

Report for: Pensions Committee and Board 11 July 2019

Title: Emerging Market Equity

Report authorised by: Jon Warlow, Director of Finance (S151 Officer)

Lead Officer: Thomas Skeen, Head of Pensions, Treasury & Chief Accountant
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Ward(s) affected: N/A

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

1. Describe the issue under consideration

- 1.1. This paper seeks to update the Committee and Board regarding the implementation of investment in a low carbon option for the fund's emerging market equity portfolio, which was discussed by the Committee and Board at the last meeting in March 2019.

2. Cabinet Member Introduction

- 2.1. Not applicable.

3. Recommendations

- 3.1. That the Committee and Board consider the report, and information outlined in Confidential Appendix 1, including any verbal updates or advice provided by the Fund's investment Consultant, Mercer, in the meeting.
- 3.2. That the Committee and Board agrees to switch its Emerging Market Equity holdings into a low carbon index linked fund.
- 3.3. That the Committee and Board delegate power to the Head of Pensions, Treasury & Chief Accountant to take all necessary steps to effect this change, including completion of necessary paperwork and to update and republish the fund's Investment Strategy Statement to be consistent with this change.

4. Reason for Decision

- 4.1. At the last meeting the Pensions Committee and Board agreed it was minded to move its emerging market equity holdings into a low carbon version of the fund it invests in, subject to final confirmation being received regarding the implementation specifics of this. These details are now attached in Confidential Appendix 1 for the Committee and Board's consideration.
- 4.2. Mercer, the Fund's Investment Consultant produced a paper for the Committee and Board for the March 2019 meeting providing a review of three alternative options to the fund's current emerging market equity strategy. This is appended at Confidential Appendix 2 for reference.

5. Other options considered

- 5.1. None

6. Background information

- 6.1. The most important investment role for the Committee and Board is the setting of an asset allocation strategy. This is the desired allocation to the various asset classes e.g. equities, bonds, property, cash etc. Different asset allocations will have different expected outcomes in terms of future returns and also the predictability of returns.
- 6.2. In setting the current strategy that has a high allocation to equities, whose values, as an asset class, have a long term correlation with economic growth, the Committee and Board is focused on funding the promised benefits primarily from investment returns while seeking to minimise / stabilise employer contributions. The Committee and Board is required to keep the strategy under review considering the impact of funding levels and market conditions.
- 6.3. The fund has undertaken regular reviews of its equity holdings in recent years, both reducing overall allocations, and utilising alternative indexation, currency hedged funds, and low carbon options, with the aim of managing overall risk for the fund. Half of the fund's developed market equity is currently invested in a low carbon fund.
- 6.4. The Fund has an overall 6.66% allocation to emerging market equity. Although the percentage of total fund holding has varied as the fund has reduced exposure to equity over time, these holdings have been passively invested in the same emerging markets indexed fund since 2013/14. The value of these holdings was £99.6m as at 31.03.19.
- 6.5. The report produced by Mercer, attached at Confidential Appendix 2, outlines 3 potential options which the fund could explore utilising in the

future to reduce carbon exposure within its emerging markets portfolio. The performance figures, and carbon exposure figures were discussed in the March 2019 meeting by the Committee and Board. The option recommended will reduce the fund's emerging market equity carbon intensity by c. 63%.

- 6.6. The fund has a commitment to investing in a manner which not only secures sufficient returns to meet the fund's strategy to increase the overall funding level, and keep employer contributions to a minimum, but which also takes serious consideration of Environmental Social and Corporate Governance (ESG) factors. The fund's Investment Strategy Statement states that *'The Fund believes that further reduction in exposure to fossil fuel industries will reduce risk and secure stronger returns for the fund over the long term.'* The Committee and Board considered a number of options for its Emerging Market equity portfolio at the previous meeting, and considered decarbonising the fund's investments further as part of an ongoing project to review the fund's exposure to risk, and make positive and proactive changes, wherever these are judged to be consistent with the fund's overriding fiduciary duties.
- 6.7. The table below outlines the Fund's current and proposed equity portfolio (allocations refer to percentage of total equities).

Portfolio	Current Allocation	Proposed Allocation
Global Equity - Multi Factor Index	42.6%	42.6%
Global Equity - Developed Market Low Carbon Target Index	42.6%	42.6%
Emerging Markets Index	14.8%	-
Emerging Markets - Low Carbon Target Index	-	14.8%

- 6.8. If the fund were to transition to the emerging market low carbon strategy, the carbon intensity of the fund's overall equity portfolio would be expected to be roughly half that of a global market cap portfolio.

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 enjoyed strong returns in recent years primarily from rising equity valuations. The Pension Committee and Board's responsibility is to look to the long term when setting an investment strategy, ensuring an appropriate degree of diversification.
- 8.2. Whilst commitment to ESG issues is clearly a key consideration for Haringey Pension Fund, the overriding aim of the fund's investment strategy must be to improve the funding position with the aim of reaching fully funded status, whilst maintaining stability of employer contributions. Any changes to the Fund's investment strategy must be consistent with these principles. The details of the proposed change are judged to be consistent with the Fund's statutory duties.

Legal

- 8.7 The Council as administering authority for the Haringey Pension Fund has the power to invest fund monies as set out in Local Government Pension Scheme (Management & Investment Funds) Regulations 2016.
- 8.8 Any changes to the allocations must comply with the Pension Fund Investment Strategy Statement. There are no legal implications in respect of the recommendation.

Equalities

- 8.5 There are no equalities issues arising from this report

9. Use of Appendices

- 9.1. Confidential Appendix 1 – Emerging Market Equity Implementation Details
- 9.2. Confidential Appendix 2 – Emerging Market Equity Review (of March 2019)

10. Local Government (Access to Information) Act 1985

- 10.1. Not applicable.