLAs through pooling of their

pension assets in line with the value proposition	pension assets • Increase gross / net savings year on year • £21.1bn AUM (£11.1bn in LCIV funds and £10bn in passives)
Provide a product portfolio and pooling structure which enable LLAs to meet their investment needs and pooling requirements	• Deliver fund launch plan • Expand pooling structures • 32 LLA pooling plans obtained and incorporated into LCIV 2020 MTFS
Establish a transparent and trust-based relationship with our clients and work jointly to deliver LLA pooling plans	• SLAs agreed with 32 LLAs • Quarterly meetings held with 32 clients • Improved client satisfaction survey results
Maintain effective financial controls; ensure financial stability securing the company's capital base to meet regulatory capital requirements and ability to offer a broad range of products and pooling structures	Sufficient Regulatory Capital
Maintain a robust governance framework and a regulatory compliant and risk-controlled operating environment ensuring current and new regulation, laws and standards are adhered to	No material regulatory, audit or depositary findings
Establish and maintain a cost-effective operating model ensuring data integrity, scalable systems and cost efficiencies	Deliver on budget
Build a client and shareholder focused, collaborative work environment supported by a remuneration policy which attracts, retains and develops talented individuals	32 Staff by March 2020

3.5.3 The LCIV now publish a monthly news bulletin called the Collective Voice- a copy attached for information as Appendix 2 (private and confidential). Highlights include; the investment forum agenda for London Local authorities scheduled on 8th March, proposed fund launch plan, investment funds and people news.

3.6 **CIV Financial Implications- Implementation and running cost**

A total of 75,000 was contributed by, each London Borough, including Islington, towards the setting up and receiving FCA authorisation to operate between 2013 to 2015. All participating boroughs also agreed to..

The transfer of our Allianz managed equities to the CIV in December 2015 was achieved at a transfer cost of £7,241. pay £150,000 to the London CIV to subscribe for 150,000 non-voting redeemable shares of £1 each as the capital of the Company . After the legal formation of the London CIV in October 2015 , there is an agreed annual £25,000 running cost invoice for each financial year

All sub-funds investors pay a management fee of .050% of AUM to the London CIV in addition to managers' fees.

In April 2017 a service charge of 50k (+VAT) development funding was invoiced and a balance of £25k will be raised in December once the Joint Committee has reviewed the in-year budget.
Members agreed to the 0.005% of AUM option for charging fees on the LGIM passive funds that are held outside of the CIV and agreed that (depending on the outcome of discussions) the same will be applied to BlackRock passive funds.
The Newton transition cost the council 32k.
In a April 2018 annual service charge of 25k (+VAT) and 65k (split 43.3k and16.6k) development fund was invoiced to all members.

4. Implications

4.1 **Financial implications:**

4.1.1 Fund management and administration fees are charged directly to the pension fund.

4.2 **Legal Implications:**

4.2.1 The Council, as the administering authority for the pension fund may appoint investment managers to manage and invest an equity portfolio on its behalf (Regulation 8(1) of the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009 (as amended).

4.2.2 The Council is able to invest fund money in a London CIV fund asset without undertaking a competitive procurement exercise because of the exemption for public contracts between entities in the public sector (regulation 12 of the Public Contracts Regulations 2015). The conditions for the application of this exemption are satisfied as the London authorities exercise control over the CIV similar to that exercised over their own departments and CIV carries out the essential part of its activities (over 80%) with the controlling London boroughs.
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4.3 **Environmental Implications:**

4.3.1 None specific to this report

4.4 **Resident Impact Assessment:**

4.4.1 The Council must, in carrying out its functions, have due regard to the need to eliminate unlawful discrimination and harassment and to promote equality of opportunity in relation to disability, race and gender and the need to take steps to take account of disabilities, even where that involves treating the disabled more favourably than others (section 49A Disability Discrimination Act 1995; section 71 Race Relations Act 1976; section 76A Sex Discrimination Act 1975."

An equalities impact assessment has not been conducted because this report is updating members on the implementation of a fund structure by external managers. There are therefore no specific equality implications arising from this report.

5. Conclusion and reasons for recommendations

5.1 The Council is a shareholder of the London CIV and has agreed in principle to pool assets when it is in line with its Fund strategy and will be beneficial to fund members and council tax payers. This is a report to allow Members to review progress at the London CIV and note the progress to date.

Background papers:
Final report clearance:

Signed by:

	Corporate Director of Resources	Date
Received by:		
	Head of Democratic Services	Date

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London CIV General Meeting 31 January 2019

In the interests of good communication this note summarises the decisions made at the 31 January 2019 London CIV General Meeting, together with next steps. The draft minutes will be circulated in due course.

The London CIV Chair and the Shareholder Committee Chair who chaired the meeting both thanked shareholders for their support for London CIV during the last six months and this report is an opportunity to repeat those thanks.

In summary

There were two main items of business. The change to the legal definition of London CIV's business purpose was ***agreed by a show of hands.*** *This now requires written approval from all London Local Authorities (LLAs) to become binding on shareholders. The annual budget which is set out in the Medium -Term Financial Strategy (MTFS) was also* ***approved****. The budget includes business objectives and prospective business for the year April 2019 to March 2020.*

Mike O'Donnell has been appointed permanent CEO, subject to FCA approval starting in early March. Mark Hyde-Harrison stays until the end of March to ensure a smooth handover. Lord Kerslake took the opportunity of the meeting to express his gratitude to Mark for his contribution to London CIV, moving it forward to a better place including a new governance framework, a clear strategic framework, and working with the team to deliver some challenging objectives.

CEO and Chair's report

The CEO and London CIV Chair reported on performance against the Medium- Term Financial Strategy and key issues facing London CIV to ensure that the product offer and services provided by London CIV meet borough's expectations.

Key highlights are:

- Ongoing **work to implement the new governance framework changes, including through the work of the Shareholder Committee** which has met twice with Cllr Yvonne Johnson as Chair. A report is circulated to all Shareholders following each meeting. The effectiveness of the new governance framework will be reviewed in the Autumn of 2019, taking account of the new MHCLG guidance.
- We are working to strengthen our **client relationship engagement**, including regular meetings with individual LLAs, and events for LLAs collectively. We expect to finalise the Service Level Agreement (SLA) such that LLAs sign up to the agreement during 2019 and plan to undertake a client satisfaction survey during 2019.
- We **expect to hit most KPIs in the current budget year.** LLA decision-making and asset transfer timescales mean that the active AUM target is less certain. However, taking passive and active funds together the 50% assets pooled by 31 March 2019 milestone is potentially achievable. It was noted that the revised AUM target at the end of March 2019 of £8.6bn on the ACS may not be met due to a combination of market move and a slower rate of transitions.
- **Five fund launches**: the LCIV Global Bond Fund (PIMCO) launched on 30 November. Our LCIV Infrastructure and LCIV Private Debt Funds are due to launch in the first months of 2019. Our LCIV Global Equity fund and LCIV Inflation Plus Fund proposals will soon be circulated to LLAs for feedback prior to submission to the FCA for approval.
- Work is in progress to achieve signature of **Pension Recharge and Guarantee Agreements.**
- Ongoing work to develop the **Responsible Investment** programme of activity and implement the Responsible Investment policy ratified in October 2018 following endorsement by the Shareholder Committee. The Responsible Investment annual report will be discussed at a Shareholder Committee Autumn 2019 meeting.

Financial Performance Update

In the six months to end of September 2018 the Company delivered a profit before tax for the period of **£470k** compared to the MTFS of **£313k.** The updated forecast for the full year is a profit before tax of **£342k** vs the MTFS equivalent of **£468k.**

AUM on the ACS has risen from **£6.2bn to £7.6bn** in the period despite outflows of over £791m moving off the ACS (principally from the Allianz fund). However, the year-end AUM forecast to March 2019 has been revised down from **£9.8bn to £8.6bn** for assets on the ACS/EUUT. AUM as at 27 November 2018 was **£7.46bn**. Passive assets (LGIM/Blackrock) have increased over the period from **£8.4bn to £9.7bn**.

The forecast shortfall in AUM has resulted in a reduction in fee income of £349k. However, expenses are forecast to be lower than budgeted due to timing differences on hiring staff and the timing of the implementation of the investment and risk management system.

The capital adequacy position of the Company remains satisfactory at the end of the period and the forecast to the end of the year based on the existing business model. The balance of the DFC invoiced in January turned LCIV from a loss to a profit in the current financial year demonstrating how important the DFC remains for the company as an income source.

Change in Business Purpose Definition

The General Meeting **agreed** to change the definition of business purpose in clause 2 of the Shareholder Agreement to read

The business of the Company shall (unless and until otherwise determined in accordance with this Agreement) be confined to acting as the FCA authorised company to provide a collaborative platform through which the Administering Authorities of the LGPS funds can aggregate their pension monies and other investments. The Company will be branded as "London CIV".

The words "the FCA authorised company" replace the phrase " the FCA authorised operator of an ACS".

The **next step** is for **all** LLAs to sign the letter agreeing to the change. Some have already done so, either on the day or in response to the letter circulated immediately after the meeting. It would be helpful to know the authorisation and signature arrangements for each LLA. We are compiling a summary which we hope will assist all LLAs in signing off approvals going forward.

Annual Budget and Business Plan 2019/20 (and Medium-Term Financial Strategy)

The Annual Budget includes 8 key business objectives (each with one or more KPIs) and a summary of prospective business. It is set in the context of a rolling five- year Medium Term Financial Strategy (MTFS). Together with the financial plan the key objectives are the basis for in-year performance monitoring by the Board and reporting to the Shareholder Committee and General Meetings.

A key theme is the importance of partnership and collaboration between London CIV and its client shareholder LLAs; and between LLAs collectively in order to achieve the success and sustainability of London CIV as a joint undertaking.

The Annual Budget, including the business objectives and outline of business for the year 2019/20 was **approved, following approval by the Board**.

The 2017/2018 governance review recommended that London CIV refresh its purpose and vision statements to provide a clear strategic framework, clarity of purpose and direction.
The updated purpose and vision statements are:

*Our purpose for the company is **"to be the LGPS pool for London to enable the London Local Authorities to achieve their pooling requirements".***

*Beyond our practical purpose to deliver pooling London CIV aspires to be "**a best in class asset pool that delivers value for Londoners".***

The MTFS contains 8 key objectives for 2019-2020, each with one or more KPIs. Together with the financial plan these key objectives are the basis for in-year performance monitoring by the Board and reporting to the Shareholder Committee and General Meetings. Individual sections of the MTFS detail key operational deliverables which are monitored by ExCo and the Board with high level updates in the CEO report to the Shareholder Committee, which is available to all Shareholders

- We are working with LLAs to understand their pooling plans and how these can be delivered to achieve maximum pooling at the earliest date for the benefit of all LLAs. Delivering pooling is not **only** dependent on fund launches, but is also driven by strategic asset allocation changes, manager rotations and movement from off-LCIV to on London CIV Funds
- The MTFS includes a **provisional** fund programme which will be reviewed and prioritised on an iterative basis informed by feedback from LLAs about their Strategic Asset Allocations and specific fund proposals. The programme, prioritisation and timing of fund launches is based on ongoing quantitative and qualitative feedback from LLAs, together with LLA decisions such as seed-funding and off-pool investment.
- The business governance framework focuses on **ways of pooling, recognising that LLAs require flexibility.** Originally, London CIV provided a vehicle for collaboration using an ACS and structures appropriate to liquid funds. Subsequently this has been extended to include structures more appropriate to illiquid funds. The ability to use IMAs as a vehicle for pooling is key to achieving full pooling. It will enable us to offer transition management services, provide oversight of passives and other assets, and potentially offer other services.
- Recruiting **skilled staff** is essential to achieve our objectives and we aim to find ways to collaborate with LLAs to recruit, exchange and develop staff to improve our capability to deliver pooling. The 2018 Governance Review pointed to the need to improve resourcing "substantially below adequate levels", recognising the tension inherent in funding a business at the development stage. The phased increase in staff resources to 36 has been sense checked by NEDs against other pools allowing for differences in operating models. It is pitched at a level to deliver the services of an FCA authorised LGPS pool investment oversight company, in the expectation that pools will be under MHCLG scrutiny and mindful of the challenge for all LLAs where investment is made against a backdrop of cost challenges. The Board is committed to a comprehensive review of the Remuneration Policy, including the Pension Scheme.

There was one vote against the budget at the meeting. Cllr Keith Onslow Shareholder Representative for Bromley expressed a number of concerns, including about the level of staff resources, and suggested that rather than approve the budget the incoming CEO should be requested to undertake a review.

The **next step** is to deliver the business plan and objectives agreed for 2019/20 within the agreed budget. This will be kept under review by the Board and the Shareholder Committee, through the quarterly CEO report which includes delivery against the key objectives measured by agreed KPIs. The plan also identifies key risks to be monitored and managed.

In response to the request at the meeting, we have subsequently asked the Depository if it would permit its annual due diligence reports to be shared with shareholders. as part of the suite of regular reporting to Shareholders. The Depository has not agreed to the request, but confirmed that LCIV could summarise any findings and report on this to shareholders. Additionally, if of assistance the Depositary would be happy to present to a shareholder meeting to discuss its role and oversight duties.

In response to a question about the cost of data feeds in the budget it was explained that this budget line covered a number of investment oversight information requirements (more detailed information was provided outside the meeting and is available on request).

Remuneration and Nomination Matters

This information report was **noted**.

The Board is committed to a **comprehensive review of the Remuneration Policy**, including the Pension Scheme arrangements in 2019/20.

London CIV's current AIFMD remuneration policy and annual remuneration statement is published in the annual Authorised Contractual Scheme Financial Statements. In late 2018, following a review of the Pension Scheme, access to the LGPS scheme was capped to those paid under £120,000. Any further changes to the pension scheme arrangements require the Pension Recharge agreement to be signed for financial stability reasons and to conclude the set-up of the LGPS scheme, including the Admission Agreement and Guarantee Agreement which would should have been finalised in 2015.

The current composition of the Board is shown at the end of this report. All directors are approved by the FCA. The Remuneration and Nomination Committee holds its next formal meeting in March 2019. The meeting cycle will include (re) appointments to the board for terms expiring in the period March to September 2019.

Kristina Ingate
Chief of Staff London CIV

22 Lavington Street London SE1 0NZ
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Current members of the Board

(biographical information available at www.londonciv.org.uk)

Lord Robert (Bob) Kerslake (Chair, NED) from Sept 2015 (four-year term ends Sept 2019)
Cllr Stephen Alambritis from Sept 2018 (three-year term ends Sept 2021)
Chris Bilsland (Chair Investment Oversight Committee, NED) from Sept 2015 (second three-year term ends Sept 2021)
Carolan Dobson (NED) from March 2016 (three-year term ends March 2019)
Cllr Ravi Govindia CBE from Sept 2018 (three-year term ends Sept 2021)
Eric Mackay (Chair Audit, Risk and Compliance Committee, NED and Chair RemNomCo) from Nov 2015 second three-year terms ends Nov 2021)
Paul Niven (NED) from 1 Sept 2017 (three-year term ends Sept 2020)
Linda Selman (NED) from 1 Sept 2017 (three-year term ends Sept 2020)

Mark Hyde-Harrison (Chief Executive Officer)
Brian Lee (Chief Operating Officer with responsibilities as Chief Finance Officer and Chief Compliance Officer)
The Chief Investment Officer is expected to be a Board member

In addition, Ian Williams is appointed as Treasurer Observer but is not a Non-Executive Director.

All Directors are FCA approved.

ISLINGTON

Finance Department
7 Newington Barrow Way
London N7 7EP

Report of: **Corporate Director of Resources**

Meeting of:	Date	Agenda item	Ward(s)
Pensions Sub-Committee	25 March 2019		n/a

Delete as appropriate		Non-exempt

SUBJECT: PENSIONS SUB-COMMITTEE 2019/20– FORWARD PLAN

1. Synopsis

1.1 The Appendix to this report provides information for Members of the Sub-Committee on agenda items for forthcoming meetings and training topics.

2. Recommendation

2.1 To consider and note Appendix A attached.

3. Background

3.1 The Forward Plan will be updated as necessary at each meeting, to reflect any changes in investment policy, new regulation and pension fund priorities after discussions with Members.

3.2 Details of agenda items for forthcoming meetings will be reported to each meeting of the Sub-Committee for members' consideration in the form of a Forward Plan. There will be a standing item to each meeting on performance and the LCIV.

4. Implications

4.1 **Financial implications**

4.1.1 The cost of providing independent investment advice is part of fund management and administration fees charged to the pension fund.

4.2 **Legal Implications**
None applicable to this report

4.3 **Environmental Implications**

None applicable to this report. Environmental implications will be included in each report to the Pensions Sub-Committee as necessary.

4.4 **Resident Impact Assessment**

None applicable to this report. The council must, in the exercise of its functions, have due regard to the need to eliminate discrimination, harassment and victimisation, and to advance equality of opportunity, and foster good relations, between those who share a relevant protected characteristic and those who do not share it (section 149 Equality Act 2010). The council has a duty to have due regard to the need to remove or minimise disadvantages, take steps to meet needs, in particular steps to take account of disabled persons' disabilities, and encourage people to participate in public life. The council must have due regard to the need to tackle prejudice and promote understanding

.

5. Conclusion and reasons for recommendation

5.1 To advise Members of forthcoming items of business to the Sub-Committee and training topics

Background papers:
None

Final report clearance:

Signed by:

	Corporate Director of Resources	Date
Received by:		
	Head of Democratic Services	Date

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Email: Joana.marfoh@islington.gov.uk

APPENDIX A

Pensions Sub-Committee Forward Plan for March 2019 to March 2020

Date of meeting	Reports
	Please note: there will be a standing item to each meeting on: • Performance report- quarterly performance and managers' update • CIV update report Equity protection- semi - annual monitoring
25 March 2019	Review of Hearthstone Fund Update on Allianz replacement on LCIV platform Asset pooling consultation by MHCLG
17 June 2019	Investment Strategy Review to include -Alternative products to corporate bond portfolio PIRC presentation of annual fund performance Update on actuarial position post 31 March 2019. 4 year business plan update
10 September 2019	Infrastructure managers' presentation
3 December 2019	Investment Strategy Review
3 March 2020	Employer consultation results on FSS and draft FSS Actuarial valuation final
15 June 2020	Final position report on equity protection

Past training for Members before committee meetings-

Date	**Training**
16 September 2014	Investment in Sub Saharan Africa - 6.20-.6.50pm Infrastructure - 6.55- 7.25pm
25 November 2014	Multi asset credit- 6.15-6.45pm Real estate including social housing- 6.50-7.20pm
9 March 2015	Frontier Market public equity- 6.15 -6.45pm Emerging market debt- 6.50- 7.20 pm
11 June 2015	Impact investing
14 September 2015- 4.45pm pm	Social bonds
13 June 2016	
21 September 2016	Actuarial review training

Proposed Training before committee meetings

November 2018	Actuarial update

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of the Local Government Act 1972.

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