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DATE: 25 February 2019

To: Members of the
PENSIONS INVESTMENT SUB-COMMITTEE

Councillor Keith Onslow (Chairman)
Councillor Russell Mellor (Vice-Chairman)
Councillors Gareth Allatt, Simon Fawthrop, Simon Jeal, David Jefferys and Gary Stevens

A meeting of the Pensions Investment Sub-Committee will be held at Bromley Civic Centre on **TUESDAY 5 MARCH 2019 AT 7.00 PM**

Members of the Local Pension Board are also invited to attend this meeting

MARK BOWEN
Director of Corporate Services

Copies of the documents referred to below can be obtained from http://cds.bromley.gov.uk/

A G E N D A

1 **APOLOGIES FOR ABSENCE AND NOTIFICATION OF SUBSTITUTE MEMBERS**

2 **DECLARATIONS OF INTEREST**

3 **MINUTES OF THE MEETINGS HELD ON 7TH NOVEMBER 2018 AND 14TH JANUARY 2019 (SPECIAL MEETING)** (Pages 5 - 14)

4 **QUESTIONS BY MEMBERS OF THE PUBLIC ATTENDING THE MEETING**

In accordance with the Council's Constitution, questions to this Sub-Committee must be received in writing four working days before the date of the meeting. Therefore please ensure that questions are received by the Democratic Services Team by 5pm on Wednesday 27th February 2019.

5 **CHAIRMAN'S UPDATE**

6 **PENSION FUND PERFORMANCE Q3 2018/19** (Pages 15 - 44)

7 PENSION FUND - INVESTMENT REPORT

Printed copies of reports from certain Fund Managers are circulated to Sub-Committee Members with this agenda. Remaining reports will be circulated as soon as possible.

Representatives of Baillie Gifford are expected to attend the meeting for this item.

8 LBB RESPONSE TO DRAFT LGPS STATUTORY GUIDANCE ON ASSET POOLING CONSULTATION (Pages 45 - 68)

9 LOCAL GOVERNMENT ACT 1972 AS AMENDED BY THE LOCAL GOVERNMENT (ACCESS TO INFORMATION) (VARIATION) ORDER 2006 AND FREEDOM OF INFORMATION ACT 2000

The Chairman to move that the Press and public be excluded during consideration of the items of business referred to below as it is likely in view of the nature of the business to be transacted or the nature of the proceedings that if members of the Press and public were present there would be disclosure to them of exempt information.

	Items of Business	Schedule 12A Description
10	**EXEMPT MINUTES OF THE MEETINGS HELD ON 7TH NOVEMBER 2018 AND 14TH JANUARY 2019 (SPECIAL MEETING)** (Pages 69 - 76)	Information relating to the financial or business affairs of any particular person (including the authority holding that information)
11	**CHAIRMAN'S UPDATE ON EXEMPT MATTERS**	Information relating to the financial or business affairs of any particular person (including the authority holding that information)
12	**OPERATIONAL DUE DILIGENCE REVIEW OF LONDON CIV** (Pages 77 - 100)	Information relating to the financial or business affairs of any particular person (including the authority holding that information)
13	**DUE DILIGENCE REPORT FROM LONDON CIV'S DEPOSITORY (NORTHERN TRUST)** Report to be tabled at the meeting.	Information relating to the financial or business affairs of any particular person (including the authority holding that information)
14	**LCIV - CHANGE OF BUSINESS DESCRIPTION LETTER** (Pages 101 - 110)	Information relating to the financial or business affairs of any particular person (including the authority holding that information)

PENSIONS INVESTMENT SUB-COMMITTEE

Minutes of the meeting held at 7.00 pm on 7 November 2018

Present

Councillor Keith Onslow (Chairman)
Councillor Russell Mellor (Vice-Chairman)
Councillors Gareth Allatt, Simon Fawthrop, Simon Jeal, David Jefferys and Gary Stevens

Also Present

John Arthur, M J Hudson Allenbridge Investment Advisers

63 APOLOGIES FOR ABSENCE AND NOTIFICATION OF SUBSTITUTE MEMBERS

There were no apologies.

64 DECLARATIONS OF INTEREST

Interests were declared by virtue of deferred membership of the Local Government Pension Scheme as per those previously notified (for the Register of Interests).

65 CONFIRMATION OF MINUTES OF THE MEETING HELD ON 13TH SEPTEMBER 2018 EXCLUDING THOSE CONTAINING EXEMPT INFORMATION

The Minutes were agreed.

In so doing two matters were raised. The first concerned the LCIV receiving any additional permissions under their Phase 3 of development which could lead to investments being managed on behalf of boroughs. The Chairman explained that the LCIV's Financial Plan had been raised in principle at the October Meeting of the LCIV Shareholder's Committee.

The second matter concerned the LCIV's Depositary. With the LCIV Interim CEO previously confirming Northern Trust as the LCIV's Depositary, it was minuted that a check would be necessary on whether a copy of the Depositary's report could be provided. This remained outstanding and it was agreed that the matter should be reflected as a continuing action point for the current minutes **(ACTION: LCIV/Director of Finance)**.

66 QUESTIONS BY MEMBERS OF THE PUBLIC ATTENDING THE MEETING

There were no questions.

67 PENSION FUND PERFORMANCE Q2 2018/19

Report FSD18086

Details were provided of the Fund's investment performance for the second quarter of 2018/19. Additional detail was provided in an appended report from the Fund's external advisers, MJ Hudson Allenbridge.

The market value of the Fund ended the September quarter at £1,045.5m (£1,017.9m at 30th June). The quarter total fund return was +2.84% against the benchmark of +3.36%. Detail on performance by individual fund managers was appended to Report FSD18086.

The Fund's medium and long-term returns remain very strong overall - the Fund ranking third in the PIRC LGPS universe for the year to 31st March 2018, first over three years, second over five years, first over ten years and second over 20 and 30 years. In addition to winning the LGPS Investment Performance of the Year in 2017, the Fund has also recently won the LGPS Fund of the Year (assets under £2.5bn) in 2018, recognising the consistent high performance of the Fund.

Information on general financial and membership trends of the Pension Fund was also outlined along with summarised information on early retirements. Final outturn details for the 2017/18 Pension Fund Revenue Account were included as was the second quarter position for 2018/19 and fund membership numbers. A cash surplus for the Fund of around £3m is expected for the year.

For the Sub-Committee's meeting on 5th March 2019, it was proposed to invite Baillie Gifford (global equities and fixed income) with MFS invited to the Sub-Committee's following meeting (currently set for 23rd May 2019).

John Arthur (M J Hudson Allenbridge) commented on the Fund's performance for the quarter. Reference was made to the Fund's increased value although underperformance from Baillie Gifford's Global Equity portfolio (accounting for over 40% of the Fund's assets) returned at 3.4% over the quarter leading to the Fund underperforming its benchmark by 0.5%. The quarter had not favoured Baillie Gifford's approach to investment growth and they had now underperformed over a couple of quarters. In view of the economic/market outlook, Baillie Gifford could be expected to struggle a little in future (but long term the portfolio had performed very well and continued to hit its long term performance target).

Conversely, MFS outperformed during the quarter on the Fund's other Global Equity portfolio and MFS were now more stable following a period of poor performance (MFS invests in a different manner to Baillie Gifford and was selected because of this diversification of investment philosophy and approach).

On economic outlook, a period of falling growth and rising inflation will be difficult for equities and fixed rate bonds. Events can happen to take the economy into different phases (e.g. Stagflation, Reflation, Deflation, increased productivity) causing uncertainty. In the U.S. The President tended to act specifically for the U.S. and economic growth. Mr Arthur was optimistic of having economic growth; however, recession was further away but when it occurs it could be more extreme.

The Fixed Interest portfolios and their value were discussed. Fixed interest provided diversification and returns will rise in a deflationary cycle when returns from equities reduce. Mr Arthur referred to removing some duration from fixed interest and explained how Fidelity can achieve a higher yield in such a difficult market (involving the purchase of Government debt). Provided a procurement process is not necessary, this was worth exploring, and a meeting could be arranged with Fidelity. Fidelity can then bring a proposal to the Sub-Committee's meeting on 5th March 2019. The Chairman questioned the value of the current Fixed Interest allocation and if Mr Arthur's approach looked possible, he suggested Members consider any better mandate. Although from an actuarial perspective it might not be appropriate to take too much from Fixed Interest, it would be a good area to look at given the market volatility. Supporting the approach, another Member asked to see information on U.S. default rates and securitised debt. It was highlighted that some 6.4% of Schroder's Alternatives portfolio is allocated to Securitised Debt and Mr Arthur indicated that (U.S.) default rates are particularly low.

A Member wanted to see the investment income that is paid to the Council from MAI and property funds to see how the return is spent. The Director advised that a memorandum summary can be produced in future with the quarterly Fund performance report **(ACTION: Director of Finance)**.

Concerning Baillie Gifford's under-performance, Mr Arthur did not expect the portfolio to fall much further and commented on the exceptional run of good performance (over recent years). Noting that Fixed Income is in line with benchmark, a Member suggested that passive is also looked at if Fixed Interest is reviewed. Mr Arthur indicated that he would not naturally put forward a passive rate in Fixed Interest.

RESOLVED that the contents of Report FSD18086 be noted.

68 PENSION FUND - INVESTMENT REPORT

Representatives from Schroders (Multi-Asset Fund Manager and Client Director) attended to present their investment report.

The Schroders ISF Global Multi-Asset Income (MAI) fund sets out to achieve a sustainable, stable investment outcome with an income objective of 4 to 6%

p.a. over a market cycle and an expected volatility of 5 to 7% p.a. The Fund had returned 4% p.a. since inception (GBP hedged).

The previous three months had been challenging for performance. At 30th September 2018, the Year to Date (YTD) contribution to return for Schroders MAI fund provided a 0.3% portfolio return in U S Dollars (Gross of Fees) and a return of -1.0% in GBP (Gross of Fees). Broken down, equity contributed 0.7% return, Fixed Income contributed -0.4%, Alternatives contributed 0.4% and cash and currency contributed -0.3%. Equities had been a driver for the marginal returns but fixed interest is challenging as interest rates are rising. Alternatives behave differently from other classes and are inexpensive, providing good returns in October. For cash and currency, sterling was a little difficult in view of Brexit but the risk had been managed.

Details were provided of current allocation and yield by asset class (allocations at 31st October 2018 and yields at 30 September 2018). Over the next four years, a yield of between 4% and 6% was expected. The presentation also illustrated the current portfolio composition with 26.9% allocated to equities, 49.6% to fixed income, 18.9% to alternatives and 4.5% to cash.

Although asset class returns for 2017 exceeded Schroders expectations, 2018 is proving more difficult. In 2017 only one asset class failed to return above 0% (US dollar) but so far in 2018 seven asset classes are failing to return with just five asset classes doing so i.e. US Tech Equities (9.8%), Oil (8%), US dollar (5.4%), US Equities (3%) and High Yield Debt (0.9%). October in particular had proved negative with only the US dollar asset class (2.1%) and Gold (2%) positively returning.

Concerning Schroder’s view of global growth, this was forecast to be 3.3%for 2018 and 3% for 2019. Risk cycle trend data from 1978 to date for both the Business Cycle Indicator (BCI) and a US output gap model also suggested that an expansion stage is currently being experienced (particularly in the U.S.). However, this was not good for fixed income with global inflation gradually rising (and inflation rising faster in the U.S.). Central banks were also starting to raise interest rates slowly and Quantitative Easing had ended. With interest rates rising, Schroder’s needed to be more creative (in obtaining returns). The presentation also showed that monetary policy is normalising with details provided on how value is being sought in equities (US equity valuations look extended and assets are inexpensive in the U.S). Buying cheaper assets was thought beneficial. Further details showed how a granular approach is being taken to fixed income (capitalising on market dislocations and inefficiencies).

Information was also provided on: alternative assets; current risk adjusted yield for the Global MAI strategy against other asset classes set against volatility; and a diagrammatic (dynamic) analysis of what can happen to the global economy (stagflationary, reflationary, deflationary and productivity boost) set against certain scenarios. A number of further slides were also appended to the Schroders presentation.

Concerning infrastructure, this had produced wealth but there were now challenges including those around Brexit. Longer term, the Multi-Asset Fund Manager considered infrastructure attractive, particularly in terms of what is available globally, but short term investment in infrastructure (over one to three years) was not considered so attractive.

On income, a 4.5% to 5% return was currently expected for the next 12 months with overachievement expected in the following 12 months (in the order of 5%). Four months previously, income was about 4% and to generate 5% at that point would have meant Schroders taking undue risk.

In regard to Brexit, the Fund Manager had a positive view on sterling, noting that UK data had surprised since the referendum vote. Against the U.S. dollar, sterling was particularly cheap leading to tentative moves back into sterling. The UK equity market was starting to look cheap and apart from infrastructure, UK assets are looking quite attractive.

In October, global equities fell some 7% to 8% and it was thought that this was due to the markets being too optimistic rather than a result of economic weakness. Schroders were ‘parking’ investments into alternative assets where real yield is obtainable; it would then move back into the market when it was more attractive. Reference was also made to dollar exposure to manage risk but more broadly Schroders sought to increase investment in alternatives.

Uncertainty was causing jitters (a Member noted developments concerning a U.S./China trade war, U.S. inflation, concerns over Italy, and the German Chancellor having given notice of leaving office) and the level of panic in markets during October had been considerable. The Fund Manager predicted the start of a negative period (a U.S./China trade war starting and more volatility) and Schroders needed to be more creative and move to other assets. China was worrying; official data indicated that the economy is well managed but non-official reports suggest a fall in electricity demand. The Fund Manager felt that a number of analysts are too optimistic and it is necessary to prepare now for the future.

Noting a 3.3% investment allocation to infrastructure (within a total alternatives allocation of 18.9%), the Director of Finance questioned whether the allocation should be more like 10% rather than 3.3% and whether any increased allocation would be non-U.K (any future nationalisation under a new Government would remove the attraction of U.K. based infrastructure). The Fund Manager considered 3.3% low but access can be difficult with infrastructure investment and an element of liquidity is necessary. She indicated that investment would be non-UK but preferred a 5% allocation to infrastructure rather than an increase to 10%.

A question was asked on how the allocation of assets is decided and whether fees are paid annually or quarterly. Schroders took a diversified approach (on allocation); should one asset not perform, others will perform and the sequence of returns mattered to create a stability (of income return).

Schroders have a qualitative process to focus on the value of assets in the economic cycle. Harnessing an algorithm and human input (for sentiment) combined to make a judgement. The Client Director indicated that fees are 0.35% of the value of an investment with invoices provided quarterly.

Although Schroders manage a £70bn sterling mandate which they had won, along with managing an additional £60bn, the Fund Manager confirmed there would be no disruption to the portfolio (in performance management) and her team would continue to focus on their current mandate for L B Bromley.

Following the discussion, and with the representatives having left the room, all Members agreed that an excellent presentation had been provided and the Chairman asked that the Sub-Committee's feedback be provided to the Schroders representatives **(ACTION: Director of Finance)**.

69 LOCAL PENSION BOARD - ANNUAL REPORT

Report FSD18081

Members noted the Annual Report of the Local Pension Board.

RESOLVED that the contents of the Local Pension Board Annual Report (dated October 2018) appended to Report FSD18081 be noted.

70 LOCAL GOVERNMENT ACT 1972 AS AMENDED BY THE LOCAL GOVERNMENT (ACCESS TO INFORMATION) (VARIATION) ORDER 2006 AND FREEDOM OF INFORMATION ACT 2000

RESOLVED that the Press and public be excluded during consideration of the items of business referred to below as it is likely in view of the nature of the business to be transacted or the nature of the proceedings that if members of the Press and public were present there would be disclosure to them of exempt information.

**The following summaries
refer to matters
involving exempt information**

71 CONFIRMATION OF EXEMPT MINUTES OF THE MEETING HELD ON 13TH SEPTEMBER 2018

Members received Part 2 minutes of the Sub-Committee's previous meeting and the Chairman requested that future Sub-Committee meetings include "Chairman's Update" as a regular item **(ACTION: Democratic Services).**

The opportunity was also taken at this point to apprise the Sub-Committee on certain matters under Part 2 proceedings of the meeting.

72 LONDON CIV - PENSION RECHARGE AND GUARANTEE AGREEMENTS

The report for this item had been withdrawn. It was considered too soon to look at recommendations for L B Bromley to enter into a Pension Guarantee Agreement (requested by the LCIV and City of London) and Pension Cost Recharge Agreement (requested by the LCIV) related to the pension liability of LCIV employees in the LGPS scheme. Further legal information was necessary and the matter would not be considered at the present time.

The Meeting ended at 9.55 pm

Chairman

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PENSIONS INVESTMENT SUB-COMMITTEE

Minutes of the special meeting held at 6.30 pm on 14 January 2019

Present:

Councillor Keith Onslow (Chairman)
Councillor Russell Mellor (Vice-Chairman)
Councillors Gareth Allatt, Simon Fawthrop, Kira Gabbert, Simon Jeal and Gary Stevens

Also Present:

John Arthur, MJ Hudson Allenbridge Investment Advisors

73 APOLOGIES FOR ABSENCE AND NOTIFICATION OF SUBSTITUTE MEMBERS

Apologies for absence were received from Councillor David Jefferys, who was replaced by Councillor Kira Gabbert.

Apologies for lateness were received from Councillor Gary Stevens.

74 DECLARATIONS OF INTEREST

There were no declarations of interest.

75 LOCAL GOVERNMENT ACT 1972 AS AMENDED BY THE LOCAL GOVERNMENT (ACCESS TO INFORMATION) (VARIATION) ORDER 2006 AND FREEDOM OF INFORMATION ACT 2000

RESOLVED that the Press and public be excluded during consideration of the items of business referred to below as it is likely in view of the nature of the business to be transacted or the nature of the proceedings that if members of the Press and public were present there would be disclosure to them of exempt information.

The following summaries refer to matters involving exempt information

76 DUE DILIGENCE REVIEW OF LONDON CIV BAILLIE GIFFORD GLOBAL ALPHA GROWTH FUND

The Sub-Committee considered a report on the due diligence review of the London CIV Global Alpha Growth Fund commissioned from the Council's independent advisor.

77 CESSATION OF ADMISSION BODY - DEFICIT REPAYMENT PLAN

The Sub-Committee agreed to consider an urgent report regarding the cessation of an admission body, and agreed recommendations for a decision by General Purposes and Licensing Committee.

The Meeting ended at 7.30 pm

Chairman

Report No.
FSD19034

London Borough of Bromley

PART 1 - PUBLIC

Decision Maker:	**Pensions Investment Sub-Committee**
Date:	**5th March 2019**
Decision Type:	Non-Urgent Non-Executive Non-Key
Title:	**PENSION FUND PERFORMANCE Q3 2018/19**
Contact Officer:	Jo-Anne Chang-Rogers, Principal Accountant Tel: 020 8313 4292 E-mail: jo-anne.chang-rogers@bromley.gov.uk
Chief Officer:	Director of Finance
Ward:	All

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1. Reason for report

1.1 This report provides a summary of the investment performance of Bromley's Pension Fund in the 3rd quarter of 2018/19. More detail on investment performance is provided in a separate report from the Fund's external advisers, MJ Hudson Allenbridge, which is attached as Appendix 5. The report also contains information on general financial and membership trends of the Pension Fund and summarised information on early retirements.

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2. RECOMMENDATION

2.1 The Pensions Investment Sub-Committee is asked to:

(a) Note the contents of the report.

(b) Agree that the balance of Blackrock Global Equity Fund be invested in the Baillie Gifford Fixed Income Portfolio (paragraph 3.2.3)

(c) Agree the further award of the Pension performance measurement contract, via an exemption to competitive tendering, as set out in paragraph 3.3.3

(d) Agree the programme for Fund Manager attendance as set out in paragraph 3.7.1

Corporate Policy

1. Policy Status: Existing policy. The Council's Pension Fund is a defined benefit scheme operated under the provisions of the Local Government Pension Scheme (LGPS) Regulations, for the purpose of providing pension benefits for its employees. The investment regulations (The LGPS (Management and Investment of Funds) Regulations 2016) allow local authorities to use all the established categories of investments, e.g. equities, bonds, property etc, and to appoint external investment managers who are required to use a wide variety of investments and to comply with certain specific limits.

2. BBB Priority: Excellent Council.

Financial

1. Cost of proposal: No cost

2. Ongoing costs: Recurring cost. Total administration costs estimated at £5.1m (includes fund manager/actuary/adviser fees, Liberata charge and officer time)

3. Budget head/performance centre: Pension Fund

4. Total current budget for this head: £40.7m expenditure (pensions, lump sums, etc); £52.5m income (contributions, investment income, etc); £963.7m total fund market value at 31st December 2018)

5. Source of funding: Contributions to Pension Fund

Staff

1. Number of staff (current and additional): 0.4 FTE

2. If from existing staff resources, number of staff hours: c 14 hours per week

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Legal

1. Legal Requirement: Statutory requirement. Local Government Pension Scheme (LGPS) Regulations 2013, LGPS (Management and Investment of Funds) Regulations 2016

2. Call-in: Call-in is not applicable.

Customer Impact

1. Estimated number of users/beneficiaries (current and projected): 6,316 current employees; 5,328 pensioners; 5,755 deferred pensioners as at 31st January 2019

Ward Councillor Views

1. Have Ward Councillors been asked for comments? No.

2. Summary of Ward Councillors comments: N/A

3. COMMMENTARY

3.1 Fund Value

3.1.1 The market value of the Fund ended the December quarter at £963.7m, down from £1,045.5m as at 30th September. The comparable value as at 31st December 2017 was £998.0m. Historic data on the value of the Fund are shown in a table and in graph form in Appendix 1.

3.2 Performance Targets and Investment Strategy

3.2.1 Historically, the Fund's investment strategy was broadly based on a high level 80%/20% split between growth seeking assets (representing the long-term return generating part of the Fund's assets) and protection assets (aimed at providing returns to match the future growth of the Fund's liabilities). Between 1998 and 2012, Baillie Gifford and Fidelity managed balanced mandates along these lines, and, a comprehensive review of the Fund's investment strategy in 2012 confirmed this high-level strategy. It concluded that the growth element would, in future, comprise a 10% allocation to Diversified Growth Funds (DGF) and a 70% allocation to global equities, with a 20% protection element remaining in place for investment in corporate bonds and gilts.

3.2.2 The asset allocation strategy was reviewed again during 2016/17, mainly to address the projected cash flow shortfall in future years, and a revised strategy was agreed on 5th April 2017. The revised strategy introduced allocations to Multi Asset Income Funds (20%) and Property Funds (5%), removed Diversified Growth Funds, and reduced the allocations to Global Equities (to 60%) and Fixed Income (to 15%). In order to implement the revised strategy, it was agreed to sell all of the Diversified Growth Funds and the Blackrock Global Equities assets.

3.2.3 At the meetings on 21st November and 14th December 2017, the Sub-Committee appointed Schroders (60%) and Fidelity (40%) to manage the MAI fund mandates, and Fidelity to manage a UK pooled property fund mandate. The Fidelity MAI and initial drawdown of the property fund were completed in February 2018, the Schroders MAI investment completed in May 2018. A further drawdown of the Fidelity property fund was completed in August 2018. The final drawdown of the Fidelity property was completed in December 2018. As at the end of January 2019, the balance on the Blackrock Global Equity Fund, was £10,953,304. On 14 December 2017, this committee agreed that "*the balance of the Blackrock sale, less £3 million required to meet the cash-flow shortfall that had occurred during 2017/18, be invested in the Fixed Income Portfolio*." Members are asked to confirm the investment of the balance of the Blackrock fund be invested in the Bailee Gifford Fixed Income portfolio.

3.3 Summary of Fund Performance

3.3.1 Performance data for 2018/19 (short-term)

A detailed report on fund manager performance in the quarter ended 31st December 2018 is provided by the fund's external adviser, MJ Hudson Allenbridge, in Appendix 5. As explained in their report, market conditions have led to significant negative performance. The Bromley Fund experience is echoed around the country, with PIRC citing this quarter's performance, for the funds they benchmark, as the worst since 2011. The total Bromley fund return for the third quarter was -7.94% against the benchmark of -5.91%. Further details of individual fund manager performance against their benchmarks for the quarter, year to date, 1, 3 and 5 years and since inception are provide in Appendix 2.

3.3.2 Medium and long-term performance data

The Fund's medium and long-term returns have remained very strong overall, with returns of 6.7% for 2017/18 and 26.8% for 2016/17 against the benchmark of 3.1% and 24.6% respectively. The overall Fund ranked third against the 61 funds in the PIRC LGPS universe for the year to 31st March 2018, first over 3 years, second over 5 years, first over 10 years and second over 20 and 30 years.

The following table shows the Fund's long-term rankings in all financial years back to 2005/06 and shows the medium to long-term returns for periods ended 31st March. The medium to long-term results have been good and have underlined the fact that the Fund's performance has been consistently strong over a long period.

Year	Whole Fund Return	Benchmark Return	Local Authority average*	Whole Fund Ranking*
	%	%	%	
Financial year figures				
2017/18	***6.7***	***3.1***	***4.5***	***3***
2016/17	26.8	24.6	21.4	1
2015/16	0.1	0.5	0.2	39
2014/15	18.5	16.4	13.2	7
2013/14	7.6	6.2	6.4	29
2012/13	16.8	14.0	13.8	4
3 year ave to 31/3/18	***10.6***	***8.9***	***8.3***	***1***
2014/15	14.6	13.4	11.2	1
2013/14	8.4	7.5	6.4	6
2012/13	14.2	12.1	11.1	5
2011/12	2.2	2.0	2.6	74
2010/11	9.0	8.0	8.2	22
5 year ave to 31/3/18	***11.5***	***9.8***	***8.8***	***2***
2012/13	13.6	12.0	10.7	1
2011/12	8.8	7.6	7.1	6
2010/11	10.7	9.2	8.8	11
2009/10	48.7	41.0	35.2	2
2008/09	-18.6	-19.1	-19.9	33
2007/08	1.8	-0.6	-2.8	5
2006/07	2.4	5.2	7.0	100
2005/06	27.9	24.9	24.9	5
10 year ave to 31/3/18	***10.5***	***n/a***	***7.7***	***1***
20 year ave to 31/3/18	***7.8***	***n/a***	***6.5***	***2***
30 year ave to 31/3/18	***9.7***	***n/a***	***8.9***	***2***

*The most recent LA averages and ranking as at 31/03/18 are based on the PIRC LA universe containing 61 of the 89 funds.

In addition to winning the LGPS Investment Performance of the Year in 2017, the Fund has also recently won the LGPS Fund of the Year (assets under £2.5bn) in 2018, recognising the consistent high performance of the Fund.

3.3.3 Performance Measurement Service

As previously reported, in April 2016, the Council was informed that WM Company (State Street) would cease providing performance measurement services to clients to whom they do not act as custodian, with effect from June 2016. There are currently no providers offering a like for like service, so the Council is using its main custodian, BNY Mellon, to provide performance measurement information, and the 3rd quarter summary of manager performance is provided at Appendix 2. PIRC currently provide LA universe comparator data, and at the time of writing has 62 of the 89 LGPS funds (69%) signed up to the service, including the London Borough of Bromley.

The current performance measurement contract with BNY Mellon expires in June 2019.

The Council's pension fund advisers have undertaken recent research and the situation is as it was in 2016, with no company offering performance measurement, or performance measurement with accounting without custody. Members are therefore requested to agree an an award of contract to the custodian, BNY Mellon, for a further 3 years, at an estimated value of £30k per annum (whole life value £90k), via an exemption to competitive tendering, subject to annual review.

3.4 Early Retirements

3.4.1 Details of early retirements by employees in the Fund are shown in Appendix 3.

3.5 Admission agreements for outsourced services

3.5.1 As part of the Council's commissioning programme, all of its services are being reviewed, which may result in the outsourcing of further services. The final transfer payment for GS Plus is still being considered by the Actuary. There are no other updates at this point, but the position will continue to be monitored and updates provided for future meetings.

3.6 Bromley College

3.6.1 As previously reported to this sub-committee in May 2016, February 2017, September 2017 Bromley College merged with Greenwich Community College on 1st August 2016, and in accordance with the Secretary of State's direction all assets and liabilities would transfer to the Local Pensions Partnership. £32.1 million of Blackrock global equities fund was sold on 5th July 2017. As reported to the September 2017 committee, the Fund's actuaries were calculating the final transfer value. This was to reflect additional cashflows/liablities in respect of three pensioners not included in the initial calculation, as well as fund returns in June 2017. The final balancing transfer payment of £529k was made on 7 December 2018, bringing the total to £32.6 bn.

3.7 Fund Manager attendance at meetings

3.7.1 Meeting dates have been set for 2018/19, with Baillie Gifford attending this meeting. While Members reserve the right to request attendance at any time if any specific issues arise, the timetable for subsequent meetings is as follows:

Meeting 5th March 2019 – Baillie Gifford (global equities and fixed income)
15th May 2019 – MFS (global equities) - rescheduled

The committee calendar for 2019/20 has now been issued. Members are asked to agree attendance at the future meetings as follows:

Meeting 24th July 2019 – Fidelity (fixed income, multi-asset income and property)
Meeting 27th August 2019 – Schroders (multi-asset income)
Meeting 3rd December 2019 – Baillie Gifford (global equities and fixed income)
Meeting 3rd January 2020 – MFS (global equities
Meeting 13th February 2020 – Fidelity (fixed income, multi-asset income and property)

4. POLICY IMPLICATIONS

4.1.1 The Council's Pension Fund is a defined benefit scheme operated under the provisions of the Local Government Pension Scheme (LGPS) Regulations, for the purpose of providing pension benefits for its employees. The investment regulations (The LGPS (Management and Investment of Funds) Regulations 2016) allow local authorities to use all the established categories of investments, e.g. equities, bonds, property etc, and to appoint external investment managers who are required to use a wide variety of investments and to comply with certain specific limits.

5. FINANCIAL IMPLICATIONS

5.1.1 Details of the final outturn for the 2017/18 Pension Fund Revenue Account and the position after the third quarter of 2018/19 are provided in Appendix 4 together with fund membership numbers. A net deficit of £0.7m occurred during 2017/18 and total membership numbers rose by 516. In the first three quarters of 2018/19, a net surplus of £8.9m has arisen, and membership numbers increased by 373.

5.1.2 It should be noted that the net deficit of £0.7m in 2017/18 includes investment income of £8.8m which was re-invested in the funds, so in cashflow terms, there would have been a £8.1m cash deficit for the year. Similarly, the £8.9m surplus in the first three quarters of 2018/19 would be cash a surplus of only £0.8m excluding reinvested income. With the Fidelity Fund and the Schroders MAI investment now completed, the distributed income should increase significantly, and a cash surplus of around £3m is expected for the year.

5.1.3 The cost of the performance measurement contract with BNY Mellon is recharged to the pension fund (£30k p.a.). The current contract with BNY Mellon for the provision of a performance measurement service is for 3 years, ending on 30 June 2019 at a total cost of £85k. The proposed extension will result in a cumulative value of £175k. Under the council's contract procedure rules, approval is requested from this committee to agree this extension.

6. LEGAL IMPLICATIONS

6.1.1 The statutory provisions relating to the administration of the Local Government Pension Scheme are contained in the Local Government Pension Scheme (LGPS) Regulations 2013. The investment regulations (The LGPS (Management and Investment of Funds) Regulations 2016) set out the parameters for the investment of Pension Fund monies.

7. PROCUREMENT IMPLICATIONS

7.1.1 This report seeks to award a contract to BNY Mellon for a duration of three years at an estimated value of £30k per annum (whole life value of £90k).

7.1.2 This action is permissible under the general waiver power of the Council (CPR 3.1). The Council's specific requirements for authorising an exemption are covered in CPR 13 with the need to obtain the Approval of members, following Agreement by the Chief Officer, the Assistant Director Governance & Contracts, the Director of Corporate Services and the Director of Finance for a contract of this cumulative value (£175k over 6 years – 01/07/16 to 30/06/22). Contracts of this nature are exempt from the EU procurement procedures by virtue of Regulation 10 9e) of the Public Contracts Regulations 2015.

7.1.3 The actions identified in this report are provided for within the Council's Contract Procedure Rules, and the proposed actions can be completed in compliance with their content

Non-Applicable Sections:	Personnel Implications, Impact on Vulnerable Adults and Children,
Background Documents: (Access via Contact Officer)	Monthly and quarterly portfolio reports of Baillie Gifford, Blackrock, Fidelity, MFS and Standard Life.

Appendix 1

MOVEMENTS IN PENSION FUND MARKET VALUE SINCE 2002

Date	**Baillie Gifford**					**Fidelity**					**Blackrock**	**MFS**	**Standard Life**	**Schroders**	**CAAM**	
	Balanced Mandate	DGF	Fixed Income	Global Equities	Total	Balanced Mandate	Fixed Income	MAI	Property	Total	Global Equities	Global Equities	DGF	MAI	LDI Investment	**GRAND TOTAL**
	£m	£m	£m	£m	£m	£m	£m			£m	£m	£m	£m	£m	£m	£m
31/03/2002	113.3				113.3	112.9				112.9						226.2
31/03/2003	90.2				90.2	90.1				90.1						180.3
31/03/2004	113.1				113.1	112.9				112.9						226.0
31/03/2005	128.5				128.5	126.7				126.7						255.2
31/03/2006	172.2				172.2	164.1				164.1						336.3
31/03/2007	156.0				156.0	150.1				150.1					43.5	349.6
31/03/2008	162.0				162.0	151.3				151.3					44.0	357.3
31/03/2009	154.4				154.4	143.0				143.0						297.4
31/03/2010	235.4				235.4	210.9				210.9						446.3
31/03/2011	262.6				262.6	227.0				227.0						489.6
31/03/2012	269.7				269.7	229.6				229.6						499.3
31/03/2013#	315.3	26.5			341.8	215.4				215.4			26.1			583.3
31/03/2014@	15.1	26.8	45.2	207.8	294.9		58.4			58.4	122.1	123.1	27.0			625.5
31/03/2015		45.5	51.6	248.2	345.3		66.6			66.6	150.5	150.8	29.7			742.9
31/03/2016		44.8	51.8	247.9	344.5		67.4			67.4	145.5	159.2	28.3			744.9
31/03/2017		49.3	56.8	335.3	441.4		74.3			74.3	193.2	206.4	28.5			943.8
31/03/2018$&			58.0	380.0	438.0		75.6	79.2	15.9	170.7	155.2	206.8				970.7
30/06/2018£			57.1	408.4	465.5		75.8	79.7	16.1	171.6	44.0	217.8		119.0		1017.9
30/09/2018^			56.8	421.8	478.6		75.2	79.8	35.2	190.2	26.6	230.6		119.5		1045.5
31/12/2018*			56.8	369.6	426.4		75.8	77.6	49.0	202.4	10.4	209.9		114.6		963.7

£50m Fidelity equities sold in Dec 2012 to fund Standard Life and Baillie Gifford DGF allocations.

@ Assets sold by Fidelity (£170m) and Baillie Gifford (£70m) in Dec 2013 to fund MFS and Blackrock global equities.

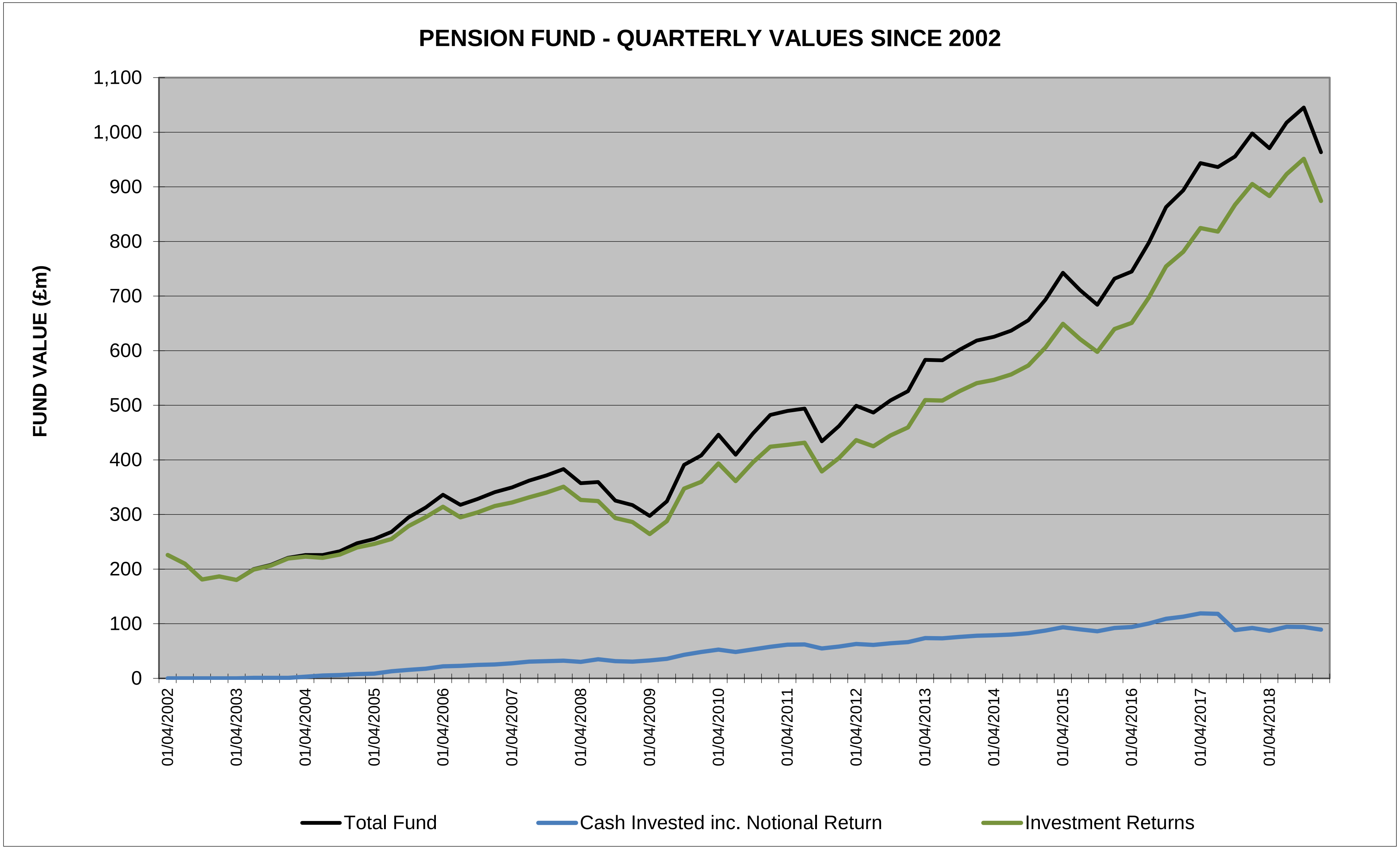
$ £32m Blackrock global equities sold in July 2017 to pay group transfer value re Bromley College.

& Assets sold by Baillie Gifford (£51m), Standard Life (£29m) and Blackrock (£19m) in Feb 2018 to fund Fidelity MAI and Property funds.

£ Assets sold by Blackrock (£120m) in May 2018 to fund Schroder MAI fund.

^ Assets sold by Blackrock (£20m) in August 2018 to fund Fidelity Property fund.

* Assets sold by Blackrock (£13.7m) in December 2018 to fund Fidelity Property fund.



PENSION FUND - QUARTERLY VALUES SINCE 2002
FUND VALUE (£m)
1,100
1,000
900
800
700
600
500
400
300
200
100
0
01/04/2002
01/04/2003
01/04/2004
01/04/2005
01/04/2006
01/04/2007
01/04/2008
01/04/2009
01/04/2010
01/04/2011
01/04/2012
01/04/2013
01/04/2014
01/04/2015
01/04/2016
01/04/2017
01/04/2018
Total Fund
Cash Invested inc. Notional Return
Investment Returns

PENSION FUND MANAGER PERFORMANCE TO DECEMBER 2018

Portfolio	Month %	3 Months %	YTD %	1 Year %	3 Years %	5 Years %	Since Inception %
Baillie Gifford Global Equity	-7.05	-12.47	-2.83	-3.60	14.40	12.61	8.04
Benchmark	-6.84	-10.56	1.16	-3.27	12.53	10.47	7.22
Excess Return	-0.21	-1.91	-3.99	-0.33	1.87	2.14	0.82
Baillie Gifford Fixed Income	1.13	0.28	-1.96	-1.43	4.29	5.14	4.98
Benchmark	1.51	1.09	-0.15	-0.58	4.59	5.31	5.00
Excess Return	-0.38	-0.81	-1.82	-0.85	-0.30	-0.17	-0.02
Blackrock Global Equity	-6.36	-11.47	-1.15	-5.06	12.64	10.83	11.05
Benchmark	-6.84	-10.56	1.16	-3.27	12.53	10.48	10.84
Excess Return	0.48	-0.90	-2.31	-1.79	0.12	0.35	0.21
Fidelity Fixed Income	1.12	0.91	0.22	-0.61	5.41	6.18	6.47
Benchmark	1.70	1.09	0.01	-0.47	4.34	5.30	5.66
Excess Return	-0.58	-0.17	0.22	-0.14	1.07	0.89	0.82
Fidelity MAI	-1.17	-3.19	-0.95				-2.14
Benchmark	0.38	1.13	3.33				3.67
Excess Return	-1.54	-4.32	-4.27				-5.81
Fidelity Property	0.92	2.42	0.91				1.52
Benchmark	0.89	2.40	2.41				4.36
Excess Return	0.02	0.02	-1.50				-2.83
MFS Global Equity	-7.90	-8.94	1.56	-4.26	11.43	11.26	11.58
Benchmark	-6.88	-10.67	0.74	-3.79	11.92	9.88	10.15
Excess Return	-1.02	1.73	0.82	-0.47	-0.49	1.38	1.43
Schroder MAI	-2.40	-4.90					-4.54
Benchmark	0.41	1.23					2.89
Excess Return	-2.81	-6.13					-7.43
Total Fund	**-4.89**	**-7.94**	**-0.64**	**-3.01**	**11.05**	**10.10**	**8.64**
Benchmark	**-3.75**	**-5.91**	**1.57**	**-1.09**	**10.38**	**9.06**	
Excess Return	**-1.14**	**-2.03**	**-2.20**	**-1.92**	**0.68**	**1.04**	
PIRC universe average		-4.7	n/a	-0.9	9.0	7.7	
N.B. returns may differ to fund manager reports due to different valuation/return calculation methods							

EARLY RETIREMENTS

A summary of early retirements and early release of pension on redundancy by employees in Bromley's Pension Fund in the current year and in previous years is shown in the table below. With regard to retirements on ill-health grounds, this allows a comparison to be made between their actual cost and the cost assumed by the actuary in the triennial valuation. If the actual cost of ill-health retirements significantly exceeds the assumed cost, the actuary will be required to consider whether the employer's contribution rate should be reviewed in advance of the next full valuation. In the last valuation of the Fund (as at 31st March 2016), the actuary assumed a figure of 1.2% of pay (approx. £1.2m p.a from 2017/18), compared to £1m in the 2013 valuation, and £82k p.a. in the 2010 valuation. In 2015/16 there were nine ill-health retirements with a long-term cost of £1,126k, in 2016/17 there were six with a long-term cost of £235k, in 2017/18 there were five with a long-term cost of £537k, and in the first three quarters of 2018/19 there were two with a long-term cost of £214k. Provision has been made in the Council's budget for these costs and contributions have been and will be made to reimburse the Pension Fund, as result of which the level of costs will have no impact on the employer contribution rate.

The actuary does not make any allowance for other (non-ill-health) early retirements or early release of pension, however, because it is the Council's policy to fund these in full by additional voluntary contributions. In 2015/16 there were 23 non ill-health retirements with a total long-term cost of £733k, in 2016/17 there were 22 with a total cost of £574k, in 2017/18 there were ten with a long-term cost of £245k, and in the first three quarters of 2018/19 there were six with a long-term cost of £345k. Provision has been made in the Council's budget for severance costs arising from LBB staff redundancies and contributions have been and will be made to the Pension Fund to offset these costs. The costs of non-LBB early retirements are recovered from the relevant employers.

Long-term cost of early retirements	**Ill-Health**		**Other**	
	No	£000	No	£000
Qtr 3 – Dec 18 - LBB	-	-	-	-
- Other	-	-	-	-
- Total	-	-	-	-
2018/19 to date - LBB	3	292	4	309
- Other	1	65	2	36
- Total	4	357	6	345
Actuary's assumption - 2016 to 2019		1,200 p.a.		N/a
- 2013 to 2016		1,000 p.a.		N/a
- 2010 to 2013		82 p.a.		N/a
Previous years – 2017/18	5	537	10	245
– 2016/17	6	235	22	574
– 2015/16	9	1,126	14	734
– 2014/15	7	452	19	272
– 2013/14	6	330	26	548
– 2012/13	2	235	45	980
- 2011/12	6	500	58	1,194

PENSION FUND REVENUE ACCOUNT AND MEMBERSHIP

	Final Outturn 2017/18 £’000’s	Estimate 2018/19 £’000’s	Actuals to 31/12/18 £’000’s
INCOME			
Employee Contributions	6,284	6,400	4,958
Employer Contributions			
- Normal	20,385	22,600	17,229
- Past-deficit	2,569	2,600	
Transfer Values Receivable	3,568	3,500	2,335
Investment Income			
- Re-invested	8,805	8,800	8,049
- Distributed to Fund *	0	8,600	6,201
Total Income	41,611	52,500	38,772
EXPENDITURE			
Pensions	26,332	26,800	20,497
Lump Sums	5,801	6,000	5,002
Transfer Values Paid	3,842	2,500	2,065
Administration			
- Manager fees	3,654	3,900	1,612
- Other (incl. pooling costs)	1,114	1,200	552
Refund of Contributions	171	300	168
Total Expenditure	40,914	40,700	29,896
Surplus/Deficit (-)	697	11,800	8,876
MEMBERSHIP	**31/03/2018**		**31/12/2018**
Employees	6,198		6,227
Pensioners	5,185		5,308
Deferred Pensioners	5,537		5,758
	16,920		17,293
*** Distributed to Fund**		**3rd Quarter**	**Year To Date**
Fidelity MAI		1,237	2,482
Fidelity Property		380	769
Schroders MAI		1,954	2,950
		3,571	6,201

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Appendix 5

MJ HUDSON
Allenbridge

London Borough of Bromley Pension Fund

Quarterly Report

Q4 2018

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Performance Summary

The poor market conditions lead to a fall in the value of the fund in the fourth quarter of 2018 to £960M. The Fund underperformed its Strategic Benchmark quite significantly returning -7.94% over the quarter, slightly more than 2% below the benchmark return of -5.91%. The Fund return now lags the Strategic Benchmark by almost 2% over the year returning -3.01% against the benchmark return of -1.09%. Over the longer term the Fund continues to outperform its benchmark despite this setback.

It is the underperformance in this quarter particularly which has affected the one year performance numbers. It has been caused by three main factors, firstly the Fund entered the quarter overweight in Equities against its Strategic Benchmark with a 65% exposure against the benchmark at 60% and correspondingly underweight Bonds, Multi Asset Income and Property, secondly The Multi Asset Income portfolios have an absolute benchmark related to short term interest rates which generates a positive return for every quarter even if markets fall and thirdly Baillie Gifford which manages the majority of the Funds Global Equities underperformed in the quarter.

Looking at each of these issues in turn:

1. The 5% overweight in equities and corresponding underweights in other asset classes cost the Fund approximately -0.50% in performance terms at the Total Fund level. The outperformance of equity markets over recent quarters had increased the weighting of this asset class in the Fund against the Strategic Benchmark which has static weights.

   It would be worth discussing whether the Fund should have limits on the deviation of its actual weightings against the Strategic Benchmark and thereby to automatically rebalance as the relative performance of individual asset classes moves the Funds asset allocation away from the Strategic Benchmark.

2. Both Multi Asset Income portfolios have an absolute return target set against LIBOR (a measure of short term interest rates). Fidelity target a return of LIBOR +4% and Schroders a return of LIBOR +5% per annum, both over the long term. By having the slightly higher return target you can assume that the Schroders portfolio takes slightly more investment risk to achieve its target than Fidelity.

   The LIBOR based targets reflect the desired return of the portfolios over the longer term but will not reflect the performance of specific asset classes in any individual quarter. With short term interest rates currently set by the Bank of England at 0.75% per annum, both the Fidelity and Schroder return targets will always be positive irrespective of market returns. In a quarter where the vast majority of assets fell in value it will be almost impossible for either portfolio not to reflect this fall in its quarterly performance and thereby underperform its benchmark for that quarter. It is important, therefore, to look at the performance of these managers against their benchmark only over the longer term. This does not remove the fact that their performance against the benchmark in any specific quarter will affect the performance of the total Fund against its Strategic Benchmark for that quarter. The effect of this on the performance of the total Fund was approximately -1.0%. It is difficult to see an easy solution to this issue but remember it is less relevant over the longer term.

3. The Baillie Gifford global equity portfolio underperformed its benchmark by almost 2.0% in the quarter. This accounted for almost -0.75% of the underperformance at the total Fund level. Baillie Gifford invest with a philosophy which concentrates on a company's long term growth potential rather than any specific valuation criteria. They believe they are better able to analyse the long term growth potential of any business rather than calculate an exact valuation based on a company's short term profit numbers. They back this approach by investing over the long term which provides the time for this growth potential to be realised. They have performed exceptionally well over the long term and even after this set back have outperformed their benchmark by over 2% per annum over 5 years and by over 1% per annum since inception in 1999. This performance has added significant value to the Fund over the long term. The divergence of performance in the quarter is not out of line given the amount of investment risk in the portfolio against its benchmark. I would continue to back this manager to add value over the long term.

In total, these three items account for all of the Fund's underperformance against its benchmark of -2.03% over the quarter and the vast majority of the negative performance against the benchmark over the full year. Against this disappointing performance should be set the major asset allocation changes made by the Pensions Committee over the last 9 months. The Fund had a 75% allocation to equities as recently as 31/3/18. This has been reduced by firstly funding the departure of Bromley College purely with equities and then by allocating 20% of the Fund to Multi Asset income and 5% of the Fund to UK property, both of which performed better than equities in the final quarter of the year and since inception in last year. Because these moves are reflected in the Strategic Benchmark the benefit of these moves is not captured in the Fund's relative performance against its benchmark but have had a beneficial impact on the total value of the Fund and therefore the funding level when the next actuarial revaluation is done starting in March 2019.

Executive Summary

The fourth quarter of 2018 was one of those where the numbers tell the story. Because of that, below is a table of market returns in local currency. It is worth comparing the returns for Q4 with the returns for 2018 as a whole. This shows just how much the markets turned from a relatively stable, albeit low return environment, to one of 'risk off' and run for the cover of Government Bonds. The falls in equity markets in Q4, particularly in December, wiped out any small gain seen in the first 9 months of the year for all risk assets and boosted Government bond returns into positive territory. The fall in equities was exacerbated by light trading volumes over Christmas.

Market Indicators

Index (Local Currency)		Q4 2018	Q4	2018	2017
Equities					
UK Equities	FTSE 100 Index	6728.13	-9.44%	-8.31%	11.41%
UK Equities	FTSE All-Share Index	3675.06	-10.15%	-9.09%	12.57%
US Equities	S&P 500 Index	2506.85	-13.84%	-5.18%	20.79%
European Equities	EURO STOXX 50 Price EUR	3001.42	-11.77%	-10.99%	9.34%
Japanese Equities	Nikkei 225	20014.77	-17.34%	-13.22%	18.37%
Emerging Markets Equities	MSCI Emerging Markets	965.67	-7.47%	-14.42%	37.85%
Global Equities	MSCI World	1883.90	-13.48%	-8.19%	22.97%
Government Bonds					
UK Govt Bonds	Bloomberg Barclays UK Govt All Bonds TR	371.50	2.18%	0.49%	1.96%
Euro Govt Bonds	Bloomberg Barclays EU Govt All Bonds TR	236.06	1.76%	0.99%	-0.01%
US Govt Bonds	Bloomberg Barclays US Treasury TR Unhedged USD Index	2217.70	2.70%	1.18%	2.35%
Bond Indices					
Pan-European Investment Grade	Bloomberg Barclays Pan-European Aggregate Corporate TR Index Value Unhedged	226.28	-0.69%	-1.40%	2.03%
Pan-European High Yield	Bloomberg Barclays Pan-European HY TR Index Value Unhedged	367.70	-3.85%	-3.71%	5.91%
US Corporate Investment Grade	Bloomberg Barclays US Corporate Investment Grade TR Index Unhedged	175.03	-0.09%	-2.07%	6.37%
US High Yield	Bloomberg Barclays US Corporate High Yield TR Index Value Unhedged	1909.36	-4.72%	-2.18%	7.19%
Commodities					
Brent Crude Oil	Generic 1st Crude Oil, Brent, bbl.	53.80	-34.96%	-19.55%	-15.03%
Natural Gas	Generic 1st Natural Gas, MMBtu	2.94	-2.26%	-0.44%	26.11%
Gold	Generic 1st Gold, 100oz	1281.30	7.54%	-2.14%	-12.04%
Copper	Generic 1st Copper, lb	263.10	-6.20%	-20.28%	-24.09%
Currencies					
GBP/EUR	GBPEUR Spot Exchange Rate	1.11	-0.86%	-1.15%	4.18%
GBP/USD	GBPUSD Spot Exchange Rate	1.27	-2.19%	-5.68%	-8.68%
EUR/USD	EURUSD Spot Exchange Rate	1.15	-1.31%	-4.61%	-12.39%
USD/100JPY	USDJPY Spot Exchange Rate	109.66	-3.55%	-2.69%	3.79%
AUD/USD	AUDUSD Spot Exchange Rate	0.70	-2.51%	-9.81%	-7.70%
Alternatives					
Infrastructure	S&P Global Infrastructure Index	2289.51	-5.22%	-9.83%	19.83%
Private Equity	S&P Listed Private Equity Index	120.16	-17.79%	-12.99%	25.85%
Hedge Funds	Hedge Fund Research HFRI Fund-Weighted Composite Index	13488.92	-5.35%	-4.07%	7.30%
Property					
UK Property	UK House Price Index - Average	230630.00	-0.51%*	2.77%*	5.00%
Volatility					
VIX	Chicago Board Options Exchange SPX Volatility Index	25.42	111.83%	160.18%	-14.09%

*Up to November 2018

So, what was it that changed market sentiment in the fourth quarter?

The global economy continued to slow as the major economies advanced towards the latter stages of the business cycle with only Japan seeing a pick up from a natural disaster impaired Q3. Inflation fell, mainly driven by the fall in Oil prices which were down 35% during the quarter, this reinforced the feeling of a slowing economy.

	GDP		CPI		
	Q3 2018	Q4 2018*	Oct	Nov	Dec
UK	0.60%	0.30%	2.40%	2.30%	2.10%
US	3.40%	2.60%	2.50%	2.20%	1.90%
Eurozone	0.20%	0.30%	2.20%	1.90%	1.60%
Japan	-2.50%	2.10%	1.40%	0.80%	0.30%

What worried markets, I believe, was the initial lack of recognition of the slowdown from the US Federal Reserve which raised interest rates by 0.25% in September and then again in December. US rates now stand at 2.5%. With the new Fed chair, Jay Powell, an unknown quantity and his relationship with Trump already under some stress, market commentators had limited insight over the Fed's likely response to a slowdown and this created uncertainty. China also looked to be slowing, partly due to the effect of trade frictions with the US.

The lesson to take from this period is that, with many assets classes valued above historic levels, Central Banks withdrawing liquidity from markets and high levels of political stress globally, any further uncertainty can lead to a sharp sell-off in risk assets. Equity markets bottomed on the 27th December and following some more 'dovish' noises from the US Fed, suggesting a slower pace of future rate rises, risk assets have shown some recovery. At the time of writing (19/2/19) risk assets have reversed around 50% of the December sell off.

- US equities declined particularly steeply in December with the S&P 500 falling by 13.8% over the quarter; disappointing corporate earnings from tech stocks, particularly Amazon and Alphabet, which missed revenue targets, gave rise to investor concerns over the broader earnings slowdown. European stocks also declined given the backdrop. Continued uncertainties surrounding Brexit and the stability of the UK government continued to act as a drag on the UK market.

- In December, the Federal Reserve increased rates by 25 basis points to a range of 2.25%-2.50%, its fourth rate hike in 2018. The Bank of England kept interest rates at 0.75% - the highest level since 2009.

- US Treasury yields were lower and the yield curve flattened. 10-year UK government yields also fell from 1.59% to 1.28% over the period, as a flight-to-quality increased amidst Brexit and macroeconomic uncertainty.

- US Investment Grade (IG) bond yields did not follow Government yields lower leading to widened credit spreads, bucking the trend of narrowing spreads seen over the last few quarter. Press release research[1] suggested that $90 billion worth of bonds have been downgraded from A to BBB within Investment Grade, the largest amount since Q4 2015.

- Widening credit spreads were also present in the high-yield bond market as interest rate hikes and the high levels of corporate debt raised concerns over corporate creditworthiness.

- The dollar continued to strengthen in Q4, as trade tensions looked to be easing with the meeting of Presidents Trump and Xi at the G20 summit and interest rates were increased. Weakness in Sterling continued as unease over the potential Brexit agreement persisted. Yen strengthened in Q4, as investors looked for a safe haven.

- Gold rose by 7.5% over the quarter reversing the declining trend seen since the start of the year, as volatility in the stock markets and concerns over the global economy left investors seeking a safe haven. Equity markets volatility over the quarter made the VIX (a measure of equity price volatility) jump from 12.1 to 25.4.

[1] https://www.cnbc.com/2018/12/07/bond-markets-flashing-red-and-an-oil-plunge-could-make-things-worse.html

Global Outlook

The fourth quarter of 2018 served as an indicator of choppier waters ahead for investors; however, most market participants are looking forward to 2019 with a certain amount of nervousness that even rougher conditions loom large. While brighter days still punctuate the gloom on the release of strong jobs reports or surprisingly good earnings for some bellwether stocks, market sentiment has currently turned from cautious optimism that the bull market had room to run yet, to an acceptance that all good things come to an end.

The pessimism seems to be derived from three main areas: that the US Technology (FAANG[2]) stocks may have come back down to earth from unsupportable valuations and can no longer drive markets higher on their own; that the economic cycle which seemed to peak in 2018 might be showing signs that it is turning; and that central banks are aggressively draining liquidity from the global system even while inflation seems relatively tame and private sector balance sheets have failed to "repair the roof while the sun was shining" and not deleveraged to an extent which might have lowered borrowing costs and insulated against rising interest rates in the future.

Geopolitical events, from Trump's stalled trade war against China, to the possible denouement of Britain's Brexit saga, also create uncertainty and lend themselves to pessimistic forecasts as we look ahead, although successful trade resolutions are likely to cheer markets substantially.

The loudest prophets of doom, however, have come from those worried about the removal of liquidity from the global market system by central bankers keen to reverse more than a decade of unconventional monetary policy. Stan Druckenmiller's adage that "Earnings don't move markets, It's the Fed" was clearly on his mind as the billionaire investor took to the pages of the Wall Street Journal to warn Jay Powell about further rate rises, while Charles Gave describes the effects of quantitative tightening as signifying a change from there being "more money than fools" to "more fools than money". A possible sympathetic Fed response to these warnings, reneging on planned rate rises, has led some analysts to argue that a recession in 2020 is now more likely than one in 2019.

However, market contrarians do remain, but rather than prophesying doom, these contrarians argue that risk is overblown, that economic fundamentals remain strong and, that worries about the creditworthiness of borrowers has outstripped the reality. While some areas of the globe might not be as robust as they once were, the US and Britain, for example, still have full employment with signs of real wage growth, while the Bank of England released a blog post arguing that household debt fears should be considered overwrought. Far from rotating to more defensive stocks, or allocating more to cash, they argue that the best strategy is to remain fully invested, adding to positions as some valuations drop on market skittishness.

Although markets ended 2018 on a significantly lower note, partly affected by light trading over the Christmas period, these more optimistic voices help support market levels which still price in a relatively optimistic outlook for future corporate earnings. As 2019 proceeds and, more data points either continue to give support for both optimists and pessimists, or a pattern builds that the current valuation levels cannot be sustained, we shall see if those predicting a 2019 recession were right or whether the pain can be delayed for just a little longer.

Economic impact of Brexit

Brexit has proven to be a highly emotional subject and I will attempt to stick to investment and economic issues, nonetheless, these views are my own and not those of MJ Hudson Allenbridge.

Investment markets will be driven by the outlook for global economic growth and geopolitical risk going forward and, as such, the effects of Brexit will have a limited impact on global investment returns in the medium term. From a UK specific viewpoint, however, the impact could be more substantial. Uncertainty over the outcome of Brexit negotiations has already been detrimental to the UK economy with signs of companies delaying capital investment plans until they have a clearer view of the regulatory and trade environment they will be operating in going forward. Higher inflation, caused by the weakness of sterling, has also weakened consumer spending, although

[2] FAANG = Facebook, Amazon, Apple, Netflix and Google.

whether the fall in sterling was as a direct result of the outcome of the referendum or this event just underlined the overvaluation of the currency is a moot point.

Because mainland Europe is the UK's largest trading partner, any disruption to the flow of goods between these two trading partners will have a detrimental impact on both the UK and European economy. As such, Brexit will be negative for the UK economy in the short term whatever form it takes. The softer the Brexit the less this impact will be as the changes to trading regulations and practices will be reduced. A hard Brexit or no agreement could lead to substantial barriers to trade including tariffs and could create a sudden sharp shock to the economy. The question is whether this short term impact will be worth the greater flexibility this gives the UK government in setting future policy. The softer the Brexit the less the short term economic impact but the more the UK will remain bound by EU regulations and the less flexibility this will give the Government to set policy which directly benefits the UK economy, the harder the Brexit the greater the short term impact but the greater the freedom with which future economic policy can be set. The UK is an innovative and entrepreneurial society and I have no doubt it will recover from whatever form of Brexit is finally agreed but this may take some time and, under a no deal Brexit, it may take many years to fully recover from the disruption and higher trading costs incurred, with any savings from not contributing to the EU budget quickly lost in slower GDP growth and any potential recession lowering tax returns.

Performance report

Asset Class/ Manager	**Global Equities/ Baillie Gifford**
Fund AuM	£369m Segregated Fund; 38.5% of the Fund
Benchmark/ Target	MSCI All Countries World Index +2-3% p.a over a rolling 5 years
Adviser opinion	Manager continues to meet their performance target
Last meeting with manager	No meeting this quarter
Fees	0.65% on first £30m; 0.5% on next £30m; 0.35% thereafter

The manager underperformed their benchmark by -2.0% in the fourth quarter and although the portfolio has underperformed over the last year, over the longer term the manager has added significant value and continues to hit their performance target of outperforming the MSCI All Countries index by 2% per annum over a five year period. The manager made efforts to diversify the portfolio during the early part of 2018, introducing a number of new holdings to but always within their long term growth philosophy. Whilst the scale of the underperformance is high it is not out of balance with the level of investment risk taken in this portfolio. When equity markets fall it is often easier to mark down stocks whose valuation discounts future growth than those stocks trading close to their asset values or on a low multiple of annual cash flow and Baillie Gifford's investment approach is likely to make them underperform in rapidly falling markets. In this quarter, this effect was exasperated by the shift in sentiment on a number of high profile technology companies which had, until recently, been the darlings of the stock market and responsible for pushing the index higher. The manager's commitment to research and investment over the long term continues to drive the portfolio and should add value over the longer term.

Asset Class/ Manager	**Global Equities/MFS**
Fund AuM	£210m Segregated Fund; 21.9% of the Fund
Benchmark/ Target	MSCI All Countries World Index
Adviser opinion	
Last meeting with manager	2/10/18 John Arthur / Rob Almeida; David Holding
Fees	0.6% on first £25m; 0.45% on next £25m; 0.4% thereafter

The MFS Global Equity portfolio returned -8.9% in the third quarter, outperforming its benchmark by 1.7%. The manager has underperformed over the last 1 and 3 year periods but has outperformed their benchmark over 5 years by 1.4% which is a creditable performance. MFS have an investment philosophy which concentrates on companies with defendable business models on attractive stock market valuations and this acts as a good balance to the Baillie Gifford, growth orientate, portfolio covered above. It is also an investment style which is likely to outperform in rapidly falling markets as many of the investments in the portfolio have strong valuation support in the form of physical assets/annual cash flow or high dividend yield.

The performance remains within expected tolerances against the benchmark. The speed of technological change is undoubtedly undermining many, previously secure, business models. I have discussed with MFS how they monitor this issue and will pursue this discussion further in due course. I note the London CIV's intention to commence the search for a Global Equity Value manager latter this year and will follow this process with interest as it will provide a data point on what funds are available in this area as well as an insight into the CIV's capabilities in manager selection.

Asset Class/Manager	**Global Equity/ Blackrock**
Fund AuM	£10.4m Pooled Fund; 1.1% of the Fund
Benchmark/ Target	MSCI All Countries World Index
Adviser opinion	A decision needs to be taken with the remaining monies in this portfolio
Last meeting with manager	No meeting this quarter
Fees	0.3% of fund value

Much of this portfolio has now been realised to finance the Fund's investments into Multi Asset Income and UK Property. Action should now be taken with the remaining monies as they are not of a scale to influence the return of the Fund as a whole and add unnecessary complexity through the addition of an additional manager.

Blackrock invests this portfolio by analyses vast quantities of data from foot falls in shopping malls and credit card transitions to investors risk appetite and hedge funds investment flows. Each data point gives insight into the underlying economic situation, investor sentiment or individual company prospects. The manager uses short term changes in the data to act as an early indicator and the portfolio is repositioned automatically to take advantage of these predicted changes. The portfolio seems to outperform over relatively long periods and then suffer a more significant downturn when market change more rapidly and perhaps act more irrationally. The portfolio has performed roughly in-line with its benchmark over the longer term but has underperformed over the last year and 3 months.

Asset Class/Manager	**Fixed Interest/ Baillie Gifford**
Fund AuM	£57m Pooled Fund; 5.9% of the Fund
Benchmark/ Target	Tailored benchmark
Adviser opinion	Benchmark performance over the medium term
Last meeting with manager	No meeting this quarter
Fees	0.3% of fund value

The portfolio has a composite benchmark weighted 44% UK Government Bonds (GILTS) and 44% Non-Government Investment Grade Bonds with a 6% allocation to both Emerging Market Bonds and to High Yield Bonds. The portfolio has an average credit rating of single A, a duration of 8.7 years and is currently yielding 3.7%.

Whilst Government Bond prices rose during the fourth quarter as investors fled risk assets and sought security, all other bonds fell so the cost of credit rose and the lower the quality of that credit the more it rose. This portfolio has achieved below benchmark returns over the last quarter and year and has matched its benchmark over all longer time periods. Whilst the manager is taking limited investment risk against the benchmark at the current time the portfolio is overweight in both Emerging Market bonds and High Yield bonds against the benchmark both of which detracted from performance in the fourth quarter due to their higher credit risk.

Given the outlook for the UK economy of sluggish growth and flat interest rates, UK Government Gilts are unlikely to provide any return over their yield (sub 2% at present) unless market endure a prolonged period of global uncertainty and potential recession causing a more major reappraisal of risk appetite. However, exposure to Government Gilts does provide diversification in these circumstances and potentially be one of the few asset classes to provide positive returns in this environment.

Asset Class/Manager	Fixed Interest/ Fidelity
Fund AuM	£76m Unit Trust; 7.9% of the Fund
Performance target	50% Sterling Gilts; 50% Sterling Non-Gilts; +0.75 p.a rolling 3 year
Adviser opinion	Manager continues to meet long term performance targets
Last meeting with manager	John Arthur/ Pete Turner/Cllr Onslow
Fees	0.35% on first £10m; 0.3% on next £10m; 0.21% on next £30m; 0.18% thereafter

The Fund has a current duration of 9.5 years and a yield of 2.2% both of which are close to the benchmark. The uncertainties around an eventual Brexit deal have caused the manager to move very close to the benchmark in terms of yield, duration and credit quality. The manager remains cautious despite the higher yields now on offer in some areas of the market post the sell-off in the fourth quarter of 2018.

Whilst the portfolio underperformed marginally during the quarter it has performed well over the longer term outperforming its benchmark over 3 and 5 years and since inception in 1998 by close to 1% per annum. Given the low level of yields now available within this mandate and the lacklustre performance of the UK economy I feel it is unlikely that the manager will add such value over the near future.

With this in mind, Pete Turner, Cllr Onslow and I met with the manager in January of this year to discuss possible changes to the mandate. Fidelity manage a number of bond funds which may be suitable for your Fund to invest in, the most promising of which is their Multi Asset Credit fund which invests in a variety of different bond markets globally looking to generate performance through geographic asset allocation and via different credit sectors as well as through the selection of the individual bonds. This fund has a high degree of flexibility to manage investment risk and is less reliant on the performance of the UK Gilt market to generate investment returns. It does, however, take more credit risk and may underperform the existing mandate during a prolonged global downturn.

It is this balance between holding a low yielding asset in Government Bonds as at present or investing in a broader range of Credit Bonds which will provide a higher yield but more volatility and have the potential to correlate with Equities in the event of a major market fall. Ideally you select a manager who has the ability to switch asset allocation to more defensive Government Debt if they predict a market setback but this is hard to get right and few managers show real skill in predicting such an event. I have a further meeting arranged with Fidelity on this issue and will report back in due course.

Asset Class/Manager	Multi Asset Income/ Fidelity
Fund AuM	£76m Pooled Fund of Funds; 7.9% of the Fund
Performance target	LIBOR +4% p.a.
Adviser opinion	Too early to make any assessment
Last meeting with manager	No meeting this quarter
Fees	0.4% on first £20m; 0.3% on next £30m; 0.25% on next £100m; 0.18% thereafter

This mandate was funded on 20th February 2018. It invests across multiple asset classes including Alternatives e.g. property, infrastructure, leasing and direct lending, via a Fund of Funds approach. It has a target yield of 4% per annum and is designed to help cover the cash flow requirements of the Fund into the future.

The manager returned -3.2% in Q4, this was significantly below the benchmark return for the quarter. A comment about the benchmark is made earlier in this report. The portfolio is generating the required yield from a diverse set of assets but in a quarter where almost all asset classes fell it proved impossible to generate a positive return.

The Funds allocation to Multi Asset Income provides a source of income to cover pension payments but is also intended to provide some protection from falling markets such that the assets can continue to provide this level of income going forward. Over the fourth quarter global equity markets fell -13.5% and corporate bonds -2%, it is against this environment that the portfolios fall of -3.2% should be set. This seems a credible return given the state of markets and acts as a useful stress test for the asset class and the manager. The true ability of the manager will only be seen over the longer term but so far the diversification of the portfolio has provided some protection from falling markets as intended.

Asset Class/Manager	Multi Asset Income / Schroders
Fund AuM	£112m Pooled Fund; 11.6% of the Fund
Performance target	LIBOR +5%
Adviser opinion	Too early to make any assessment
Last meeting with manager	Manager presented at the last Pension Committee meeting
Fees	0.35% of fund value

£120m was invested into this fund during the second quarter of 2018. The portfolio returned -4.9% during the quarter, significantly below the benchmark return for the period. A comment about the benchmark is made earlier in this report. The most obvious comparison for this portfolio over shorter time period is the performance of the Fidelity Multi Asset income fund which is similar in structure to this one. Schroders portfolio has a slightly higher return target and as such will take slightly more investment risk to achieve this. In a quarter such as this one, where all investment risk failed to pay off, it is unsurprising to see the value of this portfolio fall. The return of -4.9% should be seen against the return of -3.2% achieved by the Fidelity portfolio and is therefore slightly disappointing.

During the quarter the manager reduced exposure to global equities and increased exposure to Government Bonds, Convertibles and Emerging Market Debt. The portfolio remains well diversified and is currently yielding 4.7% per annum.

Currently this portfolio is invested in a dollar fund with the currency risk then hedged back to Sterling for you as a UK based client. The manager has offered to create a Sterling based version of this fund which will reduce the amount of currency hedging and should be marginally positive for performance going forward, especially as US interest rates rise and the hedging the currency becomes more expensive. This is a sensible suggestion and it is pleasing to see the manager offer to do this at their own cost. There would therefore be no transaction costs incurred by the Fund is moving to this new vehicle. The Fund would initially be the only investor in the new vehicle which could hamper disinvestment somewhat if that became an issue. Longer term the manager is making this offer because they value you as a client and what to deliver the best returns possible, but also because they hope the new vehicle will be attractive to other UK based investors which could ease any future divestment by Bromley.

I recommend this be given serious consideration by the committee and if instructed will meet again with the manager to take this forward.

Asset Class/Manager	UK Property/ Fidelity
Fund AuM	£49m Pooled Fund; 5.1% of the Fund
Performance target	IPD UK All Balanced Property Index
Adviser opinion	Too early to make any assessment
Last meeting with manager	
Fees	0.75% of fund value

The portfolio returned 2.4% in the fourth quarter, in line with its benchmark. This made UK Property the best performing asset class during the quarter. A final investment into the fund was made during the quarter and the fund has now reached its intended allocation at 5% of the fund.

The fund now holds 45 properties spread across the UK and across all major property types. It has a 5% exposure to retail assets which is significantly below the index weighting and whilst it is seeing some pressure on lease terms in this area these are within current expectations. The fund has scope for rents to rise as vacancies are filled and rent free periods expire and although their view of the market is becoming more cautious in the shorter term they do still expect the fund to return 7-8% per annum over the longer term despite the potential for near term weakness with scope for short term volatility through the Brexit process.

Global Economy

While global expansion continues, albeit less synchronised than last year and at a slightly reduced pace from the summer, many major economies are now heading towards more advanced stages of the business cycle. The US Fed's less accommodative monetary policy stance, the US-China trade tensions and China's economic slowdown as it shifts towards consumption rather than investment, are putting pressures on the global economy.

Table 1: Quarterly GDP Growth Rate

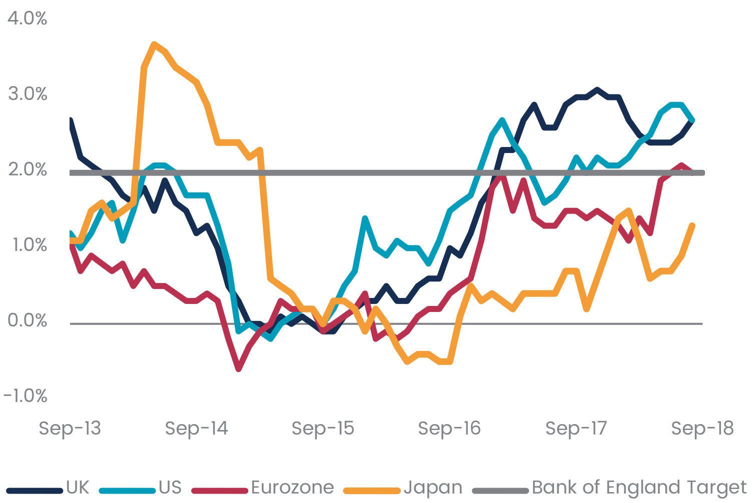
	US GDP	UK GDP	Eurozone GDP	Japan GDP
Q3 2018	3.50%	0.40%*	0.40%*	0.70%*
Q2 2018	4.20%	0.40%	0.40%	3.00%
Q1 2018	2.20%	0.10%	0.40%	-0.90%
Q4 2017	2.30%	0.40%	0.70%	0.90%

Source: Bloomberg. *Forecasts based on leading indicators.
Notes: UK Real GDP (Ticker: UKGRABIQ Index), US Real GDP (Ticker: EHGDUS Index, Eurozone Real GDP (Ticker: EUGNEMUQ Index), Japan Real GDP (Ticker: EHGDJP Index)

GDP: In the US, GDP numbers came in strong at 3.5%, slightly higher than expected as consumer spending underpinned growth, offsetting weak business investment and a drop in exports which widened the US trade deficit. The latter rose to a five-month high in July, as a result of the administration's protectionist trade policy - although towards the end of Q3, the trade deal between the US, Mexico, and Canada had been agreed.

In the UK, GDP figures were revised upwards as the economy grew faster than expected over the summer. However, there was still cause for concern as economic growth flat-lined in August.

Chart 1: 5-year CPI to September 2018



Source: Bloomberg.
Notes: UK: UK CPI EU Harmonised YoY NSA (Ticker: UKRPCJYR Index); US: US CPI Urban Consumer YoY NSA (Ticker: CPI YOY Index); Eurozone: Eurostat Eurozone MUICP All Items YoY Flash Estimate

CPI: US inflation fears calmed in Q3, as consumer prices rose less than expected. Inflation figures reached 2.3%, slowing down from 2.9% in Q2 2018. Slower increases in rental costs and energy prices contributed to the decline. However, low unemployment and wage increases in the US, which helped to boost consumer spending, also contributed to the Fed's decision to tightening its monetary policy stance.

In the UK, inflation generated by the fall in sterling following the EU referendum abated; however, households were squeezed further as CPI inflation unexpectedly rose to 2.7% in August - up from 2.4% in the second quarter. The inflation rate still remained above the Bank of England's 2% target, leading to an increase in interest rates to 0.75% – the second rate rise in 2018.

Central Banks: Central banks took further steps to slow or reverse their monetary stimulus programmes. The Bank of England increased rates due to the strengthening economy, underpinned by low unemployment levels, increasing consumer spending, and wage inflation. The Federal Reserve raised rates again in September by 25 basis points, to a range of 2.0%-2.25%, with a further rate rise expected later this year. In the Eurozone, the ECB is looking to keep rates constant at least through the summer of 2019 as its programme of quantitative easing comes to an end.

Political Headlines: Political turmoil continued to trouble markets as trade tensions between the US and China escalated. The Italian government set next year's budget deficit to 2.4%, which was more than expected by the market. In Mexico, the socialist candidate won the election by a landslide but seemed eager for better relations with the United States and Trump administration regarding NAFTA issues.

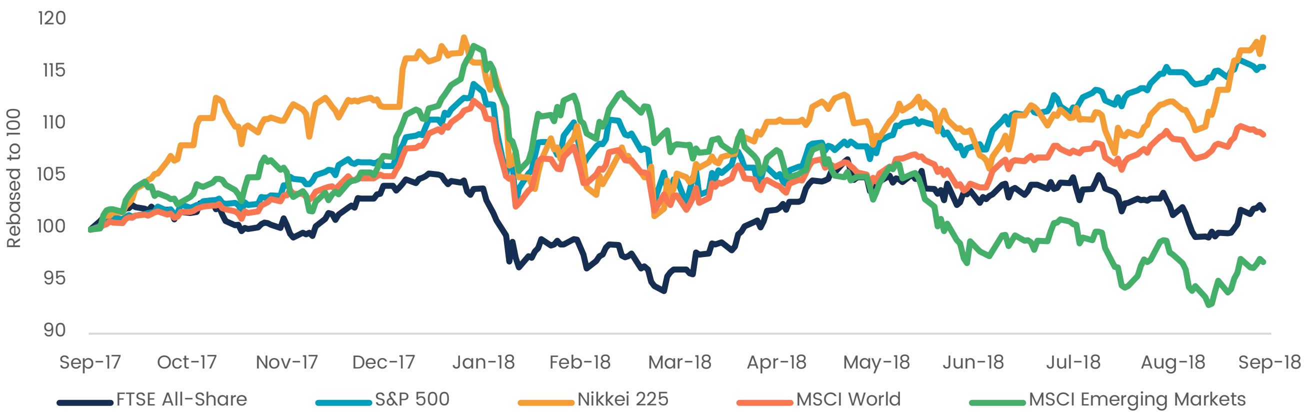
Equities

Global equities registered gains in Q3 partly due to the strength of the US economy; however, political uncertainties and fear of further trade tension escalations still dominated market concerns across the board with emerging markets enduring the most of the volatile conditions. The MSCI World returned 5.6%[3] in Q3, compared to 1.4% in the previous quarter.

UK: In addition to the above, continuing Brexit uncertainty contributed to the negative returns in Q3. UK financial and mining stocks were particularly affected due to their strong exposure to emerging markets. The FTSE 100 fell by -0.7% and FTSE-All share by -0.9%.

US: Performance in US equities remained robust over the period thanks to strong economic growth and corporate earnings. Further trade tariffs were introduced targeting China. Despite this, the US reached the milestone of the longest bull market in history, as the S&P 500 returned 7.7% and the Dow Jones Industrial Index rose by 9.6% over the quarter.

Chart 2: Global Equity Markets Performance



Source: Bloomberg. All in local currency. FTSE All-Share Index (Ticker: ASX Index) S&P 500 Index (Ticker: SPX Index)
Nikkei 225 Index (Ticker: NKY Index) MSCI World Index (Ticker: MXWO Index) MSCI Emerging Markets (Ticker: MXEF Index)

Japan: The MSCI Japan Index and the Nikkei both posted positive returns of 6.3% and 8.8%, as the Japanese Yen fell against the US Dollar boosting exports. Economic growth rebounded strongly as corporate earnings continued to improve in line with market expectations.

Emerging Markets: Emerging markets had another volatile quarter, due to the strength of the US dollar, global trade tensions, and an increase in risk aversion. South Africa and Turkey underperformed, the latter suffering the most with the sell-off in the Lira, as geopolitical tensions escalated with the US. However, Mexico outperformed following a decisive Presidential election result and an agreement with the US on the renegotiation of NAFTA. Russian equities benefited from strength in crude oil prices. The MSCI EM Index posted a return of -1.0% over the quarter.

EU: Worries over potential US tariffs on EU goods plagued the markets; this later cooled as an agreement to work towards zero tariffs on non-auto industrial goods materialised, while car tariffs were put on hold. Stock market returns were positive but financial stocks, and in particular Italian banks, weighed on performance, as there were worries over the Italian budget.

China: Further trade tensions with the US caused the MSCI China Index to fall by 7.7%. The US implemented tariffs on Chinese goods and, in September, announced a 10% tariff on $200 billion of Chinese goods, which resulted in the Chinese retaliating by enforcing their own tariffs on US imports. The central bank also introduced measures to try to stabilise the currency (Renminbi).

[3] All return figures quoted are Total Return, calculated with gross dividends reinvested. Source: Bloomberg.

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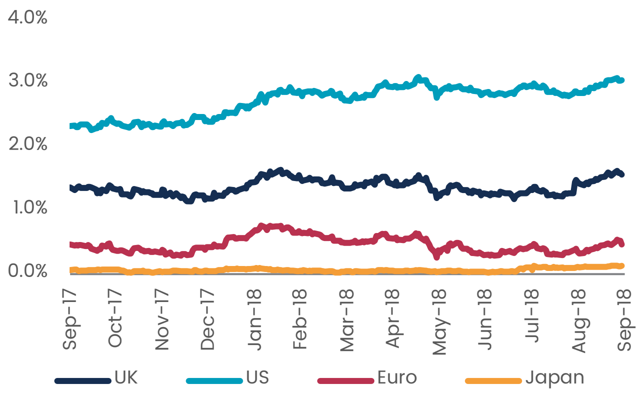
Fixed Income

Global bond markets were resilient over Q3: government bond yields rose due to positive macroeconomic data, mainly from the US, and corporate bonds registered positive total returns in local currency. However, the number of geopolitical issues continued to weigh on bond investor sentiment.

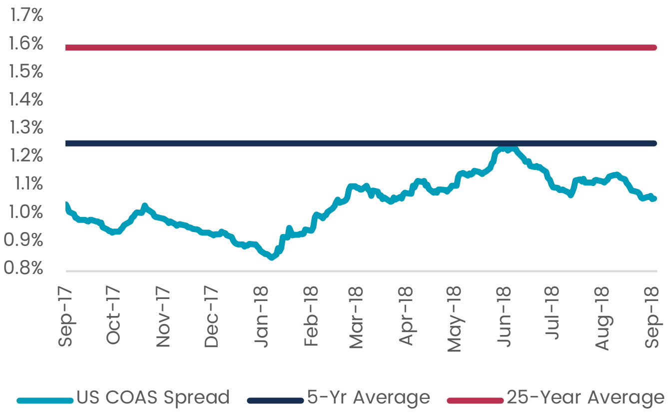
Government Bonds: Government bond yields rose over the quarter: US 10-year yields rose from 2.86% to 3.06%, Bund yields rose from 0.30% to 0.47% and UK Gilt 10-year yields rose from 1.42% to 1.57%. Another rate rise by the US Fed at the end of the year is widely expected while base rates in the UK reached their highest level since 2009. Italian 10-year bond yields rose from 2.68% to 3.06%, as concerns remained with the populist coalition as they announced a target budget deficit higher than market expectations and previous agreements with the EU.

Chart 3: Government Bond Yields



Source: Bloomberg.
Notes: US Generic Govt 10 Year Yield (Ticker: USGG10YR Index)
UK Govt Bonds 10 Year Note Generic Bid Yield (Ticker: GUKG10 Index)
Euro Generic Govt Bond 10 Year (Ticker: GECU10YR Index)

Chart 4: US Corporate Bond Spreads

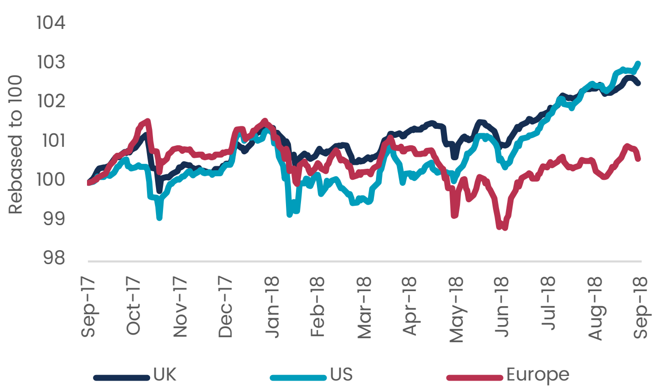


Source: Bloomberg. Notes: Bloomberg Barclays US Corporate Total Return Value Unhedged USD (Ticker: LUACTRUU INDEX)
Option-Adjusted Spreads (OAS) represent the difference between the index yield and the yield of a comparable maturity treasury.

Investment Grade Corporate Bonds: Global Investment Grade (IG) bonds registered positive total returns after two negative quarters, as credit spreads narrowed in response to the improving US macroeconomic data from a strong corporate earnings season. In Q3, the Bloomberg Barclays US Corporate Statistics returned 1.98%, up from -2.15% in Q2. However, the increase in interest rates and the high levels of corporate debt present risks to corporate creditworthiness in the long term.

High Yield Credit: High Yield (HY) credit registered higher positive returns over the quarter outperforming government bonds due to a strong corporate earnings season, rising inflatio, and steady economic growth. In Q3, the Bloomberg Barclays Pan-European High Yield bond index returned 1.56%, up from -2.15% in Q2. High yield bond issuance was low in the quarter which helped returns. The high coupon and relatively short duration gave HY credit opportunities to outperform the market, but volatility could quickly return, particularly with rising interest rates.

Chart 5: High Yield Corporate Bonds



Source: Bloomberg. Notes: Bloomberg Barclays Pan-European High Yield: Sterling Total Return Unhedged GBP (Ticker: I05892GB Index)
Bloomberg Barclays US Corporate High Yield Total Return Index Value Unhedged US (Ticker: LF98TRUU index)
Bloomberg Barclays Pan-European High Yield (Euro) TR Index Value Unhedged EUR (Ticker: LP02TREU Index)

Currencies

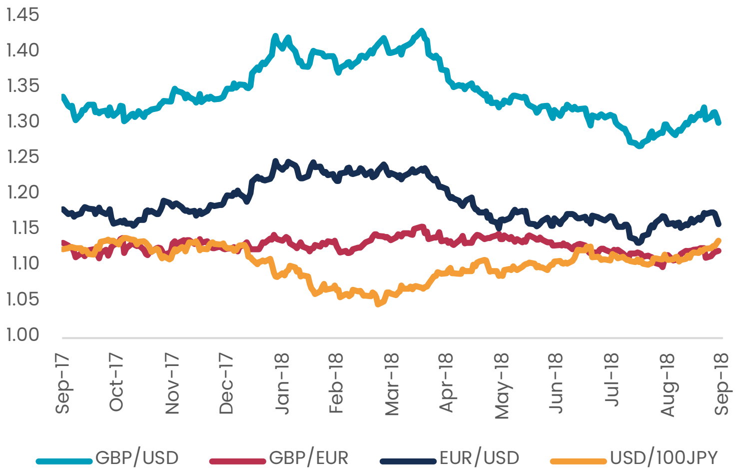
Earlier in the quarter, the dollar strengthened on the back of the strong US economic performance, which exposed frailties in emerging markets (EM), as EM currencies tend to move against the dollar. However, the dollar started to weaken as the Fed raised interest rates, despite ardent criticism from the White House while US trade talks with China did not materialise. Sterling remained volatile as the government continues to negotiate the terms of leaving the European Union and the weaker-than-expected economic data from August remained a concern.

Table 2: Currency Rates as At September 2018

	Quarter-end Value	% Quarter Change
GBP/EUR	1.12	-0.7%
GBP/USD	1.30	-1.3%
EUR/USD	1.16	-0.7%
USD/100JPY	1.14	2.7%

Source: Bloomberg.
Notes:
GBPEUR Spot Exchange Rate (Ticker: GBPEUR Currency)
GBPUSD Spot Exchange Rate (Ticker: GBPUSD Currency)
EURUSD Spot Exchange Rate (Ticker: EURUSD Currency)
USDJPY Spot Exchange Rate (Ticker: USDJPY Currency)

Chart 6: 1-Year Currency Rates of Major Currency Pairs

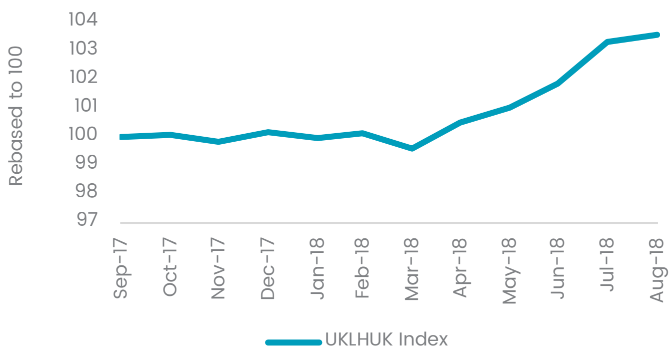


UK Property

Commercial property saw growth of 1.6% in the third quarter but, according to the CBRE, it was the weakest quarterly performance of 2018. Residential property remained flat, with continuing fears over household disposable income and debt servicing if interest rates were to venture higher.

Commercial Property: CBRE reported that UK commercial property values increased by 0.3%, down from the last quarter, with rental growth also lower at 0.1%. CBRE data showed that the industrial sector continued to outperform other sectors with capital values increasing by 0.9% and rental values by 0.4% over the last month of the quarter. The retail sector contracted further in Q3 in terms of both rental values (-0.6%) and capital values (-0.4%).

Chart 7: 1-Year UK House Price Index



Source: Bloomberg.
Notes:
UK House Price Index – Average Price for All Dwellings (Ticker: UKLHUK Index)

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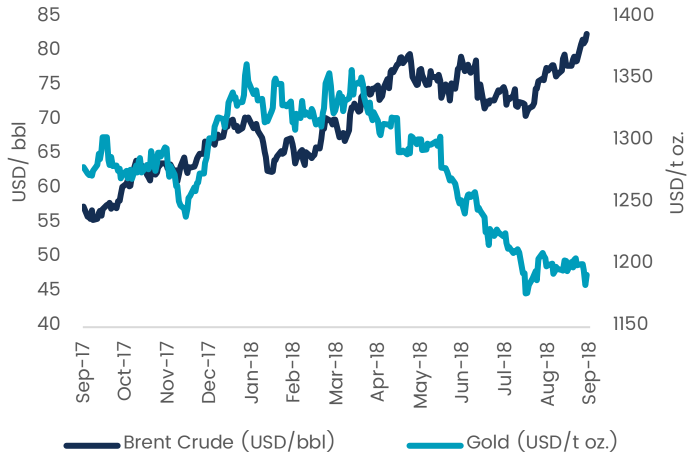
Commodities

Oil: In the second quarter, Brent Crude went above $80 per barrel for the first time since November 2014. Earlier in the quarter, Brent crude prices dipped after the US-China trade war caused volatility in emerging markets. Since then, Brent Crude oil prices have rallied to $82 per barrel due to steady demand and geopolitical tensions. A sharp drop in Venezuelan production, Libyan outages and US sanctions against Iran's oil imports helped to boost crude oil prices.

Gold: The price of gold continued to tumble and declined by 5% in the third quarter. Rising interest rates in the US and the strength of the dollar were the major contributors to the price fall. With the Fed looking to increase interest rates again in 2018 and in 2019, the bearish outlook on gold looks set to continue.

Chart 8: Gold and Brent Crude Oil Prices



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Report No.
FSD19032

London Borough of Bromley

PART 1 – PUBLIC

Decision Maker:	**PENSIONS INVESTMENT SUB-COMMITTEE**
Date:	**5th March 2019**
Decision Type:	Non-Urgent Non-Executive Non-Key
Title:	**LBB RESPONSE TO DRAFT LGPS STATUTORY GUIDANCE ON ASSET POOLING CONSULTATION**
Contact Officer:	Jo-Anne Chang-Rogers, Principal Accountant Tel: 020 8313 4292 E-mail: jo-anne.chang-rogers@bromley.gov.uk
Chief Officer:	Director of Finance
Ward:	All

1. Reason for report

1.1 This report asks Members to consider the response to the Government's consultation document "Local Government Pension Scheme – Statutory Guidance on Asset Pooling" and to delegate the finalisation of this Council's response to the consultation document to the Pension Investment Sub-Committee Chairman and the Director of Finance. The draft statutory guidance was issued on 3 January 2019 and the 12 week consultation period closes on 28 March 2019.

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2. RECOMMENDATIONS

2.1 The Pensions Investment Sub-Committee is asked to:

(a) Consider the response to the consultation document "Local Government Pension Scheme – Statutory Guidance on Asset Pooling, attached as Appendix 1.

(b) Note the consultation document "Local Government Pension Scheme – Statutory Guidance on Asset Pooling, attached as Appendix 2.

(c) Agree that the Director of Finance, in consultation with the Chairman submits the formal consultation response which will incorporate views expressed at this meeting.

(d) Note that the final consultation response will be emailed separately to all members of the Pensions Investment Sub-Committee.

Impact on Vulnerable Adults and Children

1. Summary of Impact: Not Applicable

Corporate Policy

1. Policy Status: Existing Policy: The Council's Pension Fund is a defined benefit scheme operated under the provisions of the Local Government Pension Scheme (LGPS) Regulations, for the purpose of providing pension benefits for its employees. The investment regulations (The LGPS (Management and Investment of Funds) Regulations 2016) allow local authorities to use all the established categories of investments, e.g. equities, bonds, property etc, and to appoint external investment managers who are required to use a wide variety of investments and to comply with certain specific limits.

2. BBB Priority: Excellent Council.

Financial

1. Total cost of proposal: No additional cost

2. Ongoing costs Not Applicable:

3. Budget head/performance centre: Pension Fund

4. Total current budget for this head: £40.7m expenditure (pensions, lump sums, etc); £52.5m income (contributions, investment income, etc); £963.7m total fund market value at 31st December 2018)

5. Source of funding: Contributions to Pension Fund

Personnel

1. Number of staff (current and additional): 0.4 FTE

2. If from existing staff resources, number of staff hours: c 14 hours per week

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Legal

1. Legal Requirement: Statutory Requirement: Local Government Pension Scheme (LGPS) Regulations 2013, LGPS (Management and Investment of Funds) Regulations 2016.

2. Call-in: Not Applicable

Customer Impact

1. Estimated number of users/beneficiaries (current and projected): 6,316 current employees; 5,328 pensioners; 5,755 deferred pensioners as at 31st January 2019

Ward Councillor Views

1. Have Ward Councillors been asked for comments? Not Applicable

2. Summary of Ward Councillors comments: Not Applicable

3. COMMENTARY

3.1 **Responses to the draft Statutory Guidance issued for consultation**

Members were briefed at the Special Pensions Investment Sub-Committee meeting on 14th January 2019, that the draft "Local Government Pension Scheme – Statutory Guidance on Asset Pooling" had been issued by MHCLG on 3 January 2019. The consultation will remain open for 12 weeks and will close on 28 March 2019. The terms of the consultation are that responses should:

- Be sent to LGPensions@communities.gov.uk.
- indicate if the response is an individual response or on behalf of an organisation
- indicate which section of the guidance is being commented on.

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3.2 The MCHLG guidance will replace the section at pages 7 to 8 of Part 2 of the Guidance for Preparing and Maintaining an Investment Strategy, issued in September 2016 and revised in July 2017, which deals with regulation 7(2)(d) of the 2016 Regulations. It will also replace Local Government Pension Scheme: Investment Reform Criteria and Guidance, issued in November 2015.

3.3 Overall this guidance is statutory, as indicated by the title. However, this Statutory Guidance will require different levels of adherence. This draft guidance uses 'should' or 'may' or 'are expected'. The statutory nature of some of the guidance is indicated by the sections where pool members or pool companies '*are required'* or '*must'* comply.

3.4 A draft response to the consultation document is attached in Appendix One. The consultation document is attached as Appendix Two

4. POLICY IMPLICATIONS

4.1 The Council's Pension Fund is a defined benefit scheme operated under the provisions of the Local Government Pension Scheme (LGPS) Regulations, for the purpose of providing pension benefits for its employees. The investment regulations (The LGPS (Management and Investment of Funds) Regulations 2016) allow local authorities to use all the established categories of investments, e.g. equities, bonds, property etc, and to appoint external investment managers who are required to use a wide variety of investments and to comply with certain specific limits.

5. FINANCIAL IMPLICATIONS

5.1 There will be no additional costs arising from the consultation response.

6. LEGAL IMPLICATIONS

6.1 The statutory provisions relating to the administration of the Local Government Pension Scheme are contained in the Local Government Pension Scheme (LGPS) Regulations 2013. The investment regulations (The LGPS (Management and Investment of Funds) Regulations 2016) set out the parameters for the investment of Pension Fund monies.

6.2 As set out in paragraph 3.3, the draft guidance includes some aspects which reflect legislation or regulation. Compliance with these is mandatory. Other aspects of the statutory guidance must be complied with, unless there are compelling reasons not to do so, which must be considered against the overall government framework for the LGPF. Finally some elements will be general guidance which we must consider and should comply with, unless we have good reason not to do so.

Non-Applicable Sections:	
Background Documents:	Local Government Pension Scheme – Statutory Guidance

(Access via Contact Officer)	on Asset Pooling

Appendix One

London Borough of Bromley Response to		
Draft - Local Government Pension Scheme – Statutory Guidance on Asset Pooling		
Section/Paragraph Reference	**Extract of Consultation document text**	**LBB Response**
Foreword	" …and significant annual savings have already been delivered, with the pools forecasting savings of up to £2bn by 2033…..	The Council has in previous consultations on pooling raised concerns about the opportunities to work with other councils to reduce management fees and the risk of any pooled savings being offset by significant organisational costs of the pools. The Council will always welcome measures to reduce costs which are not detrimental to fund performance. We would welcome the sharing of evidence of the savings identified and any comparison data between pools. It is important to consider whether there were opportunities to deliver savings without the use of a costly pool. After allowing for the transitional costs and annual service fees/development charge for being part of the London CIV it would take up to 9 years to fully recover the costs arising from the transfer of 40% of the Council's pension fund investment. We would welcome the sharing of evidence of the savings identified and any comparison data between pools.
Section 3 Structure and scale	3.1 All administering authorities must pool their assets in order to deliver the benefits of scale and collaboration. These include: • reduced investment costs without affecting gross risk-adjusted returns	This Council recognises that it must comply with government requirements relating to being part of a 'pool'. We welcome the benefits of scale and collaboration. However, we have a fiduciary duty to pension fund members and accountability to the council tax payer. We do not wish

London Borough of Bromley Response to		
Draft - Local Government Pension Scheme – Statutory Guidance on Asset Pooling		
Section/Paragraph Reference	**Extract of Consultation document text**	**LBB Response**
	• reduced costs for services such as custody, and for procurement • strengthened governance and stewardship and dissemination of good practice • greater investment management capacity and capability in the pool companies, including in private markets • increased transparency on total investment management costs • diversification of risk through providing access to a wider range of asset classes, including infrastructure investments	to be compelled to pool assets, where it is at the expense of higher performance. We have a track record of success in investment decisions and we would have possibly had different procurement choices which could have had a detrimental impact on the performance achieve. We have always responded on the basis that being part of a pool should be on a voluntary basis, recognizing that a pool may provide benefits to some administering authorities. Transition costs should be included in savings calculations. To our knowledge transition costs have not been collected (from us) or monitored. Therefore reported projected savings may not be as large as anticipated or reported. Transferring assets into a pool creates taxation costs and the impact of transitional costs should not be underestimated.
Section 3 Structure and scale	*Regular review of active and passive management* 3.6 Pool members, working with the pool company, should regularly review the balance between active and passive management in the light of performance net of total costs. They should consider moving from active to passive management where active management has not generated better net performance over a reasonable period. Pool members should also seek to ensure	This council favours regular review. However, this draft guidance seems to favour passive management. This council has selected asset managers who invest over the long term. The performance of the LB Bromley Fund is demonstrated by winning the LGPS Investment Performance of the Year in 2017 and LGPS Fund of the Yea (assets under £2.5bn) in 2018. The performance of the LB Bromley Fund managers has undoubtedly added value to

London Borough of Bromley Response to		
Draft - Local Government Pension Scheme – Statutory Guidance on Asset Pooling		
Section/Paragraph Reference	**Extract of Consultation document text**	**LBB Response**
	performance by asset class net of total costs is at least comparable with market performance for similar risk profiles.	the Fund. In addition, long term investing has had the benefit of allowing a manager to fully imbed Environmental, Social and Governance (ESG) factors into their investment philosophy. These issues have relevance over the longer timescale. ESG factors do not do as well with passive investing, the timescales are much shorter and the manager does not have time to build the constructive dialogue with the companies they are investing in. To illustrate the benefits of active fund management the Council has received net added value of around £100m with two global equity fund managers, compared with the equivalent passive investments.
Section 4 - Governance	4.2 Pool members, through their internal governance structures, are responsible for effective governance and for holding pool companies and other service providers to account. 4.4 Those who serve on Pension Committees and equivalent governance bodies in pool members should therefore take a long term view of pooling implementation and costs. They should take account of the benefits across the pool and across the scheme as a whole, in the interests of scheme	As a pool member, this council supports the principle of holding pool companies and other service providers to account. We would prefer a more direct influence on investments as indicated earlier. This council supports the principle of taking a long term view and believes that the long term view should also apply to investment strategies. The Council has a duty to secure best value to its council tax payers in the short, medium and longer term. It cannot agree to the regulations seeking a direction that could be at the detriment of its council tax

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London Borough of Bromley Response to		
Draft - Local Government Pension Scheme – Statutory Guidance on Asset Pooling		
Section/Paragraph Reference	**Extract of Consultation document text**	**LBB Response**
	members, employers and local taxpayers, and should not seek simply to minimise costs in the short term.	payers, particularly as a pool could make procurement decisions that could have a negative (or less positive) impact on the performance of the fund.
	4.5 Local Pension Boards of pool members have a key role in pool governance, given their responsibilities under the LGPS Regulations 2013 (regulation 106 (1)) for assisting authorities in securing compliance with legislation, and ensuring effective and efficient governance and administration of the LGPS. They can provide additional scrutiny and challenge to strengthen pool governance and reporting, and improve transparency and accountability for both members and employers.	This council will support governance arrangements that improve pool transparency and accountability and allow scrutiny and constructive challenge to take place.
	4.8 Pool members collectively through their pool governance bodies should decide the pool's policy on which aspects of asset allocation are strategic and should remain with the administering authority, and which are tactical and best undertaken by the pool company. Pool governance bodies, when determining where such decisions lie, should be	This guidance considers the trade off between 'choice and lower costs'. Investment return must also be a consideration and pool members should not be compelled to transition assets and forego their choices where proven higher returns are demonstrated.

London Borough of Bromley Response to		
Draft - Local Government Pension Scheme – Statutory Guidance on Asset Pooling		
Section/Paragraph Reference	**Extract of Consultation document text**	**LBB Response**
	mindful of the trade-off between greater choice and lower costs and should involve the pool company to ensure the debate is fully informed on the opportunities and efficiencies available through greater scale.	
Section 5 - Transition of assets to the pool	5.1 Pool members should transition existing assets into the pool as quickly and cost effectively as possible. Transition of listed assets should take place over a relatively short period. *Temporary retention of existing assets* 5.4 In exceptional cases, some existing investments may be retained by pool members on a temporary basis. If the cost of moving the existing investment to a pool vehicle exceeds the benefits of doing so, it may be appropriate to continue to hold and manage the existing investment to maturity before reinvesting the funds through a pool vehicle	This council supports the principle that asset allocation should be cost effective, but does not agree that transition of assets will be cost effective if transition must take place over a “relatively short” time period. The Council also supports having a choice to utilize alternative pools, rather than depend on one pool. There is a risk of creating a ‘monopolistic’ situation by not allowing choice across pools. Any choice should encourage a more proactive approach within pools and help keep a focus on keeping costs low and maximising performance. This council supports the principle in paragraphs 5.4, 5.5 and 5.6 that existing investments may be, for example (per 5.4) “….. should be held to maturity if costs exceed benefits”. The council does not agree that such retention should be considered as ‘exceptional’ or ‘temporary’.

London Borough of Bromley Response to		
Draft - Local Government Pension Scheme – Statutory Guidance on Asset Pooling		
Section/Paragraph Reference	**Extract of Consultation document text**	**LBB Response**
	5.6 "………Pool members should consider the long term costs and benefits across the pool, taking account of the guidance on cost-sharing, and the presumption should be in favour of transition to pool vehicles or moving such assets to the management of the pool company."	This council agrees that all members should take account of long term costs and benefits, but would not support the "presumption….in favour of transition" if it is to the detriment of performance and returns for individual pool members.
Section 6 - Making new investments outside the pool	6.1 Pool members should normally make all new investments through the pool company in order to maximise the benefits of scale. 6.2 A small proportion of a pool member's assets may be invested in local initiatives within the geographical area of the pool member or in products tailored to particular liabilities specific to that pool member. Local assets should: • Not normally exceed an aggregate 5% of the	Section 5 of the guidance suggests regular reviews should be undertaken for retained assets. This council feels that there should be a review and comparison undertaken, between pool returns and potential returns outside the pool, when new investments are due to be made. The Council would wish to have the choice to access a pool with a similar investment product which could generate greater savings, rather than rely on the outcome of negotiation of one pool. This council welcomes the opportunity to invest in assets outside the pool. The Council view is that investments should be in the best interest of the fund and council taxpayers and local investment should be on the basis that it represents the best investment choice.

London Borough of Bromley Response to		
Draft - Local Government Pension Scheme – Statutory Guidance on Asset Pooling		
Section/Paragraph Reference	**Extract of Consultation document text**	**LBB Response**
	value of the pool member's assets at the point of investment. • Be subject to a similar assessment of risk, return and fit with investment strategy as any other investment. 6.3 Pool members may invest through pool vehicles in a pool other than their own where collaboration across pools or specialisation by pools can deliver improved net returns.	This council welcomes the recognition that there may be higher returns outside of their own pool and that investment may be made across pools. This council believes this principle should be extended to wherever improved returns can be delivered.
Section 7 - Infrastructure investment	7.2 There is no target for infrastructure investment for pool members or pools, but pool members are expected to set an ambition on investment in this area. Pool companies may provide pool vehicles for investment in UK assets, or overseas assets, or both, as required to provide the risk and return profile to meet pool member investment strategies. However the Government expects pool companies to provide the capability and capacity for pools over time to move towards levels of infrastructure investment similar to overseas pension funds of comparable aggregate size.	This council's view remains that we should not be directed to invest in particular areas through regulation which could be detrimental to longer term investment returns, and which could also increase costs met by the local council tax payer. The ambition should be to ensure the fund meets the cost of pensions, meets future liabilities and represents the lowest cost to the council tax payers. There is a risk of creating an ambition for a product which may not be in the best interest of the fund.

London Borough of Bromley Response to		
Draft - Local Government Pension Scheme – Statutory Guidance on Asset Pooling		
Section/Paragraph Reference	**Extract of Consultation document text**	**LBB Response**
Section 8	Section 8 – ‘Reporting’ requirements	This council supports transparent reporting and compliance with CIPFA guidance. However section 8 underlines that membership of pool will make financial reporting more onerous and potentially add another layer of reporting.
8.2	8.2 In summary, pool member annual reports should include: • opening and closing value and proportion of pooled assets by asset class • opening and closing value and proportion of local assets by asset class • net and gross performance of pooled assets by asset class • total costs of pooled assets by asset class • for actively managed listed assets, net performance by asset class net of total costs compared to appropriate passive indices over a one, three and five year period • net and gross performance of local assets by asset class • total costs of local assets by asset class ▪ asset transition during the reporting year ▪ transition plans for local assets	This council welcomes the receipt of data from the pool. If councils are to comply with this Statutory Guidance and the recently accelerated statutory reporting deadlines, the LCIV Pool will need to provide prompt, timely and accurate data – including transition costs.

London Borough of Bromley Response to		
Draft - Local Government Pension Scheme – Statutory Guidance on Asset Pooling		
Section/Paragraph Reference	**Extract of Consultation document text**	**LBB Response**
	▪ pool set-up and transition costs, presented alongside in-year and cumulative savings from pooling ▪ ongoing investment management costs by type, with a breakdown between pooled assets and local assets	
	8.7 Pool members should ensure that pool companies report in line with the SAB Code of Cost Transparency. They should also ensure that pool companies require their internal and external investment managers to do so.	The council welcomes transparency from the Pool and its investment managers.
	8.8 Pool members should also ensure that the annual report of the pool company is broadly consistent with the reports of pool members, and with the Scheme Annual Report, in so far as it relates to their investments, and that the report includes a narrative to explain differences. These may arise for example from reporting periods of pool companies which differ from that of the pool member.	This council welcomes prompt provision of transparent data that this paragraph of the guidance entails. The council welcomes the ability to challenge that consistency between Annual Reports will necessitate. The government should include a requirement for the Pool to supply data within timescales to enable its members to meet their statutory reporting deadlines and consistency requirements. .

Local Government Pension Scheme

Statutory guidance on asset pooling

Contents

Foreword

The reform of investment management in the Local Government Pension Scheme (LGPS) for England and Wales began in 2015 with the publication of criteria and guidance on pooling of LGPS assets, following extensive consultation with the sector. LGPS administering authorities responded by coming together in groups of their own choosing to form eight asset pools.

Through the hard work and commitment of people across the scheme, those eight pools are now operational. Their scale makes them significant players at European or global level, and significant annual savings have already been delivered, with the pools forecasting savings of up to £2bn by 2033. Along the way many lessons have been learnt and great progress has been made in developing expertise and capacity, including in private markets and infrastructure investment.

This is a considerable achievement in itself, but there is still a long way to go to complete the transition of assets and to deliver the full benefits of scale. In the light of experience to date with pooling and the challenges ahead, authorities have requested guidance on a range of issues. The time is now right for new guidance to support further progress.

1 Introduction

1.1 This guidance sets out the requirements on administering authorities in relation to the pooling of LGPS assets, building on previous Ministerial communications and guidance on investment strategies, and taking account of the current state of progress on pooling. It is made under the powers conferred on the Secretary of State by Regulation 7(1) of The Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016 (the 2016 Regulations). Administering authorities are required to act in accordance with it.

1.2 This guidance replaces the section at pages 7 to 8 of Part 2 of *Guidance for Preparing and Maintaining an Investment Strategy*, issued in September 2016 and revised in July 2017, which deals with regulation 7(2)(d) of the 2016 Regulations. It also replaces *Local Government Pension Scheme: Investment Reform Criteria and Guidance,* issued in November 2015.

2 Definitions

2.1 This guidance introduces a set of definitions for use in this and future guidance, as follows:

'Pool' the entity comprising all elements of a Local Government Pension Scheme (LGPS) asset pool
'Pool member' an LGPS administering authority which has committed to invest in an LGPS pool and participates in its governance
'Pool governance body' the body used by pool members to oversee the operation of the pool and ensure that the democratic link to pool members is maintained (for example, Joint Committees and officer committees)
'Pool company' the Financial Conduct Authority (FCA) regulated company which undertakes selection, appointment, dismissal and variation of terms of investment managers, and provides and operates pool vehicles for pool members
'Pool fund' a regulated unitised fund structure operated by a regulated pool company, such as an Authorised Contractual Scheme (ACS)
'Pool vehicle' an investment vehicle (including pool funds) made available to pool members by a regulated pool company
'Pooled asset' an investment for which the selection, appointment, dismissal and variation of terms for the investment manager is delegated to a regulated pool company, or an investment held in a pool vehicle
'Retained asset' an existing investment retained by a pool member during the transition period
'Local asset' a new investment by a pool member which is not a pooled asset

3 Structure and scale

3.1 All administering authorities must pool their assets in order to deliver the benefits of scale and collaboration. These include:

- reduced investment costs without affecting gross risk-adjusted returns
- reduced costs for services such as custody, and for procurement
- strengthened governance and stewardship and dissemination of good practice

- greater investment management capacity and capability in the pool companies, including in private markets
- increased transparency on total investment management costs
- diversification of risk through providing access to a wider range of asset classes, including infrastructure investments

3.2 In order to maximise the benefits of scale, pool members must appoint a pool company or companies to implement their investment strategies. This includes:

- the selection, appointment, dismissal and variation of terms of investment managers, whether internal or external
- the management of internally managed investments
- the provision and management of pool vehicles including pool funds

It is for the pool companies to decide which investment managers to use for pool vehicles, including whether to use in-house or external management. Pool members may continue to decide if they wish to invest via in-house or externally managed vehicles.

3.3 Pool companies may be wholly owned by pool members as shareholders or may be procured and appointed by the pool members as clients.

3.4 A pool company must be a company regulated by the Financial Conduct Authority (FCA) with appropriate FCA permissions for regulated activities. This helps ensure the pools comply with financial services legislation, and provides additional assurance to scheme members and employers. Depending on the structure of the pool, appropriate permissions may include permissions for execution, acting as agent, provision of advice, or such other permissions as required by the FCA. Where regulated funds (e.g. in an ACS) are operated by the pool company it should comply with relevant UK legislation.

Regular review of services and procurement

3.5 Pool governance bodies, working with the pool company, should regularly review the provision of services to the pool, and the process of procurement, to ensure value for money and cost transparency. Where services are procured or shared by pool members, pool members should regularly review the rationale and cost-effectiveness of such arrangements, compared to procurement and management through the pool company. Pool members and pool companies should consider using the national LGPS procurement frameworks (www.nationallgpsframeworks.org) where appropriate.

Regular review of active and passive management

3.6 Pool members, working with the pool company, should regularly review the balance between active and passive management in the light of performance net of total costs. They should consider moving from active to passive management where active management has not generated better net performance over a reasonable period. Pool members should also seek to ensure performance by asset class net of total costs is at least comparable with market performance for similar risk profiles.

4 Governance

4.1 Pool members must establish and maintain a pool governance body in order to set the direction of the pool and to hold the pool company to account. Pool governance bodies should be appropriately democratic and sufficiently resourced to provide for effective decision making and oversight.

4.2 Pool members, through their internal governance structures, are responsible for effective governance and for holding pool companies and other service providers to account. Strategic asset allocation remains the responsibility of pool members, recognising their authority's specific liability and cash-flow forecasts.

4.3 Members of Pension Committees are elected representatives with duties both to LGPS employers and members, and to local taxpayers. Those who serve on Pension Committees and equivalent governance bodies in LGPS administering authorities are, in many ways, required to act in the same way as trustees in terms of their duty of care to scheme employers and members, but are subject to a different legal framework, which derives from public law. In particular while they have legal responsibilities for the prudent and effective stewardship of LGPS funds, LGPS benefits are not dependent on their stewardship but are established and paid under statute in force at the time.

4.4 Those who serve on Pension Committees and equivalent governance bodies in pool members should therefore take a long term view of pooling implementation and costs. They should take account of the benefits across the pool and across the scheme as a whole, in the interests of scheme members, employers and local taxpayers, and should not seek simply to minimise costs in the short term.

4.5 Local Pension Boards of pool members have a key role in pool governance, given their responsibilities under the LGPS Regulations 2013 (regulation 106 (1)) for assisting authorities in securing compliance with legislation, and ensuring effective and efficient governance and administration of the LGPS. They can provide additional scrutiny and challenge to strengthen pool governance and reporting, and improve transparency and accountability for both members and employers.

4.6 Local Pension Boards may also provide a group of knowledgeable and experienced people from which observers may be drawn if pool members wish to include observers on pool governance bodies.

Strategic and tactical asset allocation

4.7 Pool members are responsible for deciding their investment strategy and asset allocation, and remain the beneficial owners of their assets, in accordance with *Guidance for Preparing and Maintaining an Investment Strategy.*

4.8 Pool members collectively through their pool governance bodies should decide the pool's policy on which aspects of asset allocation are strategic and should remain with the administering authority, and which are tactical and best undertaken by the pool company. Pool governance bodies, when determining where such decisions lie, should be mindful of the trade-off between greater choice and lower costs and should involve the pool company to ensure the debate is fully informed on the opportunities and efficiencies available through greater scale.

4.9 Providing pool members with asset allocation choices through an excessively wide range of pool vehicles or investment managers will restrict the pool company's ability to use scale to drive up value. On the other hand maximising scale by significantly limiting asset allocation options may not provide all pool members with the diversification needed to meet their particular liability profile and cash flow requirements. Pool members should set out in their Funding Strategy Statement and Investment Strategy Statement how they, through the pool governance body, have balanced these considerations and how they will keep this under regular review.

4.10 Where necessary to deliver the asset allocation required by pool members, pool companies may provide a range of pool vehicles and in addition arrange and manage segregated mandates or access to external specialist funds. Pool governance bodies should ensure that their regulated pool companies have in place the necessary permissions to enable pool vehicles to be made available where appropriate.

4.11 Determining where asset allocation decisions lie will not be a one-off decision as pool member requirements will change over time. Pool governance bodies should ensure that a regular review process, which involves both pool members and pool companies, is in place.

5 Transition of assets to the pool

5.1 Pool members should transition existing assets into the pool as quickly and cost effectively as possible. Transition of listed assets should take place over a relatively short period.

5.2 Pool governance bodies, working with pool companies and, where appointed, external transition managers, should seek to minimise transition costs to pool members while effectively balancing speed, cost and timing, taking into account exit or penalty costs and opportunities for crossing trades.

5.2 The transition process will incur direct or indirect costs which may fall unevenly across pool members. For example, where the selected managers are used by some pool members but not others. In such cases pool members who are already using the selected manager may incur significantly lower (if any) transition costs than those who do not.

5.3 Inter-authority payments (or other transfers of value) may be desirable in order to share these costs equitably between pool members. The Government’s view is that such payments are investment costs within Regulation 4(5) of the 2016 Regulations, and payments made by a pool member to meet its agreed share of costs may be charged to the fund of that pool member, whether the payments are made to other pool members, the pool company, or another body by agreement.

Temporary retention of existing assets

5.4 In exceptional cases, some existing investments may be retained by pool members on a temporary basis. If the cost of moving the existing investment to a pool vehicle exceeds the benefits of doing so, it may be appropriate to continue to hold and manage the existing investment to maturity before reinvesting the funds through a pool vehicle.

5.5 In many cases there will be benefits in such retained assets being managed by the pool company in the interim. However pool members may retain the management of existing long term investment contracts where the penalty for early exit or transfer of management would be significant. These may include life insurance contracts (‘life funds’) accessed by pool members for the purpose of passive equity investment, and some infrastructure investments. Pool members may also retain existing direct property assets where these may be more effectively managed by pool members.

Regular review of retained assets
5.6 Pool members, working with the pool company, should undertake regular reviews (at least every three years) of retained assets and the rationale for keeping these assets outside the pool. They should review whether management by the pool company would deliver benefits. Pool members should consider the long term costs and benefits across the pool, taking account of the guidance on cost-sharing, and the presumption should be in favour of transition to pool vehicles or moving such assets to the management of the pool company.

6 Making new investments outside the pool

6.1 Pool members should normally make all new investments through the pool company in order to maximise the benefits of scale. Following the 2019 valuation, pool members will review their investment strategies and put revised strategies in place from 2020. From 2020, when new investment strategies are in place, pool members should make new investments outside the pool only in very limited circumstances.

6.2 A small proportion of a pool member's assets may be invested in local initiatives within the geographical area of the pool member or in products tailored to particular liabilities specific to that pool member. Local assets should:

- Not normally exceed an aggregate 5% of the value of the pool member's assets at the point of investment.
- Be subject to a similar assessment of risk, return and fit with investment strategy as any other investment.

6.3 Pool members may invest through pool vehicles in a pool other than their own where collaboration across pools or specialisation by pools can deliver improved net returns.

6.4 During the period of transition, while pool governance bodies and pool companies work together to determine and put in place the agreed range of pool vehicles, a pool member may make new investments outside the pool, if following consultation with the pool company, they consider this is essential to deliver their investment strategy. This exemption only applies until the pool vehicles needed to provide the agreed asset allocation are in place.

7 Infrastructure investment

7.1 Infrastructure investment has the potential to provide secure long term returns with a good fit to pension liabilities, and form part of investment strategies of authorities. The establishment of the pools was intended to provide the scale needed for cost-effective investment in infrastructure, and to increase capacity and capability to invest in infrastructure.

7.2 There is no target for infrastructure investment for pool members or pools, but pool members are expected to set an ambition on investment in this area. Pool companies may provide pool vehicles for investment in UK assets, or overseas assets, or both, as required to provide the risk and return profile to meet pool member investment strategies. However the Government expects pool companies to provide the capability and capacity for pools over time to move towards levels of infrastructure investment similar to overseas pension funds of comparable aggregate size.

7.3 Pool companies may provide pool vehicles for investment in existing (brownfield) or new (greenfield) infrastructure, based on an assessment of the benefits and risks in relation to pool member liabilities, and non-financial factors where relevant. Pool members may invest in their own geographic areas but the asset selection and allocation decisions should normally be taken by the pool company in order to manage any potential conflicts of interest effectively, maintain propriety, and ensure robust evaluation of the case for investment.

7.4 For the purpose of producing annual reports, infrastructure assets are defined in the Chartered Institute of Public Finance and Accountancy (CIPFA) guidance *Preparing the Annual Report* as follows:

Infrastructure assets are the facilities and structures needed for the functioning of communities and to support economic development. When considered as an investment asset class, infrastructure investments are normally expected to have most of the following characteristics:

- *Substantially backed by durable physical assets;*
- *Long life and low risk of obsolescence;*
- *Identifiable and reliable cash flow, preferably either explicitly or implicitly inflation-linked;*
- *Revenues largely isolated from the business cycle and competition, for example, through long term contracts, regulated monopolies or high barriers to entry;*
- *Returns to show limited correlation to other asset classes.*

Key sectors for infrastructure include transportation networks, power generation, energy distribution and storage, water supply and distribution, communications networks, health and education facilities, social accommodation and private sector housing.

Conventional commercial property is not normally included, but where it forms part of a broader infrastructure asset, helps urban regeneration or serves societal needs it may be.

7.5 All residential property is included in this definition of infrastructure. It is not restricted to social accommodation or private sector housing.

7.6 A variety of platforms may be required to implement the infrastructure investment strategies of pool members. Pool companies are expected to provide access to a range of options over time including direct and co-investment opportunities.

8 Reporting

8.1 Pool members are required to report total investment costs and performance against benchmarks publicly and transparently in their annual reports, following the CIPFA guidance *Preparing the Annual Report*, with effect from the 2018-19 report.

8.2 In summary, pool member annual reports should include:

- opening and closing value and proportion of pooled assets by asset class
- opening and closing value and proportion of local assets by asset class
- net and gross performance of pooled assets by asset class

- total costs of pooled assets by asset class
- for actively managed listed assets, net performance by asset class net of total costs compared to appropriate passive indices over a one, three and five year period
- net and gross performance of local assets by asset class
- total costs of local assets by asset class
- asset transition during the reporting year
- transition plans for local assets
- pool set-up and transition costs, presented alongside in-year and cumulative savings from pooling
- ongoing investment management costs by type, with a breakdown between pooled assets and local assets

8.3 Investments should be classed as pool assets on the basis of the definition in the CIPFA guidance *Preparing the Annual Report.*

For the purpose of defining those assets which are classed as being within an asset pool, 'pooled assets' are those for which implementation of the investment strategy – i.e. the selection, appointment, dismissal and variation of terms for the investment managers (including internal managers) – has been contractually, transferred to a third party out with the individual pension fund's control.

8.4 Any investment where a pool member retains the day to day management, or the responsibility for selecting or reappointing an external manager, is not a pool asset.

8.5 Pool members should provide a rationale for all assets continuing to be held outside the pool, including the planned end date and performance net of costs including a comparison which costs of any comparable pool vehicles. They should also set out a high level plan for transition of assets.

8.6 The SAB will publish an annual report on the pools based on aggregated data from the pool member annual reports, in the Scheme Annual Report. Pool members should comply with all reasonable requests for any additional data and information from the SAB to enable it to publish a comprehensive report.

8.7 Pool members should ensure that pool companies report in line with the SAB Code of Cost Transparency. They should also ensure that pool companies require their internal and external investment managers to do so.

8.8 Pool members should also ensure that the annual report of the pool company is broadly consistent with the reports of pool members, and with the Scheme Annual Report, in so far as it relates to their investments, and that the report includes a narrative to explain differences. These may arise for example from reporting periods of pool companies which differ from that of the pool member.

8.9 Pool members are required to report any change which results in failure to meet the requirements of this guidance to the LGPS Scheme Advisory Board (SAB) and to MHCLG.

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