

## PENSIONS COMMITTEE

17 March 2021

<b>Title:</b> Pension Fund Quarterly Monitoring 2020/21 – September to December 2020	
<b>Report of the Chief Operating Officer</b>	
<b>Open Report</b>	<b>For Information</b>
<b>Wards Affected:</b> None	<b>Key Decision:</b> No
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<b>Accountable Director:</b> Philip Gregory, Finance Director	
<b>Accountable Strategic Leadership Director:</b> Claire Symonds, Chief Operating Officer	
<b>Summary</b>  This report provides information for employers, members of London Borough of Barking and Dagenham Pension Fund and other interested parties on how the Fund has performed during the quarter 1 October to 31 December 2020.  The report updates the Committee on the Fund's investment strategy and its investment performance.	
<b>Recommendation(s)</b>  The Pension Committee is recommended to note:  (i) the progress on the strategy development within the Pension Fund,  (ii) the daily value movements of the Fund's assets and liabilities outlined in Appendix 1, and  (iii) the quarterly performance of pension funds collectively and the performance of the fund managers individually.	
<b>Reason(s)</b>	

## **1. Introduction and Background**

- 1.1 This report provides information for employers, members of London Borough of Barking and Dagenham Pension Fund (“the Fund”) and other interested parties on how the Fund has performed during the quarter 1 October to 31 December 2020 (“Q4”). The report updates the Committee on the Fund’s investment strategy and its investment performance. Appendix 2 provides a definition of terms used in this report. Appendix 3 sets out roles and responsibilities of the parties referred to in this report.
- 1.2 A verbal update on the unaudited performance of the Fund for the period 1 January to 28 February 2021 will be provided to Members at the Pension Committee.

## **2. Independent Advisors Market Background Q4 2020**

- 2.1 The official press release issued after both the November and December 2020 meetings of the monetary policy setting Federal Open Markets Committee (FOMC) of the US Federal Reserve included the statement “...The COVID-19 pandemic is causing tremendous human and economic hardship across the United States and around the world...” At his press conference following the December 2020 FOMC meeting Jay Powell the Chair of the US Federal Reserve stated “Economic activity has continued to recover from its depressed second-quarter level...Even so... the path ahead remains highly uncertain.” Despite this, buoyed by huge monetary stimulus from Central Banks, material fiscal intervention by governments and optimism regarding vaccine development both US and financial markets worldwide enjoyed another positive Quarter. The MSCI World Index was up over the Quarter 14% (in \$ terms) and 16% up for the calendar year 2020 despite COVID-19.
- 2.2 As with the two previous two Quarters the period October to December 2020 was clearly positive for US equities. The S&P 500 Index which had closed at 3,363 on 30 September closed at 31 December at 3,756 an increase of over 11%. All 11 sectors within the S&P 500 experienced a positive Quarter. Information Technology had yet another positive Quarter returning over 11% (and 42% for the calendar year making it the best performing sector in 2020). The Financial and Energy sectors which had suffered particularly as a result of COVID-19 experienced a clearly positive Quarter. Financials returned over 22% which did much to mitigate the earlier losses of 2020. The best performing sector was Energy which returned approaching 26% over the Quarter although such were the losses incurred earlier in 2020 that the sector ended the year at minus 37%. Despite COVID-19 the S&P 500 as a whole gained over 16% in 2020 with the Information Technology (+42%), Consumer Discretionary (+32%) and Communication (+22%) sectors all achieving particularly positive returns.
- 2.3 The Federal Open Markets Committee (FOMC) continued the extraordinary measures it had introduced earlier in 2020 to support both financial markets and the economy. At the December meeting the FOMC provided reinforced guidance on its asset purchase programme announcing it would continue to purchase at least \$80 billion of Treasury securities and at least \$40 billion of mortgage-backed securities per month “until substantial further progress has been made toward the Committee’s maximum employment and price stability goals.” In December both Congress and President Trump approved a further \$900 billion fiscal stimulus including payments of up to \$600 for an individual, \$1,200 for a married couple and \$600 per dependant child.

- 2.4 Following the Presidential election on 3 November 2020 it became apparent that President Trump had been defeated by (former) Vice President Joe Biden. This did not appear to perturb markets with the S&P 500 climbing steadily from 3,369 on 3 November to 3,756, an increase of 11%, by 31 December.
- 2.5 US gross domestic product (GDP) increased at an annual rate of 4.0% in the fourth quarter of 2020 (equivalent to 1% growth compared to the previous Quarter) according to data released by the Bureau of Economic Analysis (BEA) on 28 January 2021. The BEA release stated this reflected “both the continued economic recovery from the sharp declines earlier in the year and the ongoing impact of the COVID-19 pandemic, including new restrictions and closures that took effect in some areas of the United States.” GDP was, however, estimated to have declined by 3.5% in 2020.
- 2.6 The unemployment rate which had been 7.8% (revised) in September was down to 6.7% in December. Although much below the April high of 14.7% this is still almost double the pre COVID level of 3.5% as at January 2020. Inflation continued to be clearly below the US Federal Reserve target of 2%. Inflation as measured by the Personal Consumption Expenditures (PCE) index was 1.3% in December while Core PCE (which excludes changes in consumer energy prices and many consumer food prices) was 1.5%. The FOMC does not see a swift path to its inflation target, but it does see a path, with Chair Jay Powell stating at his December 2020 press conference that “the median inflation projection from FOMC participants rises from 1.2 percent this year to 1.8 percent next year and reaches 2 percent in 2023.” The University of Michigan Index of Consumer Sentiment was very slightly higher in December (80.7%) than September (80.4%) and therefore remained very clearly above the levels recorded following the outbreak of COVID-19 (71.8% in April and 72.3% in May).
- 2.7 Eurozone Equities had a successful Quarter with the MSCI EMU Index increasing by approaching 13% (in Euro terms) in contrast to the previous Quarter when it had been almost flat. As in the United States the financial and energy sectors which had fared particularly badly following the outbreak of COVID-19 were clearly positive this Quarter. There were encouraging announcements from November regarding vaccine development, together with further monetary policy stimulus by the European Central Bank ( ECB), and an agreement by EU leaders in December which overcame objections from Hungary and Poland which were holding up enactment of the 750 billion Euro Recovery Fund to be allocated amongst European Union states initially agreed in July.
- 2.8 While the Governing Council of the ECB did not extend its monetary policy initiatives at its October meeting it clearly signalled further likely loosening with the press release stating “In the current environment of risks clearly tilted to the downside...a thorough reassessment of the economic outlook” would be undertaken and that “the Governing Council will calibrate its instruments as appropriate...” In December the Governing Council introduced a number of initiatives to stimulate the eurozone economy. These included a further expansion of the Pandemic Emergency Purchase Programme from 1,350 billion to 1,850 billion and extending it from June 2021 to “at least the end of March 2022” as well as the extension of financing to banks to encourage further lending.
- 2.9 In Q4 2020 the Eurozone performed less robustly than other major economic areas. In contrast to both the United States and the UK where economic activity expanded (by 1%) the Eurozone contracted. Eurozone GDP decreased by 0.7% in Q4 2020

according to data released by Eurostat on 2 February 2021. Worryingly too deflation continued in the Eurozone throughout the Quarter with inflation at minus 0.3% in October, November and December 2020. Achievement of the ECB policy goal of inflation below but close to 2% over the medium term appears far away! Eurozone unemployment remained steady during the Quarter and was 8.3%, again supported by broad furlough schemes which have, so far, avoided significant expansion in unemployment in the Eurozone and will hopefully facilitate economic recovery going forward.

- 2.10 The FTSE All Share advanced over 12% during the Quarter with the bounce back by financial and energy sectors clearly contributing. Positive news regarding vaccine progress and market optimism during the Quarter that the UK and EU would avoid a no-deal Brexit (which they ultimately did on 24 December 2020) buoyed the UK equity market particularly the UK focussed FTSE 250 which advanced by over 18% over the Quarter. Notwithstanding a positive final Quarter, UK equities experienced a poor year in both absolute and relative terms with exposure to financials and energy and an under exposure to information technology weighing against positive performance. While world equities (as measured by the MSCI World Index) advanced by 16% in \$ terms (and 12% in £ terms) the FTSE All Share was down 10% (in £ terms). However, going forward, the UK market appears undervalued compared to other major markets and therefore a source of potential opportunity.
- 2.11 The Office for National Statistics announced on 12 February 2021 that UK GDP for the period October to December 2020 “is estimated to have grown by 1.0%, following revised 16.1% growth in Quarter 3.” However, the release goes on to state “Despite two consecutive quarters of growth, the level of GDP in the UK is 7.8% below its Quarter 4 2019 level.”
- 2.12 UK unemployment was 5% for the period September to November 2020 compared to 4% prior to the first COVID-19 lockdown in March 2020. The furlough scheme first introduced from March 2020 was extended in November 2020 to April 2021. In this respect the Minutes of the December meeting of the Bank of England Monetary Policy Committee (MPC) stated that “the extension of the government’s employment support schemes is likely to limit significantly the near-term rise in unemployment, although a substantial further increase is still likely over the next few quarters.” Consumer Price Inflation (CPI), which had been 1.5% in March 2020 continued to remain well below the Bank of England target of 2%. CPI which had been 0.5% in September was 0.7% in October, 0.3% in November and 0.6% in December. The Bank of England continues however to take the view that 2% inflation is possible in 2 years’ time.
- 2.13 The Bank of England MPC extended its support to the economy at its November meeting by increasing its planned purchases of “UK government bonds by an additional £150 billion” thereby increasing the planned level of quantitative easing from £745 billion to £895 billion. This further easing of monetary policy was in the context of clear concerns by the MPC, as expressed in the Minutes of their November 2020 meeting, regarding the UK economy and economic activity.
- 2.14 Japanese Equities (as measured by the Nikkei 225 Index) gained 18% over the Quarter. Over 2020 as a whole the Nikkei 225 gained 16%. Likely positive influences included COVID vaccine news and the election of Joe Biden as US President which is likely to result in both more predictable and traditional US foreign policy than under Donald Trump. In addition, the Japanese government announced a large fiscal

stimulus in December to both combat COVID-19 and provide for long term investment including in clean fuels and digital technology.

- 2.15 At its December 2020 meeting the Bank of Japan further expanded its already huge monetary stimulus and, significantly announced “the Bank will conduct an assessment for further effective and sustainable monetary easing, with a view to supporting the economy and thereby achieving the price stability target of 2 percent.” This review which is likely to be finalised in March 2021 was initiated “given that economic activity and prices are projected to remain under downward pressure for a prolonged period due to the impact of COVID-19.” Japan remained in deflation with Core CPI which had been minus 0.3% in September reaching minus 1.0% by December. The Bank of Japan target is plus 2% inflation.
- 2.16 Asian and Emerging Markets enjoyed a particularly positive Quarter partly facilitated by continuing US dollar weakness. For Emerging Markets, in general, rising commodity prices were also a boost factor. The MSCI AC Asia (excluding Japan) returned over 18% (in US \$ terms) and the MSCI Emerging Markets Index approaching 20%. South Korea, Taiwan and India were all notable positive performers. While the Chinese market rose, it underperformed Asia/Emerging Markets generally. The US government imposed further sanctions on Chinese companies while Alibaba was made subject of a monopoly probe by the Chinese authorities. Overall, 2020 was a positive, if volatile, year for Asian and Emerging Markets with the MSCI AC Asia (excluding Japan) returning 25% (in US \$ terms) and the MSCI Emerging Markets Index 18%.
- 2.17 The extensive and further increasing monetary policy initiatives of the major Central Banks were supportive of the continuing low yields of the leading Government Bonds – despite the contrary pull of potential or agreed fiscal initiatives by governments. The 10 Year Gilt Yield fell from 0.23 to 0.20 and the 10 Year Bund Yield fell from -0.52 to -0.57. The 10 Year US Treasury Yield remained below 1% but did rise from 0.68 to 0.91 with market commentators citing concerns regarding the prospect of increased fiscal stimulus under a Democrat President and Congress as a clearly contributing factor. Both investment grade and high yield corporate credit enjoyed another positive Quarter.
- 2.18 In Conclusion the October to December 2020 Quarter was clearly positive for financial markets. The calendar year 2020 saw, despite the huge human and economic cost of COVID-19, further clear advances in asset prices. Ultimately the credit for this must go to the huge stimulus initiatives of both the Central Banks and governments. The greatest benefit of these measures has however been in providing support and protection to both business and individuals in the face of an unprecedented worldwide challenge. This was in contrast to support provided by governments in the 2007-2009 financial crisis which was focussed on businesses rather than individuals. The question remains whether all this Central Bank (monetary) and government (fiscal) intervention will indeed be genuinely inflationary and help facilitate the achievement of the major Central Banks 2% inflation targets. Or perhaps it might result in inflation levels significantly above Central Bank targets which could ultimately adversely affect asset prices.

### 3. Overall Fund Performance

3.1 The Fund's externally managed assets closed Q4 valued at £1,255.59m, an increase of £92.32m from its value of £1,163.27m at 30 September 2020. The cash value held by the Council at 31 December 2020 was 1.23m, giving a total Fund value of £1,256.82m. The gross value of £1,256.82m includes a prepayment of £25.0m from the Council. The net asset value as at 31 December 2020, after adjusting for the prepayment and short term loan from the council was therefore £1,216.9m.

3.2 For Q4 the Fund returned 8.0%, net of fees, outperforming its benchmark by 2.9%. Over one year the Fund outperforming its benchmark by 2.1%, with a return of 11.6% and by 0.8% over two years, with a return of 12.1%. The Fund has also matched its benchmark over three years, with a return of 6.9%. Over five years the Fund has outperformed by 0.0%, with a return of 9.7%.

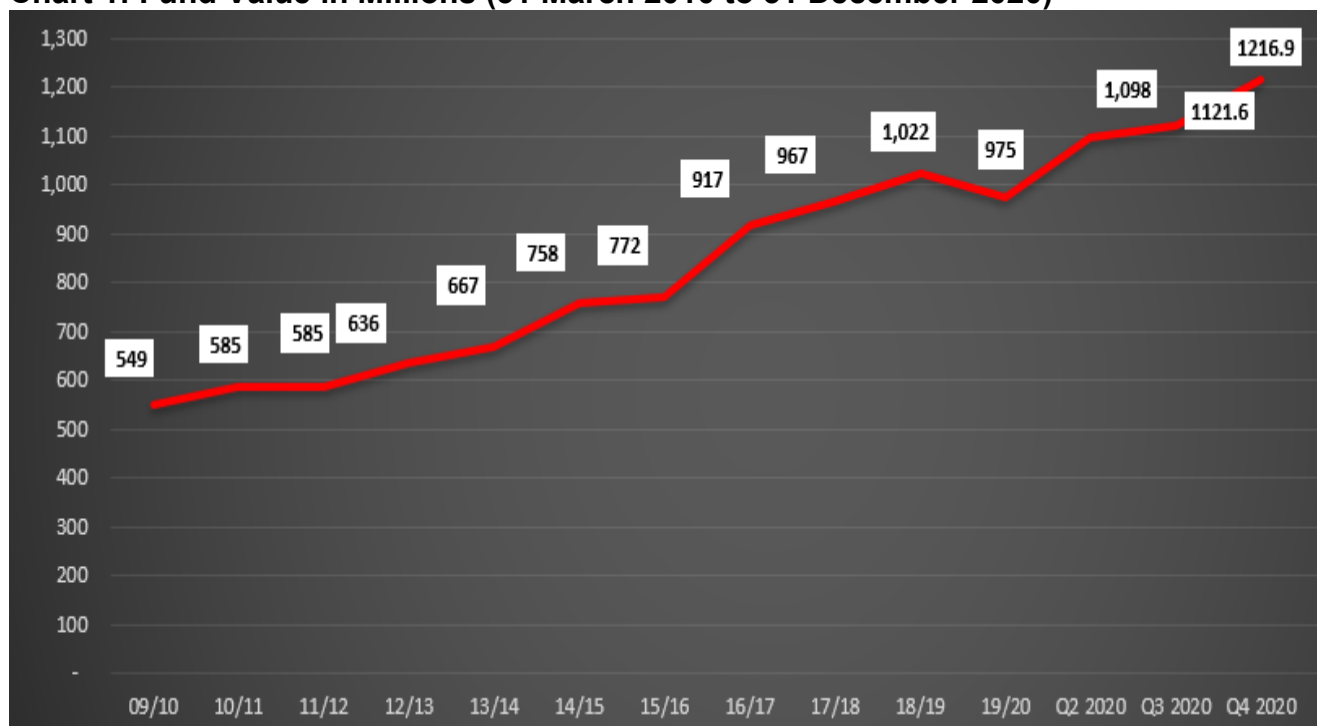
3.3 Compared to the LGPS universe of Funds, represented below by the PIRC Universe, the Fund has outperformed by 5.9% over one year and by 1.4% over three years. Over five years the Fund has outperformed by 0.4%. The Fund's returns are below:

**Table 1: Fund's 2020 and 2019 Quarterly and Yearly Returns**

Year	2020				2019				One Year	Two Years	Three Years	Five Years
	Q4	Q3	Q2	Q1	Q4	Q3	Q2	Q1				
<b>Fund Return</b>	<b>8.0</b>	<b>2.8</b>	<b>12.3</b>	<b>(11.4)</b>	<b>2.2</b>	<b>1.4</b>	<b>3.3</b>	<b>5.8</b>	<b>11.6</b>	<b>12.1</b>	<b>6.9</b>	<b>9.7</b>
<b>Benchmark</b>	<b>5.1</b>	<b>2.5</b>	<b>9.6</b>	<b>(7.7)</b>	<b>1.7</b>	<b>2.4</b>	<b>3.5</b>	<b>5.6</b>	<b>9.5</b>	<b>11.3</b>	<b>7.8</b>	<b>9.7</b>
<b>Difference</b>	<b>2.9</b>	<b>0.3</b>	<b>2.7</b>	<b>(3.7)</b>	<b>0.5</b>	<b>(1.0)</b>	<b>(0.2)</b>	<b>0.2</b>	<b>2.1</b>	<b>0.8</b>	<b>(0.9)</b>	<b>0.0</b>
<b>PIRC</b>	<b>5.8</b>	<b>1.8</b>	<b>11.3</b>						<b>5.7</b>		<b>5.5</b>	<b>9.3</b>

3.4 Appendix 1 illustrates changes in the market value, the liability value, the Fund's deficit and the funding level from 31 March 2013 to 31 December 2020. Members are asked to note the changes in value and the movements in the Fund's funding level. Chart 1 below shows the Fund's value since 31 March 2010.

**Chart 1: Fund Value in Millions (31 March 2010 to 31 December 2020)**



3.5 The fund manager's performance has been scored using a quantitative analysis compared to the benchmark returns, defined below.

●	<b>RED-</b> Fund underperformed by more than 3% against the benchmark
△	<b>AMBER-</b> Fund underperformed by less than 3% against the benchmark
○	<b>GREEN-</b> Fund is achieving the benchmark return or better

3.6 Table 2 highlights the Q4 2020 returns. Baillie Gifford returned 11.1% which was 2.5% above the benchmark. Kempen performed well this quarter returning 15.3% which was 7.5% above the benchmark of 7.8%. Hermes on the other hand provided a return of -1.5% which was 2.9% below the benchmark. All managers provided a positive return this quarter except for Hermes Infrastructure.

**Table 2 – Fund Manager Q4 2020 Performance**

Fund Manager	Actual	Benchmark	Variance	Ranking
	Returns (%)	Returns (%)	(%)	
Aberdeen Standard	8.3	1.0	7.3	○
Baillie Gifford	11.1	8.6	2.5	○
BlackRock	2.5	2.1	0.4	○
Hermes GPE	(1.5)	1.4	(2.9)	△
Kempen	15.3	7.8	7.5	○
Prudential / M&G	0.0	0.0	0.0	○
Newton	5.6	1.0	4.6	○
Pyrford	3.1	1.6	1.5	○
Schroders	2.7	2.1	0.6	○
Mellon Corporation	2.2	1.0	1.2	○
UBS Bonds	0.6	0.6	0.0	○
UBS Equities	11.2	11.2	0.0	○

3.7 Kempen has provided a return of 1.1% over one year which was 14.0% below the benchmark. Schroders and Blackrock, the funds property managers also returned -2.9% and -2.6% respectively. On the other hand, Baillie Gifford performed well returning 33.5% which was 17.5% above the benchmark. UBS Equities also performed well returning 16.2%.

**Table 3 – Fund Manager Performance Over One Year**

Fund Manager	Actual	Benchmark	Variance	Ranking
	Returns (%)	Returns (%)	(%)	
Aberdeen Standard	13.5	4.5	9.0	○
Baillie Gifford	33.5	16.0	17.5	○
BlackRock	(2.6)	(1.0)	(1.6)	△
Hermes GPE	3.3	5.8	(2.5)	△
Kempen	1.1	15.1	(14.0)	●
Prudential / M&G	1.7	1.2	0.5	○
Newton	7.8	4.2	3.6	○
Pyrford	2.9	6.1	(3.2)	●
Schroders	(2.9)	(1.0)	(1.9)	△
Mellon Corporation (	6.0	4.5	1.5	○
UBS Bonds	8.2	8.2	0.0	○
UBS Equities	16.2	16.2	0.0	○

3.8 Over two years, (table 4), most mandates are positive. Returns ranged from -1.3% for Schrodgers to 29.6% for Baillie Gifford. Absolute return and credit continue to struggle, underperforming their benchmarks but providing positive actual returns overall. Kempen also underperformed the benchmark by 11.0% with a return of 7.1%

**Table 4 – Fund manager performance over two years**

Fund Manager	Actual	Benchmark	Variance	Ranking
	Returns (%)	Returns (%)	(%)	
Aberdeen Standard	9.0	4.7	4.3	O
Baillie Gifford	29.6	18.4	11.2	O
BlackRock	(0.3)	0.3	(0.6)	Δ
Hermes GPE	1.9	5.8	(3.9)	
Kempen	7.1	18.1	(11.0)	
Prudential / M&G	2.2	2.9	(0.7)	Δ
Newton	9.8	4.4	5.4	O
Pyrford	4.1	6.6	(2.5)	Δ
Schrodgers	(1.3)	0.3	(1.6)	Δ
Mellon Corporation	4.4	4.7	(0.3)	Δ
UBS Bonds	7.6	7.6	0.0	O
UBS Equities	19.8	19.8	0.0	O

#### 4. Asset Allocations and Benchmark

4.1 Table 5 below outlines the Fund's current actual asset allocation, asset value and benchmarks

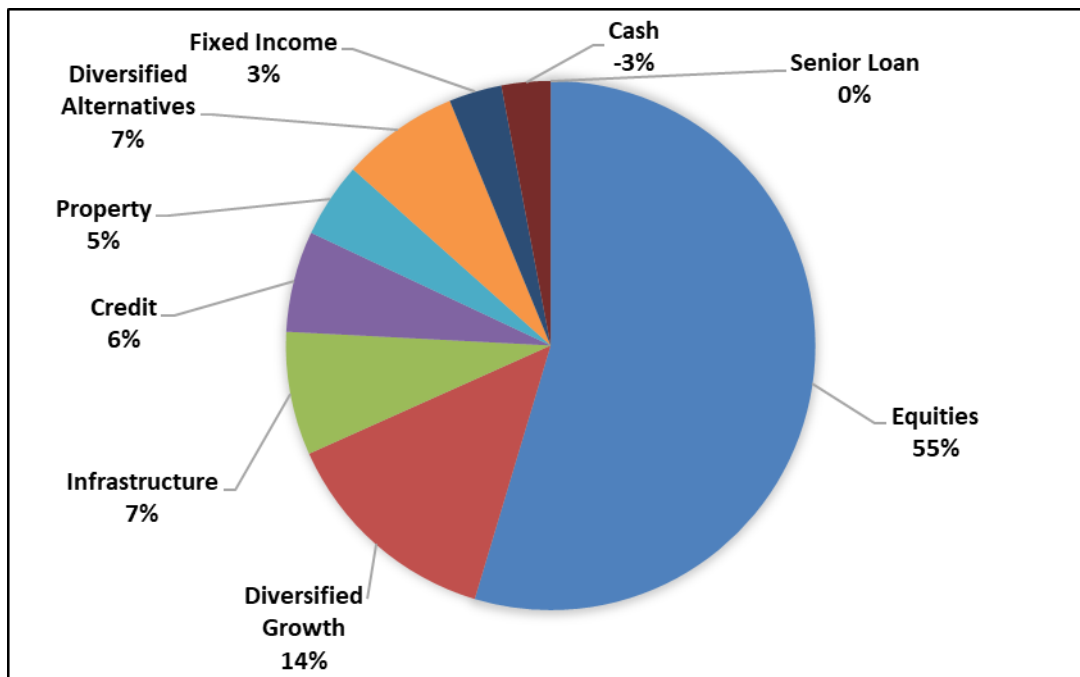
**Table 5: Fund Asset Allocation and Benchmarks as at 31 December 2020**

Fund Manager	Asset (%)	Market Values (£000)	Benchmark
Aberdeen Standard	7.6	93,020,921	3 Mth LIBOR + 4% per annum
Baillie Gifford	25.1	305,736,236	MSCI AC World Index
BlackRock	3.0	37,028,313	AREF/ IPD All Balanced
Hermes GPE	8.0	97,544,298	Target yield 5.9% per annum
Kempen	13.9	169,118,364	MSCI World NDR Index
Prudential / M&G	0.0	-	3 Mth LIBOR + 4% per annum
Newton	6.6	79,867,427	One-month LIBOR +4% per annum
Pyrford	8.9	108,659,108	UK RPI +5% per annum
Schrodgers	1.8	22,426,529	AREF/ IPD All Balanced
Mellon Corporation	5.6	68,105,985	3 Mth LIBOR + 4% per annum
UBS Bonds	3.4	41,788,685	FTSE UK Gilts All Stocks
UBS Equities	19.1	232,144,927	FTSE AW Devel. Tracker (part hedged)
LCIV	0.0	150,000	None
Cash	-3.2	(38,667,630)	One-month LIBOR
<b>Total Fund</b>	<b>100.00</b>	<b>1,216,923,163</b>	



4.2 The percentage split by asset class is graphically shown in the pie chart below.

**Chart 2: Fund Allocation by Asset Class as at 31 December 2020**



4.3 Overall the strategy is overweight equities, with equities at the top end of the range. Cash is underweight due to the pre-payment from the council. The current position compared to the strategic allocation is provided in table 6 below:

**Table 6: Strategic Asset Allocation**

Asset Class	Current Position	Strategic Allocation Target	Variance	Range
Equities	58.1%	52%	6.1%	50-60
Diversified Growth	14.5%	16%	-1.5%	14-18
Infrastructure	8.0%	8%	0.0%	7-11
Credit	6.6%	8%	-1.4%	6-10
Property	4.9%	5%	-0.1%	4-7
Diversified Alternatives	7.6%	9%	-1.4%	7-10
Fixed Income	3.4%	4%	-0.6%	3-5
Cash	-3.2%	0%	-3.2%	0-1

## 5. Fund Manager Performance

### 5.1 Kempen

Kempen	2020				2019				One Year	Two Years	Since 6/2/13
	Q4	Q3	Q2	Q1	Q4	Q3	Q2	Q1			
£169.12m	%	%	%	%	%	%	%	%	%	%	%
Return	15.3	(3.2)	16.9	(27.9)	1.2	1.3	5.2	5.5	1.1	7.1	7.4
Benchmark	7.8	3.2	19.8	(15.7)	1.0	3.8	6.5	9.9	15.1	18.1	12.8
Difference	7.5	(6.4)	(2.9)	(12.2)	0.2	(2.5)	(1.3)	(4.4)	(14.0)	(11.0)	(5.4)

#### Reason for appointment

Kempen were appointed as one of the Fund's global equity managers, specialising in investing in less risky, high dividend paying companies which will provide the Fund with significant income. Kempen holds approximately 100 stocks of roughly equal weighting, with the portfolio rebalanced on a quarterly basis. During market rallies Kempen are likely to lag the benchmark.

#### Performance Review

The strategy outperformed its benchmark by 7.5% for the quarter but has underperformed its one-year benchmark by 14.0%. Kempen provided an annual return of 7.1% over two years which was 11.0% below the benchmark. It has also underperformed its benchmark since inception by 5.4%, although the return over this period is an annualised return of 7.4%.

#### Portfolio Rebalancing

**Kempen sold four names during Q4:** SKF, Valeo, Archer Daniels Midland and Exxon Mobil.

The first three names were sold after the valuation of the shares became less attractive after the recent strong share price performances. In addition, the expected dividend yield of these shares was below the threshold. US oil major Exxon was sold as it continued to lag its oil major peers with regard to setting clear carbon reduction targets.

**No new stocks were added to the portfolio**

## 5.2 Baillie Gifford

Baillie Gifford	2020				2019				One Year	Two Years	Since 6/2/13
	Q4	Q3	Q2	Q1	Q4	Q3	Q2	Q1			
305.74m	%	%	%	%	%	%	%	%	%	%	%
Return	11.1	7.6	27.9	(13.2)	4.9	0.7	7.7	12.4	33.5	29.6	17.3
Benchmark	8.6	3.5	19.8	(15.9)	1.5	3.4	6.2	9.8	16.0	18.4	12.7
Difference	2.5	4.1	8.1	2.7	3.4	(2.7)	1.5	2.6	17.5	11.2	4.6

### Reason for appointment

Baillie Gifford (BG) is a bottom-up, active investor, seeking to invest in companies that will enjoy sustainable competitive advantages in their industries and will grow earnings faster than the market average. BG's investment process aims to produce above average long-term performance by picking the best growth global stocks available by combining the specialised knowledge of BG's investment teams with the experience of their most senior investors. BG holds approximately 90-105 stocks.

### Performance Review

For Q4 BG returned 11.1%, outperforming its benchmark by 2.5%. BG's one-year return was 33.5%, outperforming its benchmark by 16.0%. Since initial funding, the strategy has returned 17.3% p.a., outperforming its benchmark by 4.6%.

From a sector perspective, consumer discretionary added the most contribution to return to the portfolio, followed by industrials, communication services and healthcare. In consumer discretionary, Tesla added 99bps of relative performance to the portfolio with luxury retail businesses Farfetch adding 75bps. In industrials, Ryanair was the top contributor as the market expects air travel to return to some form of normality from the news of COVID-19 vaccines being approved. Energy and financials were the worst contributors to performance. Energy stocks performed well in the period however the Sub-fund is underweight and poor stock selection in financials was the culprit for underperformance.

Looking through the portfolio in terms of region, the United States was where the portfolio added the most contribution to returns. Strong stock selection in the country was a benefit for the portfolio. UK was also a strong contributor as Farfetch was one of the best performing stocks. China and Germany contracted and was most largely driven by weak stock selection. Namely, Alibaba had performed poorly as the ecommerce's sister company Ant-Group failed to IPO due to regulatory fails in China.

Whilst it is not a benchmark for the sub-fund, the manager has also been monitoring the performance vs the MSCI growth index as a comparator index and observed that they have been closely tracking since inception. However, in Q4 2020, the sub-fund was able to outperform this growth index by 4.65%. Since inception, the sub fund has beaten this comparator index by 1.6% per annum.

### 5.3 UBS Equities

UBS Equities	2020				2019				One Year	Two Years	Since 31/08/12
	Q4	Q3	Q2	Q1	Q4	Q3	Q2	Q1			
£232.14m	%	%	%	%	%	%	%	%	%	%	%
Return	11.2	5.6	18.8	(19.3)	5.7	2.1	4.0	11.5	16.2	19.8	14.0
Benchmark	11.2	5.6	18.8	(19.3)	5.7	2.1	4.1	11.5	16.2	19.8	14.1
Difference	0.0	0.0	0.0	0.0	0.0	0.0	(0.1)	0.0	0.0	0.0	(0.1)

#### Reason for appointment

UBS are the Fund's passive equity manager, helping reduce risk from underperforming equity managers and providing a cost-effective way of accessing the full range of developed market equity growth.

#### Performance

The fund returned 11.2% for Q4 and 16.2% over one year. Since funding in August 2012, the strategy has provided an annualised return of 14.0%.

#### Equities

Global equities gained in the fourth quarter, as vaccine breakthrough provided greater reassurance on a return to economic normality. On the back of this, the FTSE Developed index returned 8.2% in GBP terms, closing an unprecedented year on a positive note.

In November, the breakthrough in the hunt for an effective COVID-19 vaccine rekindled interest in more procyclical investments. This triggered a sudden and extreme style rotation from Growth and Momentum to Value; the scale of the rotation even eclipsed the 2008 financial crisis or the dotcom bubble. Cyclical stocks benefited the most from this reversal and small caps outperformed large caps.

US equities rose in the fourth quarter and performance from economically sensitive sectors such as Energy, Financials, and Industrials, outstripped returns of more defensive sectors. There was a broadening of the market away from the very narrow range of mega-cap names that had dominated returns all year.

European equities posted strong gains in the fourth quarter, benefiting from the style rotation witnessed on the market in the last months. Sectors that lost the most from the COVID-19 pandemic, such as Energy and Financials, saw the strongest bounce-back. Towards the end of December, the news of further lockdown in European markets due to the new COVID strain tempered market enthusiasm. The UK equity market which had been the weakest international equity market also recovered robustly, helped by the agreement at the end of the month of the EU-UK trade deal.

Emerging market equities returned their strongest quarterly return in over a decade with the weak US dollar partially contributing to the gains. Furthermore, a rally in commodity prices also helped Emerging Market exporters.

## 5.4 UBS Bonds

UBS Bonds	2020				2019				One Year	Two Years	Since 5/7/2013
	Q4	Q3	Q2	Q1	Q4	Q3	Q2	Q1			
£41.79m	%	%	%	%	%	%	%	%	%	%	%
Return	0.6	(1.2)	2.5	6.3	(3.9)	6.2	1.4	3.4	8.2	7.6	5.4
Benchmark	0.6	(1.2)	2.5	6.3	(3.9)	6.2	1.3	3.4	8.2	7.6	5.4
Difference	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.1

### Reason for appointment

UBS were appointed as the Fund's passive bond manager to allow the Fund to hold a small allocation (4%) of UK fixed income government bonds.

### Performance

Returned 0.6% for Q4, with a one-year return of 8.2% and a two-year return of 7.6%.

Within fixed income, spreads in non-government products outperformed government bonds as investor risk sentiment remained generally positive over the course of the quarter. US government bond yields rose driven by prospects of increased fiscal spending under a Biden administration and renewed hopes of a global economic rebound following the development of vaccines against COVID-19.

Yields on German bunds declined slightly over Q4 as investors weighted the negative impact of COVID related lockdowns on economic activity in the Euro area against improving economic data among some of the region's largest economies.

In spread product, high yield bonds outperformed investment grade although both ends of the credit quality spectrum generated positive returns. Local currency emerging market bonds were among the best performers for the quarter buoyed by EM FX strengthening against USD. Against this backdrop, higher yielding portions of the fixed income market saw continued demand in particular the Asia.

## 5.5 M&G / Prudential UK

M&G / Prudential	2020				2019				One Year	Two Years	Since 31/5/2010
	Q4	Q3	Q2	Q1	Q4	Q3	Q2	Q1			
£0.00m	%	%	%	%	%	%	%	%	%	%	%
Return	0.0	0.0	0.0	1.7	0.0	1.7	0.0	1.0	1.7	2.2	4.5
Benchmark	0.0	0.0	0.0	1.2	1.2	1.2	1.0	1.2	1.2	2.9	2.9
Difference	0.0	0.0	0.0	0.5	(1.2)	0.5	(1.0)	(0.2)	0.5	(0.7)	1.6

### Reason for appointment

This investment seeks to maximise returns using a prudent investment management approach with a target return of Libor +4% (net of fees). The strategy provided a return of 4.5% per year, The strategies holding has reduced in size to nil, with all of the loans repaid. This investment completed the sale of its last senior loan and is now closed.

## 5.6 Schroders Indirect Real Estate (SIRE)

Schroders	2020				2019				One Year	Two Years	Since 6/8/2010
	Q4	Q3	Q2	Q1	Q4	Q3	Q2	Q1			
£22.43m	%	%	%	%	%	%	%	%	%	%	%
Return	2.7	0.3	(2.0)	(3.9)	1.0	0.3	0.1	(1.1)	(2.9)	(1.3)	5.3
Benchmark	2.1	0.2	(2.0)	(1.3)	0.3	0.4	0.6	0.3	(1.0)	0.3	6.6
Difference	0.6	0.1	0.0	(2.6)	0.7	(0.1)	(0.5)	(1.4)	(1.9)	(1.6)	(1.3)

Reason for appointment: Schroders is a Fund of Fund manager appointed to manage a part of the Fund's property holdings. The mandate provides the Fund with exposure to 210 underlying funds, with a total exposure to 1,500 highly diversified UK commercial properties.

### Q4 2020 Performance and Investment Update

The fund generated a return in Q4 of 2.7% with a one-year return of negative 2.9% and a two-year return of negative 1.3%.

SIRE's portfolio structure maintains an overweight position to industria, alternative sectors and cash and is underweight office and retail sectors. One purchase was made in Q4 2020. The final commitment of £2.8 million was drawn by Income Plus Real Estate Debt Fund LP. Sales totalling £26.5 million were made across several funds to meet investor redemptions.

The performance of commercial real estate improved in Q4 2020 with SIRE recording its first positive quarterly return of the year. Listed real estate securities saw a strong bounce back over the quarter.

## 5.7 BlackRock

BlackRock	2020				2019				One Year	Two Years	Since 1/1/2013
	Q4	Q3	Q2	Q1	Q4	Q3	Q2	Q1			
£37.03m	%	%	%	%	%	%	%	%	%	%	%
Return	2.5	0.5	(2.9)	(2.8)	0.6	0.7	0.5	0.1	(2.6)	(0.3)	0.5
Benchmark	2.1	0.2	(2.0)	(1.3)	0.3	0.4	0.6	0.3	(1.0)	0.3	3.7
Difference	0.4	0.3	(0.9)	(1.5)	0.3	0.3	(0.1)	(0.2)	(1.6)	(0.6)	(3.2)

Reason for appointment: In December 2012, a sizable portion of the Fund's holdings with Rreef were transferred to BlackRock (BR). The transfer to BR provides the Fund with access to a greater, more diversified range of property holdings within the UK.

### Q4 2020 Performance and Investment Update

BR returned 2.5% for the quarter against the benchmark of 2.1%. It returned -2.6% over one year against its benchmark's return of -1.0%. During the final quarter of the year the Fund completed three disposals totaling £53.7 million. No acquisitions took place in Q4 2020.

Pressure on UK retailers continued, however October retail sales volumes rose by 1.2% and extended the continuous period of growth to six months. Offices in Central London saw vacancy rates increase at pace in Q3-Q4 2020.

## 5.8 Hermes

Hermes	2020				2019				One Year	Two Years	Since 9/11/2012
	Q4	Q3	Q2	Q1	Q4	Q3	Q2	Q1			
£97.54m	%	%	%	%	%	%	%	%	%	%	%
Return	(1.5)	0.0	0.9	3.9	(0.2)	1.2	1.0	(1.5)	3.3	1.9	7.9
Benchmark	1.4	1.4	1.4	1.5	1.4	1.5	1.5	1.4	5.8	5.8	5.9
Difference	(2.9)	(1.4)	(0.5)	2.4	(1.6)	(0.3)	(0.5)	(2.9)	(2.5)	(3.9)	2.0

### Reason for appointment

Hermes were appointed as the Fund's infrastructure manager to diversify the Fund away from index linked fixed income. The investment is in the Hermes Infrastructure Fund I (HIF I) and has a five-year investment period which ended on 30<sup>th</sup> April 2020 and a base term of 18 years. In March 2015 Members agreed to increase the Fund's allocation to Hermes to 10%.

### Performance

Hermes returned -1.5% in Q4 underperforming the benchmark by 2.9%. As at 31 December 2020, the strategy reported a one-year positive return of 3.3%, underperforming its benchmark by 2.5%. Since inception the strategy has provided a good, annualised return of 7.9%, outperforming its benchmark by 2.0%.

### Portfolio review

In the Value-Added portfolio, Eurostar continues to be the most affected asset. Current international travel restrictions have led to a precipitous reduction in passenger numbers since December, with Eurostar currently operating a single service per day from London to each of Brussels/Amsterdam and Paris. Whilst welcoming positive news regarding vaccination rollouts across Eurostar's network countries, Eurostar management remain extremely cautious on the recovery and currently anticipates passenger numbers increasing from September 2021, at the earliest. Cash flow management and cost reductions remain a key area of focus, however as a result of continued delays to a recovery, Eurostar is expecting to require between £250m and £300m of additional funding to cover a cash shortfall during 2021 and 2022. A range of options are being explored, and it is possible that further shareholder equity support will be required.

Following local travel restrictions introduced from October 2020, Scandlines experienced a sharp decrease in car volumes, which were c.75% below budget by December 2020, and have continued at the same level throughout January. Cargo volumes have remained resilient and boosted by Christmas trade, performance reached budgeted levels by the end of December 2020 and throughout January.

In the Core portfolio, Iridium Hermes Roads' Q4 traffic performance was negatively impacted by increased restrictions in Spain. December and January traffic were c.23% below budget on average, compared to a c.75% reduction in traffic during the first lockdown. A claims process with concession grantors to obtain compensation due to the impact of Covid-19 on traffic is ongoing.

## 5.9 Aberdeen Standard Asset Management

Aberdeen Standard	2020				2019				One Year	Two Years	Since 15/9/2014
	Q4	Q3	Q2	Q1	Q4	Q3	Q2	Q1			
£93.02m	%	%	%	%	%	%	%	%	%	%	%
Return	8.3	5.1	(0.6)	0.7	(0.2)	1.9	2.3	0.6	13.5	9.0	5.3
Benchmark	1.0	1.0	1.3	1.2	1.2	1.2	1.2	1.2	4.5	4.7	4.6
Difference	7.3	4.1	(1.9)	(0.5)	(1.4)	0.7	1.1	(0.6)	9.0	4.3	0.7

### Reason for appointment

As part of the Fund's diversification from equities, Members agreed to tender for a Diversified Alternatives Mandate. Aberdeen Standard Asset Management (ASAM) were appointed to build and maintain a portfolio of Hedge Funds (HF) and Private Equity (PE). All positions held within the portfolio are hedged back to Sterling.

Since being appointed ASAM have built a portfolio of HFs and PEs, which offer a balanced return not dependent on traditional asset class returns. In the case of PE, the intention is to be able to extract an illiquidity premium over time. The allocation to PE, co-investments, infrastructure, private debt, and real assets will be opportunistic and subject to being able to access opportunities on appropriate terms. In December 2020 Members agreed to invest a further £20m with ASAM, with a £10m investment in January 2021 and a further investment due in April 2021.

### Performance

Overall, the strategy provided a return of 8.3% in Q4 2020, outperforming its benchmark by 7.3%. The largest contributors included the Cinven Cullinan and Glass Technology co-investments where the underlying businesses were either listed or sold. Advent International GPE VIII, OEP VI & PAI Europe VI also made material write ups across their portfolios.

Over one year the mandate has outperformed its benchmark, with a return of 13.5% against a benchmark of 4.5%. Since inception in September 2014, the strategy has returned 5.3%, outperforming its benchmark by 0.7%.

The hedge funds selected for the Portfolio are a blend of:

- i. Relative Value strategies, intended to profit from price dislocations across fixed income and equity markets;
- ii. Global macro strategies, which are intended to benefit significantly from global trends, whether these trends are up or down, across asset classes and geographies;
- iii. Tail risk protection, which in the case of Kohinoor Series Three Fund is intended to offer significant returns at times of stress and more muted returns in normal market environments, and
- iv. Reinsurance

ASAM have built a portfolio of hedge funds, private equity funds and co-investments, which can offer a balanced return not wholly dependent on traditional asset class returns. In the case of private equity, the intention is to be able to extract an illiquidity premium over time.



## 5.10 Pyrford

Pyrford	2020				2019				One Year	Two Years	Since 28/9/2012
	Q4	Q3	Q2	Q1	Q4	Q3	Q2	Q1			
£108.66m	%	%	%	%	%	%	%	%	%	%	%
Return	3.1	(1.6)	6.2	(4.8)	0.7	0.9	1.1	2.7	2.9	4.1	3.4
Benchmark	1.6	1.8	1.3	1.5	1.5	1.7	2.8	1.1	6.1	6.6	6.9
Difference	1.5	(3.4)	4.9	(6.3)	(0.8)	(0.8)	(1.7)	1.6	(3.2)	(2.5)	(3.5)

### Reason for appointment

Pyrford were appointed as the Fund's absolute return manager (AR) to diversify from equities. The manager's benchmark is to RPI, which means that the manager is likely to outperform the benchmark during significant market rallies. AR managers can be compared to equities, which have a similar return target. When compared to equities, absolute return will underperform when markets increase rapidly and tend to outperform equities during periods when markets fall.

### Performance

Pyrford generated a return of 3.1% in Q4 outperforming its benchmark by 1.5%. Over one year the strategy has returned 2.9%, underperforming its benchmark by 3.2%. Pyrford underperformed its benchmark by 3.5% since inception.

Within the portfolio, both equities and currency hedging programme positively contributed to the quarterly performance, while bonds detracted during the last quarter of the year. The current asset allocation of the portfolio remains the same as last quarter, with 42.09% in equities, 56.38% in bonds and 1.53% allocated to cash. The portfolio witnessed a removal of the Australian Dollar hedge, with the remaining hedged position on United States dollars, Canadian dollar and Swiss Franc.

### Outlook and Strategy

The markets continue to fight their way through the turbulence. Euphoria in November as multiple vaccines were released and approved in record time quickly gave way to concerns about new virus strains and relentless third wave of infections. The availability of a choice of vaccines so quickly is nothing short of a triumph for the scientific community. However, the manufacture, transportation, distribution and dispensing of hundreds of millions of doses appears to be a logistical challenge unrivalled in peacetime. The path of the Covid-19 pandemic in 2021 remains the biggest uncertainty.

Ultra-low yields have been artificially generated by central banks cutting base rates and actively buying government bonds to push yields down further. This has allowed Governments to borrow cheaply to finance the massive amounts of fiscal stimulus they have provided this year. Coordinated Government and central bank action has provided income support to many in the developed world whilst reducing the burden of the high levels of debt. As a result, increased household savings providing the potential for pent-up demand to be released.

## 5.11 Newton

Newton	2020				2019				One Year	Two Years	Since 31/8/2012
	Q4	Q3	Q2	Q1	Q4	Q3	Q2	Q1			
£79.87m	%	%	%	%	%	%	%	%	%	%	%
Return	5.6	3.5	8.0	(9.2)	1.6	1.7	4.3	4.2	7.8	9.8	4.4
Benchmark	1.0	1.0	1.1	1.2	1.2	1.2	1.0	1.2	4.2	4.4	4.5
Difference	4.6	2.5	6.9	(10.4)	0.4	0.5	3.3	3.0	3.6	5.4	(0.1)

### Reason for appointment

Newton was appointed to act as a diversifier from equities. The manager has a fixed benchmark of one-month LIBOR plus 4%. AR managers have a similar return compared to equity but are likely to underperform equity when markets increase rapidly and outperform equity when markets suffer a sharp fall.

### Performance

Newton generated a return of 5.6% in Q4 and outperformed its benchmark by 4.6%. Over one year the strategy has returned 7.8%, outperforming its benchmark by 3.6%. Newton's performance since inception is 4.4% and underperforms its benchmark by 0.1%.

The portfolio performance was mainly driven by positions in return seeking assets, where equities, corporate bonds, Emerging Market debt and alternatives all positively contributed to the performance during the period. The exposure to equities delivered the largest chunk of return gains as the markets advanced over the quarter following positive news around the effectiveness of the vaccine, the US election result and additional stimulus measures in the US. The detractors over the quarter were centred on the protection assets within the portfolio. Derivative instruments and exposure to gold were the main detractors to the portfolio performance this quarter, but still hold an important part of the investment manager's overall strategy.

The portfolios exposure is summarised below:

Portfolio Exposures		
	30 September 2020	31 December 2020
<b>Equities</b>	<b>41.30</b>	<b>51.13</b>
North America	16.60	19.74
Europe	12.30	13.31
UK	6.50	10.19
Emerging Markets	3.10	3.69
Pacific Basin Ex Japan	2.20	3.40
Japan	0.60	0.80
<b>Fixed Income</b>	<b>21.70</b>	<b>14.85</b>
Corporate Bonds	10.50	8.46
Emerging Debt	6.50	6.04
Government Bonds	1.30	0.35
Index Linked Government	3.40	0.00
<b>Alternatives</b>	<b>37.00</b>	<b>34.02</b>
Infrastructure Funds	12.90	12.66
Precious Metals	17.80	11.55
Cash and FX Forwards	4.70	7.18
Derivative Instruments	1.60	2.63
<b>Total</b>	<b>100.00</b>	<b>100.00</b>

## 5.12 Mellon Corporation (Standish)

Mellon Corporation	2020				2019				One Year	Two Years	Since 20/8/2013
	Q4	Q3	Q2	Q1	Q4	Q3	Q2	Q1			
£68.11m	%	%	%	%	%	%	%	%	%	%	%
Return	2.2	1.5	4.7	(2.3)	(0.0)	0.1	0.8	1.9	6.0	4.4	1.1
Benchmark	1.0	1.0	1.3	1.2	1.2	1.2	1.2	1.2	4.5	4.7	5.1
Difference	1.2	0.5	3.4	(3.5)	(1.2)	(1.1)	(0.4)	0.7	1.5	(0.3)	(4.0)

### Reason for appointment

Mellon Corporation were appointed to achieve a 6% total return from income and capital growth by investing in a globally diversified multi-sector portfolio of transferable fixed income securities including corporate bonds, agency and governments debt. The return target was later reduced to 4.4%.

### Performance

The Fund returned 2.2% against a benchmark return of 1.0%. Over one year the strategy has outperformed its benchmark of 4.5% by 1.5%, providing a return of 6.0%. Since funding in August 2013, Mellon Corporation has only provided an annual return of 1.1%. The Fund's asset allocation to corporate credit was the primary contributor to its return.

### Portfolio Composition:

Allocation to investment grade corporate credit was reduced from 37% to 24% although high yield corporate exposure was maintained at 6%. The allocation to credit was increased from historically low levels held earlier in Q1 2020 to capitalise on the significant dislocation in credit spreads resulting from the COVID 19 pandemic sell off in risk in March. Asset allocation to corporate sectors and emerging markets being the principal contributors Risk assets rallied through the final quarter on the back of reduced policy uncertainty following Biden's victory in the US presidential election and the approval and distribution of vaccines easing concerns about further COVID 19 related economic disruptions.

## 5.13 Currency Hedging

No new currency hedging positions were placed in Q4 2020.

## 6. Consultation

- 6.1 Council's Pension Fund monitoring arrangements involve continuous dialogue and consultation between finance staff, external fund managers and external advisers. The Chief Operating Officer and the Fund's Chair have been informed of the approach, data and commentary in this report.

## 7. Financial Implications

*Implications completed by: Philip Gregory, Finance Director*

- 7.1 The Council's Pension Fund is a statutory requirement to provide a defined benefit pension to scheme members. Investment decisions are taken based on a long-term investment strategy. The investment performance has a significant impact on the General Fund. Pensions and other benefits are statutorily calculated and are guaranteed. Any shortfall in the assets of the Fund compared to the potential benefits must be met by an employer's contribution.
- 7.2 This report updates the Committee on developments within the Investment Strategy and on scheme administration issues and provides an overview of the performance of the Fund during the period.

## **8. Legal Implications**

*Implications completed by: Dr. Paul Feild, Senior Governance Solicitor*

- 8.1 The Council operates the Local Government Pension Scheme which provides death and retirement benefits for all eligible employees of the Council and organisations which have admitted body status. There is a legal duty fiduciary to administer such funds soundly according to best principles balancing return on investment against risk and creating risk to call on the general fund in the event of deficits. With the returns of investments in Government Stock (Gilts) being very low they cannot be the primary investment. Therefore, to ensure an ability to meet the liability to pay beneficiaries the pension fund is actively managed to seek out the best investments. These investments are carried out by fund managers as set out in the report working with the Council's Officers and Members.
- 8.2 The Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016 are the primary regulations that set out the investment framework for the Pension Fund. These regulations are themselves amended from time to time. The Regulations are made under sections 1(1) and 3(1) to (4) of, and Schedule 3 to, the Public Service Pensions Act 2013. They set out the arrangements which apply to the management and investment of funds arising in relation to a pension fund maintained under the Local Government Pension Scheme.

## **9. Other Implications**

- 9.1 **Risk Management** - Investment decisions are taken based on a long-term investment strategy. Investments are diversified over several investment vehicles (equities – UK and overseas, bonds, property, infrastructure, global credit and cash) and Fund Managers to spread risk.

Performance is under constant review, with this focused on how the Fund has performed over the past three months, one year and three years.

### **Background Papers Used in the Preparation of the Report:**

- Northern Trust Quarterly Q4 2020 Report; and
- Fund Manager Q4 2020 Reports.

### **List of appendices:**

**Appendix 1** - Fund Asset and Liability Values 31 March 2013 to 31 December 2020

**Appendix 2** - Definitions

**Appendix 3** - Roles and Responsibilities