

Pensions Committee

2.00pm, Wednesday, 26 June 2019

Joint Investment Strategy Panel Activity

Item number	5.4
Executive/routine	
Wards	All
Council Commitments	Delivering a Council that works for all

1. Recommendations

The Pensions Committee (**Committee**) is requested to:

- 1.1 **note** the activities of the Joint Investment Strategy Panel during the financial year 2018/19.

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Joint Investment Strategy Panel Activity

2. Executive Summary

- 2.1 The purpose of this report is to provide an update on the activity of the Joint Investment Strategy Panel (**the Panel**) for the year to 31 March 2019.
- 2.2 To enable efficient collaboration, the three Chief Financial Officers of the Lothian, Falkirk and Fife Pension Funds are operating the Panel, which was designed to align governance for the investment of funds. It advises the Heads of Finance of the City of Edinburgh and Fife Councils and the Chief Finance Officer of the Falkirk Council.
- 2.3 The inaugural Panel meeting with all three Funds was held in August 2018 to commence work on the first investment strategy review undertaken in collaboration. In December 2018, the relevant Committee of each Fund approved its own unique investment strategy. The Panel's advice had led to the three Funds agreeing a common set of investment beliefs and investment strategies that are now expressed in common terms.
- 2.4 While the investment strategy reviews of the three collaborative Funds represented a significant piece of work, the Panel continued to oversee and advise on the performance, asset allocation and risk of the investments of Lothian Pension Fund, Lothian Buses Pension Fund (see 3.5 below) and Scottish Homes Pension Fund. The Panel and the internal team focused on the implementation of investment strategy with the gradual reduction in equities and patient accumulation of infrastructure and private debt investments being the major changes to the first two Funds. For the fully funded Scottish Homes Pension Fund, the Panel advised on asset-liability matching.

3. Background

- 3.1 The purpose of this report is to provide an update on the activity of the Investment Strategy Panel (**the Panel**) for the year to 31 March 2019.
- 3.2 To enable efficient collaboration, the three Chief Financial Officers of the Lothian, Falkirk and Fife Pension Funds are operating the Panel, which was designed to align governance for the investment of funds. It advises the Heads of Finance of the City of Edinburgh and Fife Councils and the Chief Finance Officer of the Falkirk Council.
- 3.3 Over the year to December 2018, the Panel comprised:
- the Chief Executive Officer of LPFI Limited (**LPFI**);
 - Chief Investment Officer of LPFI;
 - Independent advisors, currently Gordon Bagot and Scott Jamieson.
- 3.4 Following the resignation of the Chief Executive Officer of LPFI (effective December 2018), a second regulated investment advisor of LPFI was co-opted to the Panel pending approval of amended Terms of Reference by the Committees of Lothian, Falkirk and Fife Funds.
- 3.5 The Panel advises the Head of Finance of the City of Edinburgh Council on the implementation of the investment strategies approved by the Pensions Committee for the three pension funds for which it is responsible – Lothian, Lothian Buses (until 31 January 2019) and Scottish Homes. The Chief Financial Officer of Lothian Pension Fund also attends meetings of the Panel.
- 3.6 The Panel also advises the Head of Finance of the Fife Council and the Chief Finance Officer of the Falkirk Council on the implementation of strategy for their respective pension funds.
- 3.7 The external independent advisors on the Panel provide an important element of the governance of the investments of the three collaborating Funds - Lothian, Falkirk and Fife. Future procurement of advisors will be mutually agreed by the participating Funds ensuring that the contract end dates are staggered as previously discussed by the Committee and Board.

4. Main report

- 4.1 The Panel meets quarterly and considers all aspects of the investments of the pension funds. Regular activities include reporting to and making recommendations about investment strategy to the Committee, directing and monitoring strategy implementation and risk and advising the Head of Finance on the types of investment manager to utilise. The Panel ensures that important issues are

reviewed on a regular basis. Its agenda planning document is attached as **Appendix 1**.

- 4.2 The Panel considers the appropriate investment management structure required to implement the Fund's investment strategy and on the process for the appointment objectives and restrictions for internally managed portfolios. It monitors the risk and performance of all portfolios. Panel and the internal investment team monitor all managers on a regular basis using a traffic light system to ensure that scrutiny of portfolios is robust. Performance, continuity of investment process, philosophy, people and ownership, are considered in the monitoring process. Where there are concerns over a manager, more regular and in-depth monitoring is undertaken.
- 4.3 The primary focus for the Panel during 2018/19 has been implementation of the existing investment strategies for Lothian Pension Fund, Lothian Buses Pension Fund and Scottish Homes Pension Fund, previously agreed by Committee as well as a new investment strategy review for Lothian Pension Fund in collaboration with the Falkirk and Fife Funds.
- 4.4 Other special items have included:
- Annual Asset Class Focus Reviews for Combined Equities, Property, Other Real Assets, Private Equity, Currency Exposures & Hedging and Debt Assets;
 - Fund Strategy Focus Reviews and Annual Reviews of Investment Mandates for the Lothian, Lothian Buses, Scottish Homes and Falkirk Funds;
 - review of governance of internally managed portfolios as well as triennial reappraisals of three internal mandates;
 - evaluation of implementation of Lothian Pension Fund's Strategy 2 (MEG);
 - review of securities lending policy and implementation;
 - appraisal of investment cost benchmarking data;
 - review of Statement of Investment Principles;
 - audit of foreign exchange transaction costs;
 - analysis of members' AVC investments;
 - review of stewardship and engagement activities, including incorporation of ESG considerations into decision-making and carbon foot-printing; and
 - assessment of effectiveness of the Joint Investment Strategy Panel.
- 4.5 The Panel's self-assessment of its effectiveness is regarded as an important element of good governance. This is a formal review, undertaken every year using qualitative output from a survey questionnaire and quantitative output from independent sources of data. Both qualitative and quantitative output indicate that the Panel is operating effectively, but the survey attempts to identify areas for improvement. One such area is more concrete measurement of Panel's effectiveness by the Committee itself, and so Panel will seek more formal evidence that all key stakeholders are satisfied with the way it is operating.

4.6 Over the year, the Panel's activity has resulted in:

- a revised investment strategy for Lothian Pension Fund;
- a revised Statement of Investment Principles, including a set of investment beliefs common to Lothian, Falkirk and Fife;
- establishment of a framework of five 'Policy Groups' – Equities, Real Assets, Non-Gilt Debt, Gilts and Cash;
- continued progress in the implementation of the investment strategies of:
 - Lothian Pension Fund – increases in infrastructure and private debt exposure;
 - Lothian Buses Pension Fund – reductions in equity and increases in gilt exposure;
 - Scottish Homes Pension Fund – restructuring of the gilts portfolio to improve the match between asset and liabilities;
- introduction of a fourth employer strategy for Lothian Pension Fund when Lothian Buses Pension Fund merged with it;
- agreement on operational changes to enhance synergies with collaborative partners, such as streamlining agenda planning (timing and content) across the governance structure;
- agreement on areas where mutual benefits can be achieved, such as in joint tenders for services;
- continued evolution of the analysis of ESG integration and of climate change impacts across the Fund, resulting in a PRI Assessment Report that rated Lothian at or above median in all modules for its approach to Responsible Investment.
- additional risk and style analysis now being available to inform ongoing monitoring; and
- updated mandates for each of the investment portfolios, including objectives and controls.

4.7 Importantly, the focus of the Panel is the long-term superior asset returns of the Funds, rather than the short-term vacillations of the investment markets, by deploying each Fund's long-term capital at an appropriate level of risk.

5. Next Steps

5.1 This report is the regular annual update of Panel activity. Updates of significant activity and changes to strategy implementation are reported to the Committee throughout the year.

6. Financial impact

- 6.1 Investment strategy is a key determinant of funding level, risk and volatility of employer contribution rates. The Funds' investment strategies are aimed at reducing the risk without sacrificing returns.

7. Stakeholder/Community Impact

- 7.1 The Pension Board, comprising employer and member representatives, is integral to the governance of the pension funds and they are invited to comment on the relevant matters at Committee meetings.
- 7.2 There are no adverse health and safety, governance, compliance or regulatory implications as a result of this report. The forward planning of the Committees' agendas should facilitate improved risk management and governance for the pension funds.
- 7.3 There are no adverse sustainability impacts arising from this report.

8. Background reading/external references

- 8.1 None.

9. Appendices

Appendix 1 – Agenda Planning for Joint Investment Strategy Panel

Joint Investment Strategy Panel – Agenda Planning

This document provides the Panel with an overview of the proposed agendas for future meetings of the Joint Investment Strategy Panel. It also provides a more general overview of the current cycle of Panel papers. An agenda planning document will be provided each quarter.

Some agenda items refer to Committee reports. These are Lothian reports and it is proposed that reporting for the Lothian, Falkirk and Fife Committees is synchronised, to the extent possible, going forward. There will, of course, be other matters and papers that need to be brought to the attention of the Panel on an *ad hoc* basis.

From September 2019, investment mandates will be reviewed annually at the same time as the relevant asset class focus.

The proposed agendas for the next two meetings are set out below.

September 2019

Special Items

- Fund Strategy Focus – Fife Council Pension Fund Annual Review
- Asset Class Focus – Real Assets (property, Infra & timber) Annual Review
- Asset Class Focus – Currency Exposures/Hedging Annual Review
- Audit of Foreign Exchange Transaction Costs
- Statement of Investment Principles
- Investment Mandates Annual review – Real Assets & Currency

Quarterly Items

- Investment Monitoring
- Asset/Liability Context – Investment Markets
- Investment Strategy Implementation

December 2019

Special Items

- Fund Strategy Focus – Scottish Homes Pension Fund Annual Review
- Asset Class Focus – Debt Assets (Gilts, Non-Gilts, Cash) Annual Review
- Review of Governance of Internal Portfolios by external JISP members
- Stewardship
- AVC Monitoring
- Internal Mandate Review – Europe ex-UK portfolio
- Internal Mandate Review – Index Linked Gilts
- Internal Mandate Review – Fixed Income Assets
- Investment Mandates Annual review – Debt Assets (Gilts, Non-Gilts, Cash)

Quarterly Items

- Investment Monitoring
- Asset/Liability Context – Investment Markets
- Investment Strategy Implementation

Future Joint Investment Strategy Panel Dates

- Tuesday 10 September 2019, 10.30am, Atria One Boardroom
- Monday 2 December 2019, 10.30am, Atria One Boardroom

Frequency			Month
Annually	Fund Strategy Focus		
	Lothian Pension Fund		March
	Falkirk Council Pension Fund		June
	Scottish Homes Pension Fund		December
	Fife Pension Fund		September
	Asset Class Focus – Annual Reviews, incl. Investment Mandates		
	Equities (listed & unlisted), incl. Carbon Assessment		June
	Real Assets (property, infra & timber)		September
	Currency Exposures/Hedging		September
	Debt Assets (Gilts, Non-Gilts, Cash)		December
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	Securities Lending Policy Review		March
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	Investment Controls & Compliance (incl. custodian)	Committee Report	June
	Statement of Investment Principles	Committee Report	September
	Investment Strategy Panel – Terms of Reference & Effectiveness		June
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	Audit of Foreign Exchange Transaction Costs		September
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	Review of Governance of Internal Portfolios by external JISP members		December
	Stewardship	Committee Report	December
	Investment Cost Benchmarking	Committee Report	March
	AVC Monitoring	Committee Report	December

Frequency				Month
Quarterly	Investment Portfolio Monitoring (traffic lights)			March, June, September and December
	Asset/Liability Context – Investment Markets (incl. Adviser Ideas/Recommendations)			
	Investment Strategy Implementation/Funding Updates			
Every 3 Years (minimum)	Investment Strategy Reviews	Due 2021	Typically December or March	
	Actuarial Valuations	Due 2021		
	Funding Strategy Statements	Due 2021		
	Internal Mandate Reviews	Most recent review:	Review due:	March, June, September and December
	UK All Cap	June 2018	June 2021	
	UK Mid Cap	June 2018	June 2021	
	Europe ex-UK	June 2016	December 2019	
	US	March 2019	March 2022	
	GLOVE	March 2018	March 2021	
	GHDY	March 2018	March 2021	
SMuRV	March 2018	March 2021		
Index-linked Gilts	December 2016	December 2019		
Fixed Income Assets	December 2016	December 2019		
As required	Development Work Transitions			