

**Report for:** Pensions Committee 27<sup>th</sup> March 2017

**Item number:** 18

**Title:** Currency Hedging Implementation

**Report authorised by:** Tracie Evans, Chief Operating Officer (COO)

**Lead Officer:** Thomas Skeen, Head of Pensions  
[thomas.skeen@haringey.gov.uk](mailto:thomas.skeen@haringey.gov.uk) 020 8489 1341

**Ward(s) affected:** N/A

**Report for Key/  
Non Key Decision:** Non Key decision

## 1. Describe the issue under consideration

- 1.1. At the February 9<sup>th</sup> 2017 Pensions Committee meeting, it was agreed that the committee will implement currency hedging on 50% of the Fund's developed market overseas exposure.
- 1.2. This report brings back a finalised implementation plan for the Committee's approval.

## 2. Cabinet Member Introduction

- 2.1. Not applicable.

## 3. Recommendations

- 3.1. That the Committee note and agree to the content of Appendix 1 – a currency hedging implementation plan from Mercer, the Fund's Investment Consultant. The plan is the hedge 50% of the Fund's exposure to developed market overseas equity in three tranches over a 2 month period. This utilises the existing relationship with Legal and General Investment Management, to ensure that costs are kept to a minimum.
- 3.2. That the Committee gives delegated authority approval to the Chief Operating Officer to speed up the currency hedging implementation, should Sterling fall to the 'trigger rate' of 1.20 compared to the US dollar, (a historic low not breached since 1985).

## 4. Reason for Decision

- 4.1. The Fund has benefited from the decline in sterling against the US dollar and other currencies. Currency hedging has been agreed by the committee to bank some of the gains made by the fund in the past 12 months due to the fall in sterling against other major currencies.
- 4.2. Legal and General Investment Management (LGIM) could monitor currency movements for the fund and speed up the currency hedging switches, should the trigger rate of 1.20 be breached: however this will be more costly than if officers monitor this position in house, (currency rate information is readily, publicly available). It is therefore proposed that officers, acting under delegated authority, will initiate this speed up in the currency hedging process should the trigger rate of 1.20 be breached.

## **5. Other options considered**

- 5.1. None

## **6. Background information**

- 6.1. One of the key roles of the Committee is setting of the Fund's asset allocation strategy. This sets out the desired allocation to various asset classes such as equities, bonds, property, etc. Different asset classes have different expected outcomes in terms of future returns, but together should provide the asset outperformance level required to enable the Fund to meet its future obligations to scheme members.
- 6.2. The current strategy has a high allocation to equities, property etc, whose values have a strong correlation to economic growth, the Committee is focused on funding the promised benefits primarily from investments returns while seeking to stabilise employer contributions. The Committee is required to keep the strategy under review considering the impact of funding levels and market conditions.
- 6.3. It is estimated that the Fund has gained up to £140m in value as a result of the fall in the value of Sterling against all major currencies since the Brexit vote. Sterling is at a historic low against other major currencies, so it is likely that it will start to appreciate at some point in the future: this will erode gains that the fund's investment assets have made in the past 12 months.
- 6.4. As the uncertainty around the implementation of Brexit clears and investors confidence in the economic growth of the UK gradually returns, Sterling will likely start to recover some of the losses incurred in the post Brexit vote period.
- 6.5. Additionally, the award of a renewable energy mandate, both of which are non-Sterling denominated during commitment/investment period

(up to 5 years), further highlights the need to have some form of protection should Sterling start to appreciate in value.

- 6.6. It is estimated that the proposed hedging strategy set out in Appendix 1 will cost the fund approximately £68k in additional fees per annum (based on asset values as at 31/12/17). This compares very favourably to the £140m of gains the fund has made since the depreciation of sterling following the Brexit vote.
- 6.7. One off transaction costs for the currency hedging switch are estimated to be in the region of £35k.

## **7. Contribution to Strategic Outcomes**

7.1. None.

## **8. Statutory Officers comments (Chief Finance Officer (including procurement), Assistant Director of Corporate Governance, Equalities)**

### Finance and Procurement

8.1. The Fund has benefitted from a period of significant growth in equities and index linked gilts due mainly to its overweight position in equities. It has also benefited from the fall in sterling versus other major currencies. The currency hedging implementation will partially insure the fund against the risk of sterling once again rising against other currencies and thus eroding gains made in the Fund's investment portfolio.

### Legal

8.3 Under Regulation 11 of the of the Local Government Pension Scheme (Management and Investment Funds) Regulations 2009 the administering authority must formulate a policy for the investment of its fund money and invest in accordance with that policy and the authority can vary its investment.

8.4 Members must in agreeing the currency hedging strategy set out in this report do so in accordance with the Fund's policy, investment statement and the funding strategy.

8.5 Members should note that Regulation 11 will no longer be effective when the authority first publishes its investment strategy statement under Regulation 7 of the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016.

### Equalities

8.6 There are no equalities issues arising from this report.

## **9. Use of Appendices**

9.1. Confidential Appendix 1 – Currency Hedging Implementation

## **10. Local Government (Access to Information) Act 1985**

10.1. Not applicable.