

Pensions CIV Sectoral Joint Committee

Item no: 6

Investment Advisory Committee Update

Report by: Ian Williams **Job title:** Chair of Investment Advisory Committee

Date: 8 February 2017

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Summary The Investment Advisory Committee (IAC) continues to work closely with the London CIV on a wide range of investment related projects.

Recommendations The committee is recommended to:

- i. Note the contents of this report;

London CIV Investment Advisory Committee Update

December 2016 – January 2017

Introduction

1. The Investment Advisory Committee (IAC) was formed in September 2015 with the remit to:
 - i. To support the Joint Committee in the investment decision making process
 - ii. To liaise with the Fund Operator of the CIV in defining Shareholders' investment needs.
2. Since the last Joint Committee meeting the IAC has formally met twice in December and January, in addition, the Treasurers from the IAC have continued to work with the London CIV Management Team on the proposals for the London CIV financial plan and budget.
3. Other key areas for discussion for the meetings have surrounded the global equity procurement, developments for fixed income, how and when infrastructure should be progressed and stewardship of investments.

Global Equities

4. Further to the update provided to this Committee in December on the global equities procurement, the IAC received a presentation from LCIV and briefing notes on the shortlisted managers and those being put forward for recommendation to the LCIV Board. A survey of Fund views in respect of likely future global equity product requirements was also reviewed and consideration given to the timing of sub-fund openings.
5. LCIV provided a presentation setting out the findings of the global equity selection process, setting out the rationale for manager selection including fee scales and performance. Key points arising from the meeting were:
 - i. Agreed that the Committee will note the recommendations from the CIV, although clearly the decision on the appointment remains with the CIV Board.
 - ii. The paperwork provided was very helpful and that it was evident that the exercise had been a very thorough process with London Fund involvement from the GE sub-group.
 - iii. The involvement of the global equity working group comprising a number of borough officers has been a crucial element in the procurement process.
 - iv. Results from the survey of Local Authority Pension Funds would indicate that there is strong demand for global equity income strategies, with reasonable demand for sustainable equity, emerging market and value strategies.
 - v. The IAC were keen to understand in more detail the decision making process following the selection and how soon strategies would be available for Funds to invest.

- vi. Comments received from an adviser involved in the procurement process were supportive of the selected managers for the respective investment strategies.
- vii. The IAC sought assurances that the selection process for managers had included their general approach to environmental, social and governance factors, which the global equity sub-group were able to confirm.
- viii. There was some concern from the IAC about how the relationship with existing managers would be managed where these had not been selected and this was to be raised in correspondence.
- ix. Questions were raised over how Funds would transition from existing managers and whilst this would be a matter for individual Funds following decisions at Committee on the investment strategy selection, the CIV was working with the National Frameworks group to look at a procurement exercise for transition managers.
- x. It was agreed that the Chair of the IAC should compile a letter and circulate for comment setting out the views of the IAC on the global equity process to be sent to the Chair of the CIV Board (a copy of which is attached in the Annex to this report).
- xi. The IAC were also keen to understand how details of the new investment strategies and managers would be disseminated to the London Funds to enable them to make informed decisions and look forwards to seeing these details including information days and briefing notes.

Fixed Income / Cashflow Products

- 6. Members will recall that the IAC has also previously asked the CIV to bring forwards work in this area in acknowledgement of the pressure that some Funds are facing increasing pressure to find secure income streams to meet cashflow needs. The IAC have reviewed the results of a survey alongside participating in a dedicated fixed income / cashflow seminar organised by LCIV, which was well attended and received very positive feedback. Feedback from that seminar and the survey should now feed into the work being the sub-group and the CIV to come forward with proposals in this area and the IAC look forward to working with the CIV and hearing of the progress of this project.

Stewardship

- 7. The IAC Stewardship Working Group has also been working closely with the CIV to review the requirements of the new Investment Strategy Statements that Funds are required to publish by 1st April, which include how they will approach Pooling, ESG issues and Voting. The IAC considered this at its meeting in January and agreed that the wording be circulated to all London Funds. Whilst acknowledging that it is for individual Funds to determine these policy matters, the IAC recognise that it would be helpful to have a reasonably cohesive approach in order to avoid too many conflicting priorities which make delivery of such policies unrealistic for the CIV to implement at a pool level.
- 8. The IAC also considered the draft Stewardship Code Compliance Statement for the CIV, which had also been reviewed and agreed by both the Officer and Member Stewardship Working Groups.

9. The IAC also discussed the Stewardship Seminar being organised by the CIV and input into the agenda.

Infrastructure / Housing

10. The IAC reviewing current allocations in this area note that currently London Funds have less than 1% invested in infrastructure. It is recognised that the asset class itself means very different things to different people covering a whole range from established infrastructure which produce consistent income streams such as utility companies to green field projects which are effectively 'holes in the ground' and it is perhaps essential to understand where Funds are in this area in terms of the risk/reward profile that they are looking for.
11. The IAC acknowledged that some initial work has been done in the area of infrastructure including a discussion paper produced by Hermes and a couple of specific deals which have been shared with some of the London Funds.
12. The IAC received a report on social housing which had been arranged by one of the London Funds and whilst acknowledging that it could be of interest to some Funds, it may have a limited appeal to the wider group and there was concern expressed that any further development on this area by the CIV at this time could deflect resources from other ongoing key projects. It was however, recognised that some Funds may wish to pursue investments in this area on their own.
13. The IAC have discussed how much of a priority infrastructure and housing should be for the CIV. Whilst recognising that some Funds may be keen to see opportunities in this area, the IAC is also conscious that Funds have significant requirements for fixed income/cashflow products and for the global equity options and have concerns that these high demand areas to meet Fund needs, might be impacted by diverting CIV resources at this time into infrastructure. The IAC are of course mindful that Funds may well look to allocate to this area, but these are likely to be relatively small proportions compare to their need for fixed income and global equities products. The IAC are keen to engage with Members to understand the extent of the demand for infrastructure and housing and if this to be an area of priority for the CIV, what type of investments are required and how much of an allocation across London is likely to be invested in this area over the next year or whether this could receive more of a focus once some of the other key projects have been delivered.

Additional Items

14. **MiFID II** - The IAC encouraged Funds to respond to the MiFID II consultation and noted the response submitted by the CIV to this. They received an update at the January meeting which covered the establishment of a working group at a cross-pool level to work closely with the FCA to see if changes can be made to the criteria to assist with the opt-up criteria for LGPS Funds. A volunteer from the IAC will also be sitting on this group and reporting back.
15. **Reporting and Transparency** – The IAC has established a further working group to work closely with London CIV to develop comprehensive Reporting Framework to meet the needs of the London Funds in both statutory and wider reporting and received feedback from the first meeting of the group.

16. **Passive Management** – The IAC reviewed the draft proposals for the passive fee management charge by the CIV and proposed some amendments, which are being included in the proposals before this Committee.
17. **Academies** – At its last meeting the IAC reviewed a note regarding Academies and ongoing discussions with the Department for Education. This raised a number of concerns for Funds including the potential for academies to be taken out of Local Authority Pension Funds into a separate central Academy Pool. This could cause issues for Funds in terms of funding levels, cashflow and staffing and could also promote faster conversions. Whilst this may not at first glance appear to affect LCIV, it could ultimately impact on the level of assets that would be available to transition into the London CIV and into other Pools being established around the Country affecting delivery of the Criteria and Guidance set out by Government.
18. **Actuarial Valuation** – The IAC has been working closely with the Society of London Treasurers to collate the actuarial valuation results via a survey and has reviewed updates at the IAC meetings. Given that there had been some major concerns going into the valuation period around what funding would look like, the results that have come through in the survey have actually painted a slightly better position than many had feared. Funding positions have generally improved, deficit recovery periods shortened and contribution increases minimised.
19. **Governance Review of the London CIV** – Treasurers represented on the IAC have also been working closely with the CIV to look at the scoping of the governance review to ensure that it covers key areas including but not limited to the committee structures, roles and responsibilities, composition and the key decision making processes. The IAC treasurers look forwards to working with the CIV feeding into the review as required and to considering the findings in due course. The scoping document is due to be presented to Leaders Committee for consideration in due course.
20. **Future work** – The IAC will continue to work closely with the CIV on key projects to help ensure that they are able to deliver the investment strategies that the Funds need to meet their requirements. In recognition of this the IAC have requested a 12 month work plan for consideration at the next meeting in February.

Recommendations

21. The committee is recommended to:
- i. Note the contents of this report

Financial implications

22. There are no financial implications for London Councils

Legal implications

23. There are no legal implications for London Councils.

Equalities implications

24. There are no equalities implications for London Councils

Annex A – Letter to the Chair of LCIV from the Chair of the IAC

Baron Kerslake

Chair

London CIV

Mr Ian Williams

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Date: 26th January 2017

**Letter from IAC regarding Global Equity
Procurement to the Investment Oversight Committee and Board**

Dear Baron Kerslake,

As Chair of the Investment Advisory Committee (IAC), I wanted to write to you and the Board to feedback from the IAC in respect of the recent global equity tender that has been undertaken by the CIV on behalf of London Borough Pension Funds.

At our last IAC meeting held in December 2016, the IAC received a presentation setting out the preferred manager selections for the global equity strategies. The Committee wanted to emphasise to both the Investment Team at the CIV and the Global Equity Working Group of the IAC, how impressed we were with the process of the procurement, the fact that they had been kept informed of progress on a monthly basis and it was clear that an extensive amount of work had clearly been undertaken. It is clear that this has been a very extensive exercise requiring significant resource dedicated to delivering the best outcomes for London Funds. In particular it was felt:

- There was clear recognition that global equities was by far and away the largest asset class across London and whilst the CQC approach has delivered for a number of London Funds, there are others who have not been able to participate in the early stages because their managers were part of the process on early on-boarding. Therefore it was going to be helpful to have a wider range of managers to choose from, particularly in the global equity income and sustainable space where funds currently don't have much exposure. A number of funds have held off undertaking their own procurement exercise awaiting the outcome of the CIV procurement programme and are keen to see new opportunities as soon as possible.

- The inclusion of a dedicated group of pension managers on the global equity sub-group provided assurance that the views of funds are being taken into account as well as being able to confirm the robustness of the process for Funds.
- This has been a significant exercise and the IAC wanted to acknowledge the amount of work that has been undertaken by the CIV Investment Team in delivering a detailed robust exercise on behalf of London Funds
- The views of the selected managers from the IAC were in the majority supported by one of the leading LGPS consultants across London, who had been involved in the initial stages of the procurement exercise. It is recognised that other consultants will need to be briefed on the chosen managers in order to support the selections at Pension Committee meetings.
- Going forwards the IAC are keen to understand the decision making process once the preferred managers have been selected. They understand their role in the decision process is to satisfy themselves of the robustness of the decisions being put forward, which they have been and now want to understand how the final decision is made so that fund openings can be progressed swiftly.
- The IAC are also keen to understand in more depth how the transition process to the new managers will operate, in particular how the relationship with long standing managers will be managed where they haven't been selected for particular strategies. The IAC acknowledge the CIV have agreed to be part of the National Framework for Transition managers and recognise that this will facilitate the transition process for London Funds, they are also keen to understand in more depth the transition costs that Funds will incur when moving managers, particularly where this would be occurring outside of the normal investment strategy process. Funds are also still keen to understand how long standing relationships will be managed with unselected managers. The IAC are also keen to understand from the IOC and Board what their views are regarding why Funds would undertake a transition from existing managers to the new ones on the CIV platform. In addition, we recognise the need for pace so that the investment vehicles available meet pension fund requirements.
- Whilst recognising that the Fund's survey had suggested that historic performance was an important factor, they were also keen to understand in more detail how they would deliver performance going forwards. It is acknowledged that this is covered in the detailed briefing notes and was further illuminated in discussions at the Committee meeting, but some more detail around this would be helpful as will the opportunity to hear from the managers direct.

- The Committee were also keen to understand the Environmental, Social and Governance aspects of each of the selected managers, if these could be covered in the manager notes, this would be a helpful addition for Funds that place greater emphasis on these aspects. This should also cover whether the manager has particular approach to fossil fuel and low carbon.

In conclusion, the IAC would like to express their appreciation for the work put in by the Investment Team for ensuring the involvement of the Boroughs in the procurement exercise and for delivering a detailed robust process to the IAC. There are naturally a number of concerns given that this is the first time the process has been undertaken and some clarity about the governance process from here. Borough funds are really keen to ensure that the pace of providing the investment vehicles is considered a priority and that the CIV focuses on doing the high priority areas of work. Finally, it is clear to members of the IAC that the scheduled governance review is important to the London Boroughs to ensure that the confidence is maintained in order for the transition of further £billions of the Pension Fund Investments.

Yours sincerely,

A handwritten signature in black ink that reads "Ian Williams". The signature is written in a cursive style with a horizontal line underneath the first name.

Ian Williams

Group Director of Finance and Corporate Resources
London Borough of Hackney
Chair of the IAC