

**Minutes of the Pension Fund Investment Sub-Committee
meeting held on 18 December 2017**

Present:**Members**

Councillors John Horner, Corinne Davies (replacing Alan Webb for this meeting), Bill Gifford (Vice Chair), Wallace Redford and Bob Stevens (Chair)

Officers

John Betts – Head of Finance
Mathew Dawson - Treasury and Pension Fund Manager
Aneeta Dhoot – Senior Finance Officer
Chris Norton – Strategic Finance Manager
Jane Pollard – Legal Services Manager
Sukhdev Singh – Senior Finance Officer
Paul Williams - Democratic Services Team Leader

Invitees

Rachel Elwell – Border to Coast Pensions Partnership
Emma Garrett – Hymans Robertson
Peter Jones – Independent Investment Adviser
Paul Potter – Hymans Robertson
Karen Shackleton – Independent Investment Adviser
Richard Warden – Hymans Robertson

Observers

None

No members of the public attended.

1. General**(1) Apologies for absence**

Councillor Alan Webb (Replaced for this meeting by Councillor Corinne Davies)

(2) Members Disclosures of Pecuniary and Non-Pecuniary Interests

None

(3) Minutes of the previous meeting held on 11 September 2017

The minutes of the meeting held on 11 September 2017 were agreed as true and correct records and were signed by the Chair.

2. Investment Performance

Mathew Dawson (Treasury and Pension Fund Manager) introduced the report stating that following another successful quarter the pension fund value stood at £2,039.4m at 30 September 2017, this being an increase of 1.32% on the previous 3 months. Referencing table 1 it was explained that a certain amount of rebalancing

has been undertaken, that the allocation to government bonds has now been sold and that there has been a change in the allocation of equity. A certain cash weighting will need to continue to be held. This will be drawn down throughout the life of the fund. Members sought assurance that 1.5% cash was reasonable. This was given by Paul Potter (Hymans Robertson) who stated that there should be no concern for cash assets up to 2%. The Sub-Committee was informed of the impending withdrawal of a major employer from the fund. This will result in the loss of £15m as a cash withdrawal from the fund. Assurance was provided that whilst not an insignificant development it should have no direct impact on the fund.

Regarding table 2 (page 3 of 6) it was noted that JP Morgan underweight as income is distributed back to the fund not re-invested. However the Sub-Committee learned that this has been topped up with the sale of gilts and will be increased temporarily with the sale hedge funds due as cash post February 2018.

Fund Manager performance was explored by members. That of MFS and Threadneedle was noted to be markedly below that of others. However figure 4 showed that both these managers had performed well since 2014. Members were informed that quarterly figures can be misleading. Performance should be monitored over a two year period at least. Schroders Property and Threadneedle Property were acknowledged as having performed well, outperforming expectations. Members were informed that having the right active managers can be the key to success.

Mathew Dawson observed that the benchmarking performance placed before the committee did not contain all the information collected. Analytics are commissioned by the fund as part of a debate on whether to use active or passive managers. Detailed data was considered necessary as it is not enough to simply know if the agreed benchmark is being met. It was considered more important to know whether fund managers were skilful in buying and selling stocks. There is a considerable amount of data provided to the fund by Analytics. This can be made available to the Sub-Committee should it so wish.

Peter Jones (Independent Investment Adviser) requested that the Sub-Committee bear in mind the very good performance of the fund in recent years.

Resolved

That the Pension Fund Investment Sub-Committee notes the fund value and investment performance for the first quarter of 2017/18 to 30 September 2017.

3. Appointment of Private Debt Manager

Councillor Bob Stevens (Chair of the Pension Fund Investment Sub-Committee) introduced this item explaining that interviews had been held on 1 December 2017 for the role. Members were reminded that whilst the interviews had resulted in two appointments it was still necessary for the Sub-Committee to ratify that decision. Mathew Dawson stated that the decision had been taken to assign Alcentra and Partners Group £50m each adding that MJ Hudson had been appointed to ensure legal and operational due diligence.

Resolved

That the Pension Fund Investment Sub-Committee ratifies the appointment of Alcentra and Partners Group as Private Debt Managers.

4. Pooling Verbal Update

The Chair welcomed Rachel Elwell (CEO of BCPP) to the meeting. Having introduced herself and shared her credentials Rachel proceeded to update the Sub-Committee on progress with the setting up of BCPP. The mission statement of the BCPP was noted this being “making a difference to investment outcomes for Local Government Pension Funds through pooling to create a stronger voice; working in partnership to deliver cost effective and innovative responsible investment now and into the future; thereby enabling great, sustainable performance”. That BCPP is now moving from a transition position to an operational one as a permanent company was noted. Recruitment is underway with a view to becoming operational out of an office in Leeds in 2018.

Phase one of operations will focus on asset management with the first transfers of assets happening in summer 2018. These transfers will need careful planning and an efficient process to ensure they are all undertaken smoothly. Given that it will take two to three years to become fully established it is likely that the arena in which BCPP is working will change. For this reason it will be necessary to be agile and strive to remain ahead of those changes.

The success of BCPP will be measured partly in terms of the cost savings it delivers to its 12 partner funds.

BCPP will need to pay due regard to responsible investment and governance. It will also need to ensure its resilience through the appointment of the right people.

Councillor Bill Gifford questioned whether the drive to cut fees and make savings and pressure to invest in infrastructure would undermine the independence of individual partner funds in the pool. In response the meeting was informed that liabilities will remain with the fund. Success is achieved 80% through strategic asset allocation and 20% through tactical measures eg manager selection. Ultimately the Sub-Committee will retain responsibility for strategic planning. In terms of investment in infrastructure, the Sub-Committee was informed that this can be better than some might suppose. At a general level it works well as an asset class. It provides global investment opportunities although as lead-in times are lengthy and it carries very specific risks infrastructure investment requires careful and long term consideration.

Transition to BCPP will be tightly controlled with a number of stop/go decisions required over the next few months. The Board will need to be comfortable with progress as will the Regulator. Those assets that transfer in June 2018 will mark the first testing point. With £47bn in assets BCPP should achieve a strong voice.

Members asked whether the establishment of BCPP will result in an increase in staffing. It was explained that there will be 70 staff employed by BCPP. Those funds that currently have internally managed teams will TUPE them over. Internal fund management will increase over time. This will result in a reduction in fees being paid to external fund managers. For example if the equity fund is managed internally it

will no longer be necessary to pay fees to HarbourVest. Members were also informed that as BCPP is not a large profit-based commercial concern it will not have the major overheads that the major fund managers have. This will result in further savings.

The various pools across the country are currently cooperating. However it may be that as they become established that level of cooperation will decline.

Leeds is considered to be a good location for the BCPP headquarters. The city has a strong financial industry and to date its location away from London does not appear to have deterred good quality people from wishing to work there. However, it may be that when filling investment roles the location might provide a challenge.

Karen Shackleton (Independent Investment Adviser) observed that that cost savings are to be made via procurement. For example the process used for the appointment of the Private Debt Manager. Karen requested that she and her fellow independent advisers be kept firmly in the loop when correspondence is being sent out and decisions made. This was duly noted.

It was explained that the production of a prospectus is required as part of the Authorised Contractual Scheme. This in turn will need to be approved by the Financial Conduct Authority.

In terms of reporting of performance it was acknowledged that whilst a common approach across the 12 partner pools would be desirable, some variation is inevitable. The key around monitoring and reporting is to get the accounting right. Warwickshire is not as data-heavy as some pension funds plus it also has a custodian platform of which BCPP will be a part. As BCPP will manage assets externally it will be necessary to have strong data management. In addition transaction costs will need to be closely and accurately monitored.

Training for Sub-Committee members was regarded as very important. Members agreed that this should be given further attention.

Resolved

That the Pension Fund Investment Sub-Committee notes progress to date with the Border to Coast Pension Partnership

5. MIFID II Verbal Update

Mathew Dawson informed members that on Wednesday 13 December the County Council had learned that it was now classified as a professional investor under MIFID II by each of its fund managers. One exception was JP Morgan who have decided that the pension fund is protected under the rules applied by the "Undertakings for the Collective Investment of Transferable Securities" (UCITS).

It is expected that over the next few months many more managers will request the fund to opt-up in order that prospective managers can continue to engage with officers.

One area identified for development is training. The fund has been advised that it needs to maintain a more formal training record and that it should have regular training on a quarterly basis. Members acknowledged that MIFID II had encouraged pension funds to reflect on and improve their practices.

Resolved

That the Pension Fund Investment Sub-Committee notes the latest position regarding MIFID II.

6. Results from Training Survey

Karen Shackleton briefed the Sub-Committee on the results of the recent training survey. Seven questions had been asked. The results can be summarised as follows.

1. Pensions legislative and governance context

Members demonstrated a clear knowledge base with a good understanding of MIFID II. A lower score was achieved for LGPS Regulations and Legislative Framework.

2. Pensions accounting and auditing standards

A good working knowledge was demonstrated although that around accounts and audit regulations was weaker.

3. Financial services procurement and relationship management

Scores were high in this area.

4. Investment performance

Results suggest that post pooling engagement and monitoring may require more support.

5. Risk management

More training is required in this area especially around what influences risks and what can be done to mitigate against it.

6. Financial markets and products knowledge

Scores were high in this area.

7. Preferred training method

Members expressed a desire to attend more training days, undertake internal training and to have training before meetings. Online training scored low.

Regarding training Mathew Dawson suggested that short sessions prior to the commencement of meetings may not be sufficient to meet members' requirements or those of MIFID. It was agreed that the matter be discussed in greater depth at the Sub-Committee's March 2018 meeting.

Resolved

- 1) That the Pension Fund Investment Sub-Committee notes the results of the survey.
- 2) That the agenda for the March 2018 meeting of the Pension Fund Investment Sub Committee include an item on training.

7. Investment Guiding Principles

During the introduction to this item it was emphasised that the guiding principles (that resulted from the MIFID II exercise) are not mandatory or definitive but serve to assist in decision making. Mathew Dawson observed that principles 1 -4 are the most significant. Of the remaining guiding principles it was noted that with reference to number 9, had a \$ based manager been appointed as Private Debt Manager it would have been necessary to consider currency hedging. With regards principle 13, quarterly performance reports cover too short a period. A more accurate indication of performance will be obtained over a 3 to 5 year period. Finally with regards principle 15, whilst it is recognised that BCPP will be investing in line with the agreed strategy further advice will be required especially regarding strategic asset allocation.

Councillor Bill Gifford, referred to paragraph 1.2 of agenda item 8 which states, "BCPP will engage with companies on environmental, social and governance issues and exercise its voting rights at company meetings". Members agreed that this should form the basis of a further guiding principle concerning responsible investment.

Regarding currency risk members were informed that equity managers do not manage this. Rather they have to accept that there is volatility in this area.

The Sub-Committee was informed that fund managers' contracts are not normally terminated owing to short term underperformance. They will, however be terminated if managers do not act on instructions and do what they are told.

Resolved

That the Pension Fund Investment Sub-Committee

1. approves the investment guiding principles for inclusion as an appendix in the fund's Investment Strategy Statement.
2. agrees that a further principle be included at number 16 stating, "BCPP will engage with companies on environmental. Social and governance issues and exercise its voting rights at company meetings".
3. agrees that the guiding principles be presented to the next meeting of the Sub-Committee along with any amendments/additions.

8. Responsible Investment and Share Voting

Following a brief introduction by the Chair the Sub Committee was informed that a voting policy is required as the pension fund has a say in how companies operate. A manifest voting system is used whereby suggestions are supplied to the fund on

which way it might choose to vote. This system has the advantage in that votes are recorded and accounted for.

The fund has a choice. It can redesign the Warwickshire Voting Policy to harmonise with BCPP or it can develop its own policies independently. Officers' advice was to align with BCPP.

The meeting was informed that the Warwickshire fund does not have its own Responsible Investment (RI) policy. Any issues around RI form part of the Investment Strategy Statement and Governance Statement. The advantage of aligning with BCPP is that the fund can benefit from its policy.

It was noted that passive managers have a different approach to responsible investment to active managers.

It was agreed that Responsible Investment needs to be good investment that brings a good return.

Resolved

That the Pension Fund Investment Sub Committee approves,

1. The BCPP Corporate Governance Voting Guidelines
2. The BCPP Responsible Investor (RI) Policy
3. The redrafting of the fund's voting policy to align with BCPP for presentation to the June 2018 meeting of the Sub Committee.

9. Any other items

None

10. Reports Containing Confidential or Exempt Information

Resolved:

'That members of the public be excluded from the meeting for the items mentioned below on the grounds that their presence would involve the disclosure of exempt information as defined in paragraph 3 of Schedule 12A of Part 1 of the Local Government Act 1972'.

11. Exempt Minutes of the Meeting held on 11 September 2017

The exempt minutes were agreed as a true and accurate record for signing by the Chair.

12. Investment Review

Paul Potter updated the Sub Committee on a number of issues that were raised at its 12 June 2017 meeting. Details of this update are set out in the exempt minute.

The meeting rose at 11.50am

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Chair