

Report for: Pensions Committee and Board – 4 March 2020

Title: Investment Strategy Considerations on the Strategic Asset Allocation to Gilts and/ or the London Fund

Report authorised by: Thomas Skeen, Assistant Director of Finance (Deputy Section 151 Officer)

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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. In July 2020, The Pensions Committee and Board (PCB) considered a report to review the Fund's investment strategy. At the time, the Fund deferred the decision on investment in residential property until the London CIV's had set up the London Fund, a fund that is expected to be largely invested in residential real estate.
- 1.2. The PCB, at the July 2020 meeting, also agreed to reduce allocation to gilts from 15% to 10% and considered a proposal to earmark up to a further 5% of allocation to gilts for future investment in residential property through the London Fund. A decision on whether to switch back to index linked gilts would be deferred until the government's position on RPI is clearer was deferred to a future meeting.
- 1.3. This paper considers these outstanding issues including proposals on how the PCB should address these issues.

2. Cabinet Member Introduction

- 2.1. Not applicable.

3. Recommendations

The Pensions Committee and Board is asked:

- 3.1. To note the Investment Strategy Considerations paper, included as Confidential Appendix 1 to the report.

- 3.2. To approve a change to the Pension Fund's strategic asset allocation within the Investment Strategy Statement, as shown in Confidential Appendix 1 to the report, namely to:
- Allocate between 3% and 5% to the London Fund;
 - Reduce the allocation to gilts by 3% - 5%; and
 - Switch the current/residual investment in fixed interest gilts back to indexed linked gilts.
- 3.3. To delegate authority to the Assistant Director of Finance to implement the above changes (if approved), after consultation with the Chair of the Pensions Committee and Board and Independent Advisor and after taking professional advice from the Pension Fund's Investment Consultant.
- 3.4. To delegate authority to the Assistant Director of Finance to update and republish the Pension Fund's Investment Strategy Statement consistent with decisions made above.

4. Reason for Decision

- 4.1. The PCB expressed an interest in a strategic allocation to residential property through the London Fund at the July 2020 review of the investment strategy but deferred a final decision until the London Fund has been launched.
- 4.2. The Committee and Board as part of its consideration of the Fund's allocation to gilts reviewed a proposal to earmark up to 5% of revised allocation to gilts for a future decision on whether to allocate to residential property.

5. Other options considered

- 5.1. The Fund could opt not to invest in the London Fund and maintain its current 10% allocation to gilts. The Fund could also opt to continue to invest in fixed interest government bonds rather than switch to indexed linked bonds.

6. Background information

Gilts Allocation

- 6.1. The PCB had an initial discussion about the Fund's allocation to index linked gilts in January 2020 when it was decided to switch to fixed interest gilts on a temporary basis until the uncertainty around the RPI consultation was settled.
- 6.2. The Fund's 15% allocation to gilts was considered high and the PCB decided as part of the July 2020 review of the Fund's investment strategy to reduce allocation to gilts to 10% and possible further reduction of 5% if the Fund decided to invest in the London Fund.

The London Fund

- 6.3. The PCB has discussed residential property on several occasions because this asset class amongst other things has the potential to have strong positive responsible investment credentials. As part of the discussion on investment in residential properties, a training session on the asset class was provided to members of the PCB in February 2020 and a decision on potential investment in the asset through the London Fund was deferred to a future meeting once the London Fund has launched.

Gilts/London Fund

- 6.4. The London Fund is a joint venture between the London CIV and the Local Pensions Partnership (LPP) another Local Government Pension Scheme (LGPS) pool that seeks to invest predominantly in residential properties, but the fund would also invest in infrastructure along with a small allocation to growth capital (i.e. private equity). As part of the consideration at the July 2020 investment strategy review, the options presented to the Committee included proposals for a up to a further 5% from the allocation to gilts be earmarked for a future decision on whether to allocate to residential property.
- 6.5. It was also made clear at the July review that a final decision regarding residential property will be dependent on LCIV's progress in setting up the London Fund and that once the London Fund has launched a further review of the Fund's strategic asset allocation will be undertaken, and recommendations put to the PCB to either change or maintain the current strategic allocations to gilts/residential property.

7. Contribution to Strategic Outcomes

- 7.1. Not applicable

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

Finance and Procurement

- 8.1. As highlighted in previous meetings, given the increasing ongoing costs of servicing LGPS pensions, de-risking the Fund's investment strategy at this time would not be appropriate. The report of Mercer, attached as confidential appendix, presents options that, if implemented, will likely result in increased expected returns without a commensurate increase in overall risk in the Fund's investment portfolio.

Comments of the Head of Legal and Governance (Monitoring Officer)

8.2. Under Regulation 7 of the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016 the administering authority must, after taking proper advice, formulate an Investment Strategy (in accordance with guidance issued from time to time by the Secretary of State). It must also keep this under review (at least every three years) and if necessary revise it.

8.3. The Investment Strategy must include:

- a) a requirement to invest fund money in a wide variety of investments;
- b) the authority's assessment of the suitability of particular investments and types of investments;
- c) the authority's approach to risk, including the ways in which risks are to be assessed and managed;
- d) the authority's approach to pooling investments, including the use of collective investment vehicles and shared services;
- e) the authority's policy on how social, environmental and corporate governance considerations are taken into account in the selection, non-selection, retention and realisation of investments; and
- f) the authority's policy on the exercise of the rights (including voting rights) attaching to investments.

8.4. The Investment Strategy must set out the maximum percentage of the total value of all investments of fund money that will be invest in particular investments or classes of investment. Therefore, any decision made by the PCB must not exceed the maximum percentage for that particular or class of investment. The decision in this report is to change the percentages for the particular and classes of investment mentioned in the recommendation.

Equalities

8.5. Not applicable.

9. Use of Appendices

9.1. Confidential Appendix 1: Investment Strategy Consideration – Gilts/London Fund

10. Local Government (Access to Information) Act 1985

10.1. Not applicable.