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Collective Investing

Technical Update – Investment Strategies for LGPS 2014

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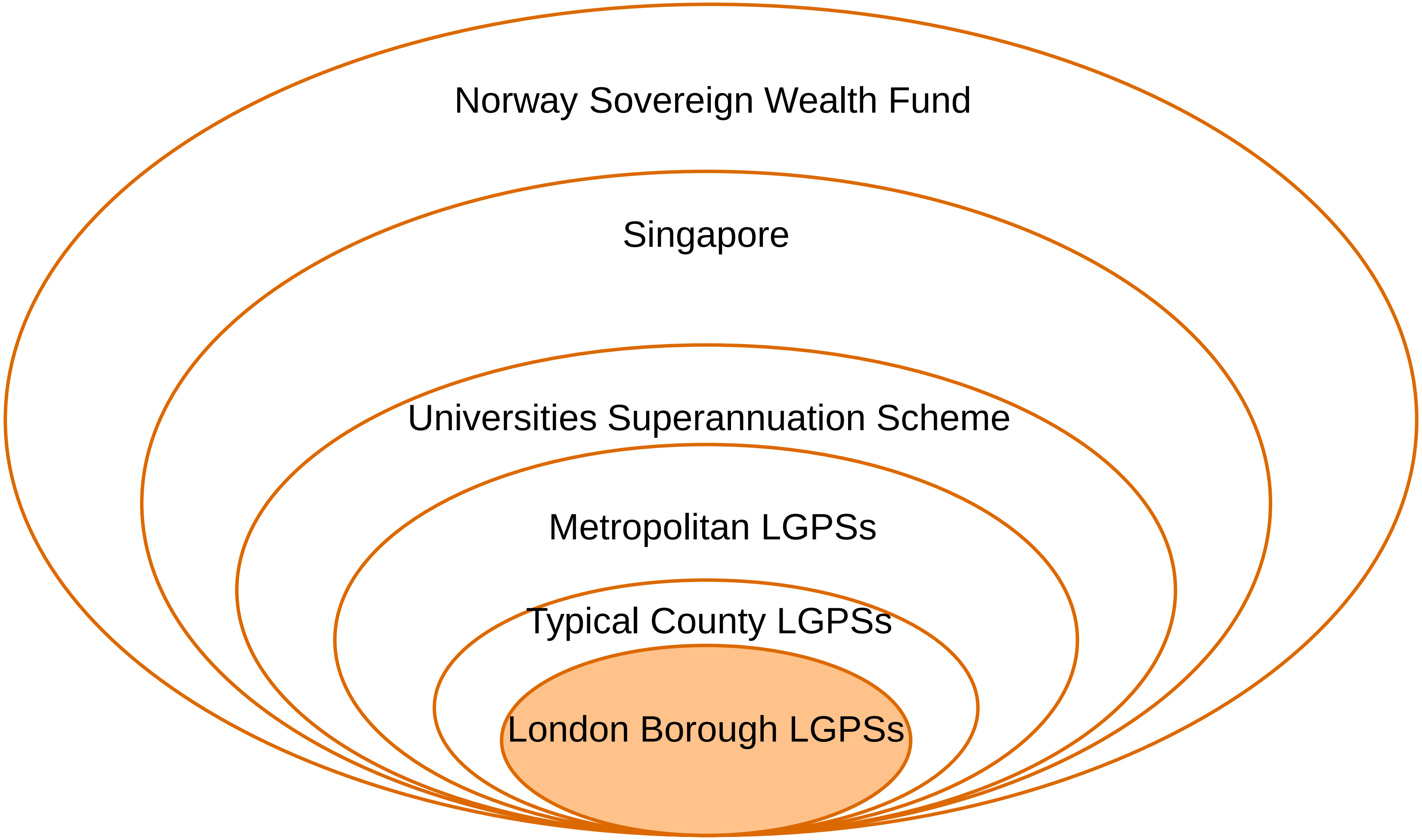
Agenda

How can collective investing benefit the LGPS?

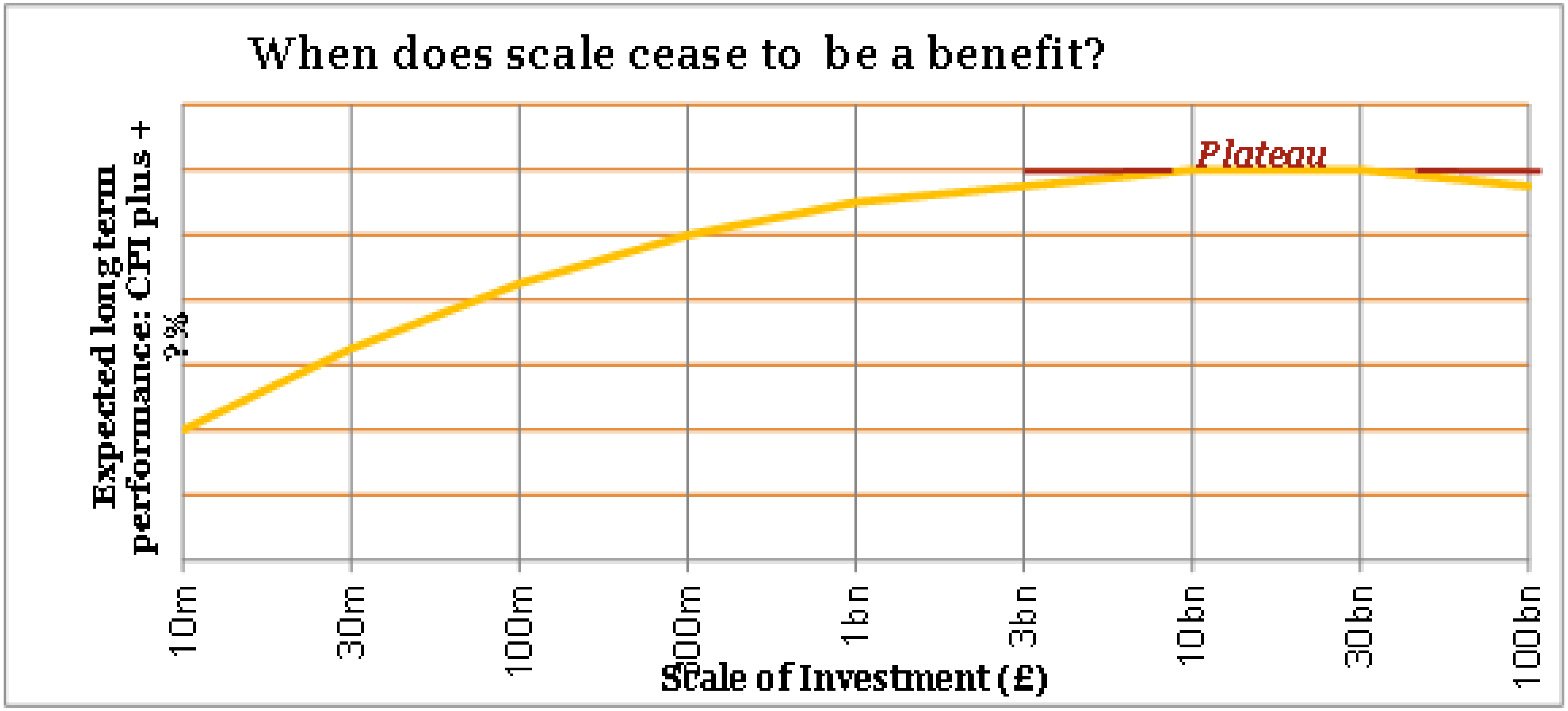
What are the challenges and practicalities?

And the reality is?

Size and collective investment

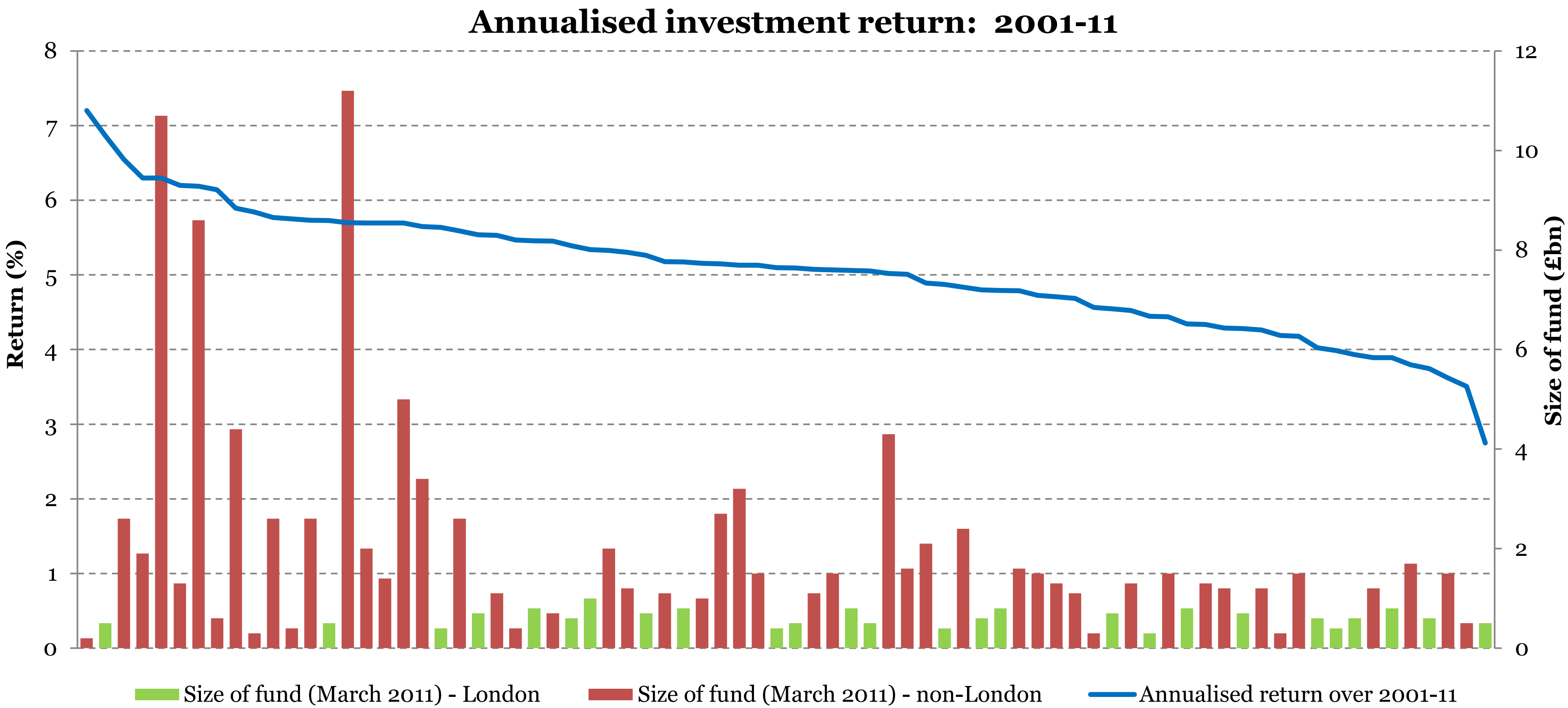


Are we at the top yet?



- Scale itself can reduce costs and deliver performance – but to what point?
- Quality of governance as important?
- Actionable market insight as important?

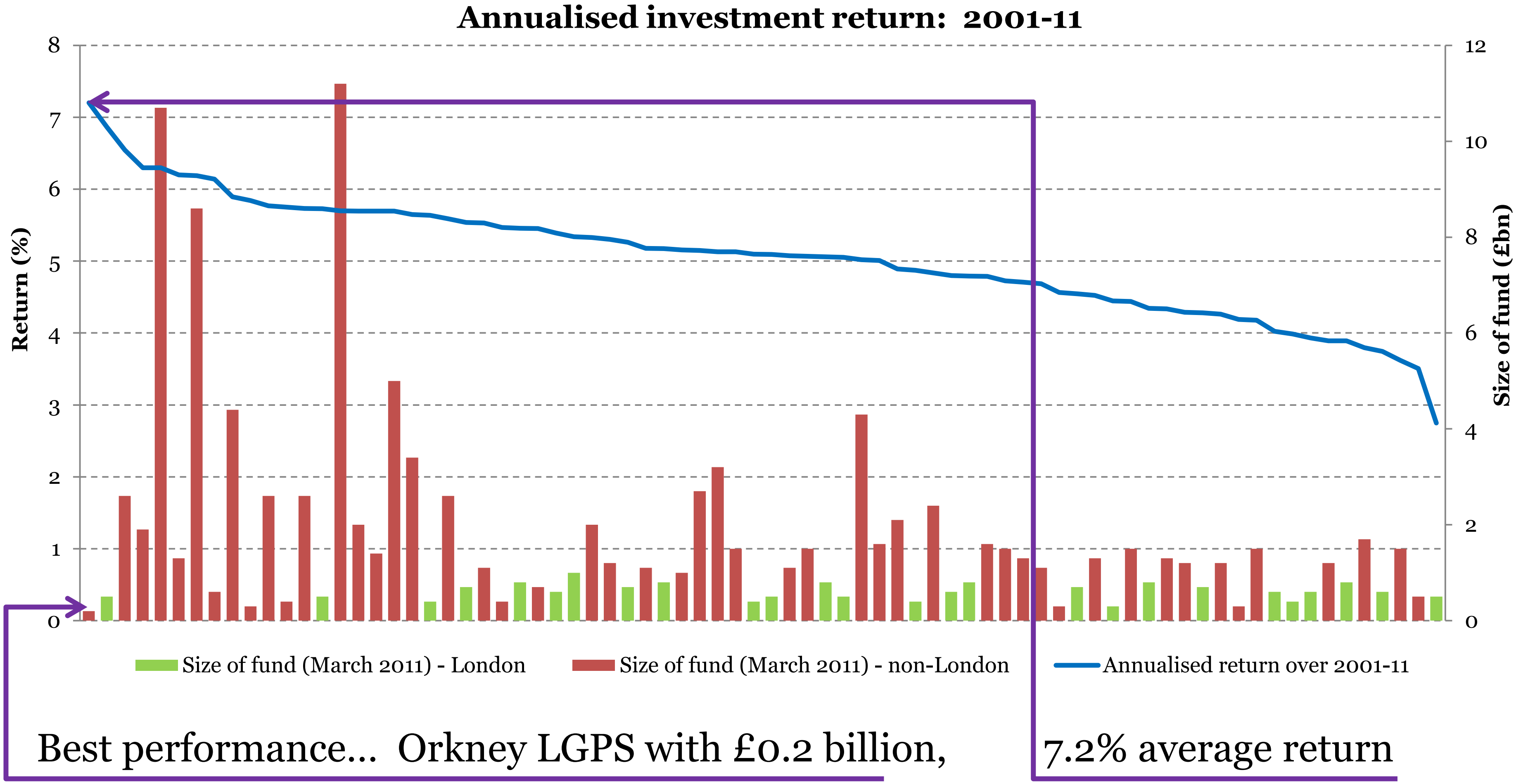
Q: Where's the evidence? A: from LGPS funds



Best performers on the left. Blue line shows how well they performed.

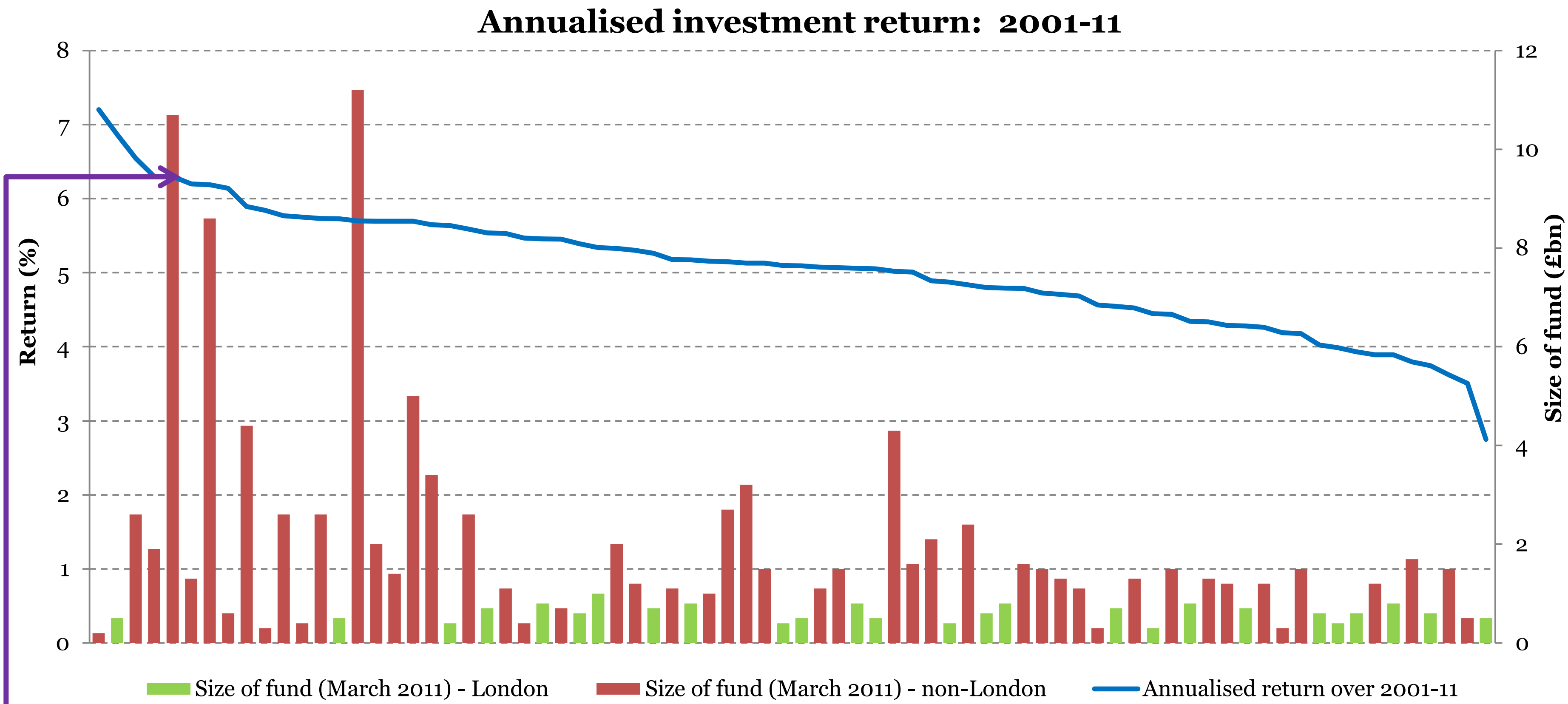
Height of bar = size of fund. See scale on right

Q: Where's the evidence? A: from LGPS funds



Best performance... Orkney LGPS with £0.2 billion, 7.2% average return

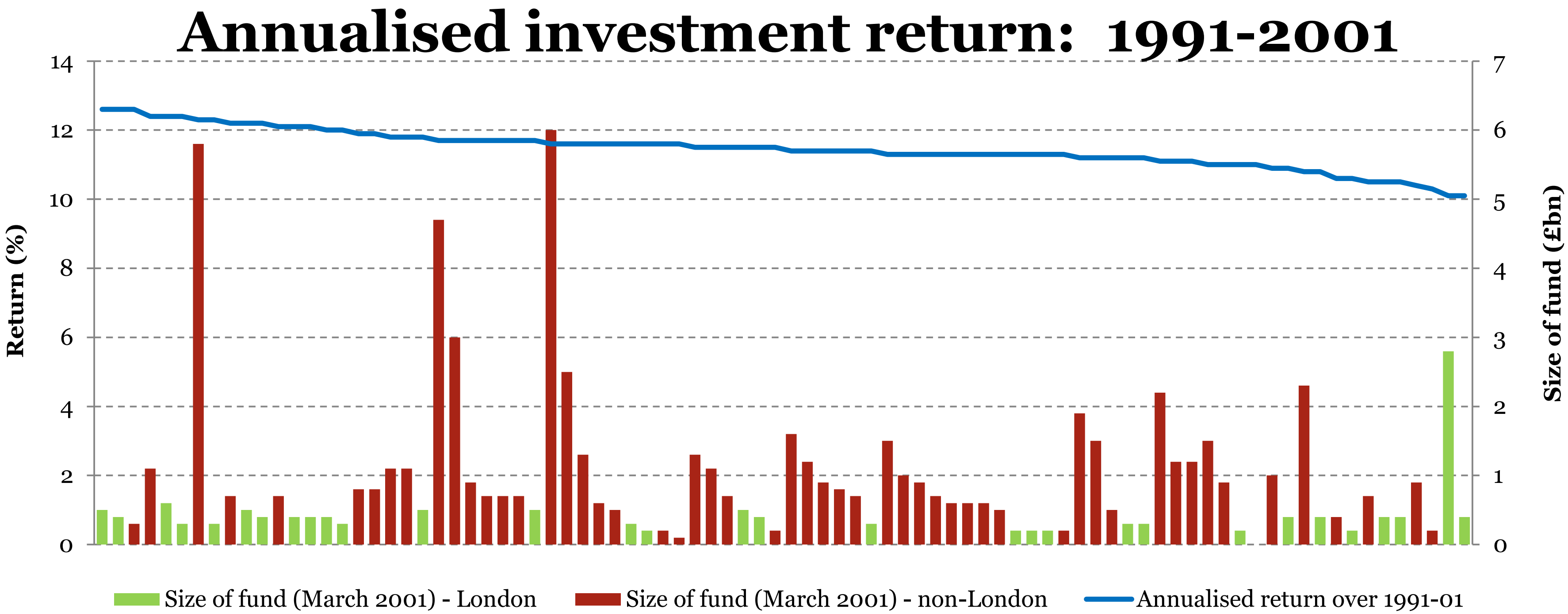
Q: Where's the evidence? A: from LGPS funds



Or? … Greater Manchester LGPS with £10.7 billion, 6.3% average return. The 7 largest funds averaged 5.73%.

The 26 London Funds measured by CIPFA averaged 4.87%pa.

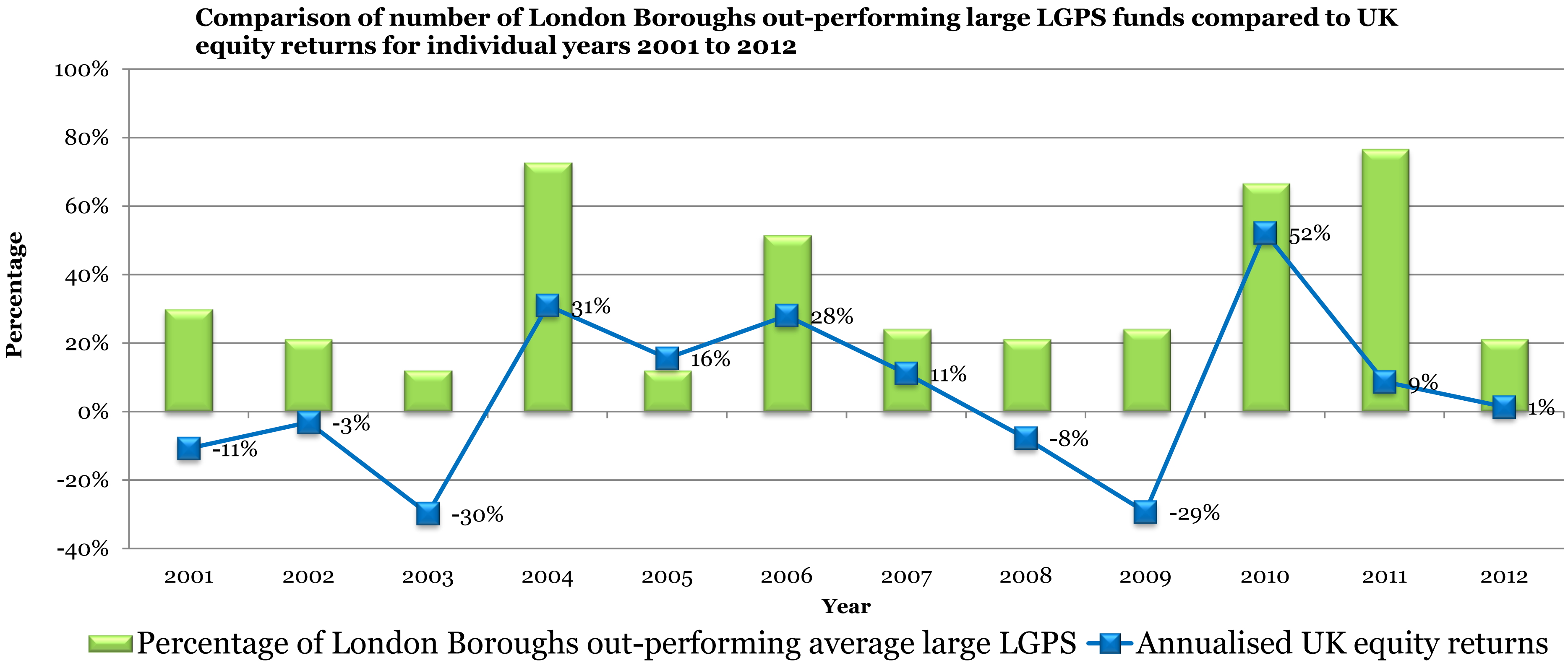
Why it matters now – times have changed



A rising tide once floated all boats.

In the 90s, most LGPS Funds achieved 11% pa plus, and there was less variability.

More recently, some smaller funds performed well



Equities are the largest holding in almost all LGPS Funds.

2003 and 2009: negative equity markets returns. Few London funds outperformed the largest LGPSs. In "bounce back" years, 2004 and 2010, many London funds outperformed.

But, both times, the bounces didn't fully recoup relative performance against the large funds.

How can collective investing benefit the LGPS?

- Lower investment costs
- Higher investment returns
- Smarter allocations of assets
- Consistent governance
- Local investment
- Infrastructure investment
- Greater transparency
- A competitive market for investment services
- Integral element of clearer strategy for the LGPS

What are the challenges and practicalities?

The Society of London Treasurers challenges:

- The responsibilities of each London Borough towards their pensioners in minimising risk and maximising returns for their funds delivered through the Trustee responsibilities of Members of Pension Committee in accordance with the Myners principles.
- The need for local decision making in relation to asset allocation.
- The recognised relationship between local decision making in relation to the fund and its associated returns and deficit and local taxation implications.
- The statutory responsibilities of local Authorities in relation to actuarial valuations and pension fund accounts and audit requirements.
- The political and managerial ownership of the decisions in relation to the pension fund its associated risks and need for influence over decision-making.

What are the challenges?

- Choosing the ultimate destination: investment is rightly leading the debate, but investment solutions will prefigure operational decisions
- Cutting investment costs, internal, external and hidden
- Paying for investment expertise: do fees to external managers and salaries to internal appointees amount to the same thing?
- Achieving the best results in each asset class, with mechanisms that enable effective monitoring and rapid change
- Delivering strategic approach to fees – from passive management to hedge funds
- Sharing those niche investment managers, some of which are doing a good job at a small scale

What are the challenges?

- Gaining from asset allocation decisions
- Delivering different allocations not just to different Authorities, but different employers
- Delivering macroeconomic benefits: what is the net effect, for example, of selling gilts and buying infrastructure?
- Permitting an appropriate (?) measure of local investment
- Minimising the legal changes required
- Sustainable and efficient legal structures for funds
- Implementing it !

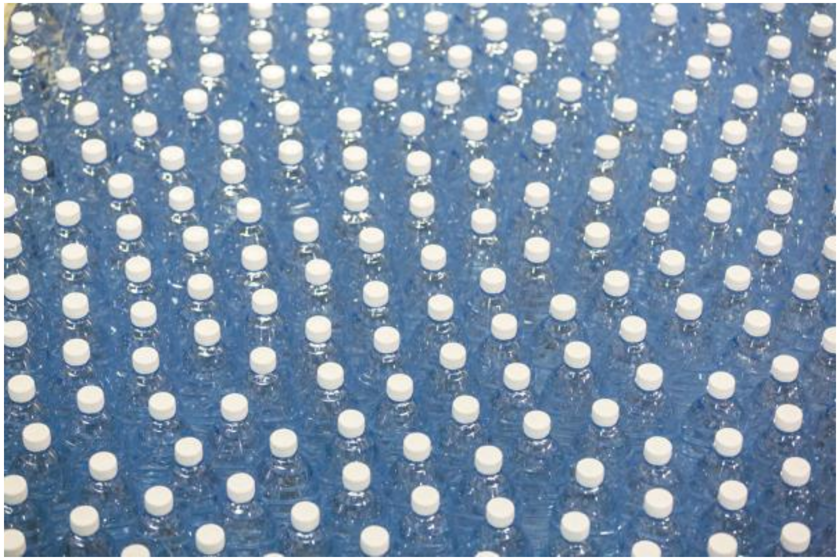
What will be the reality?

Working together, procurement solutions, CIVS or mergers?

Body of evidence under evaluation – DCLG / Shadow Board

"Government moving forward with pension fund consolidation" in England and Wales: asset managers earned £353 million from LGPS

Solutions bubbling up or a top-down architecture?



What is being researched?

Comparing the Gwynedd and the DCLG invitations to quote

- Move from outline to detailed business case, with cashable saving opportunities
- Highlight options for the CIV, with legal and organisational implications
- Establish benefits, business and financial, along with sensitivity to non-participation

- Robust analysis of costs and benefits associated with structural reform
- Only consider change to the investment structure
- Costs, explicit and implicit
- Passive and active issues
- 3 potential collaborative models: 1 CIV, 5-10 CIVs, 5-10 merged funds
- Asset allocation decisions either local (with CIVs) or at the 5-10 merged fund level

What is being researched?

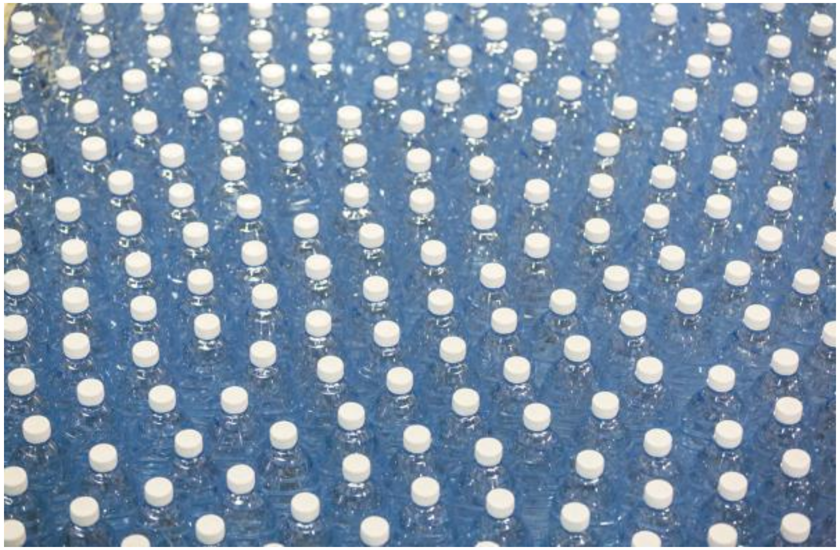
Comparing the Gwynedd and the DCLG invitations to quote

- Delivery model, with a clear structure and governance
- Impacts for individual authorities
- Opportunities to best use investment resources currently employed
- Implementation plan

- Barriers to implementation, and how to overcome them
- Implementation programme
- Impact on contribution rates
- Replication in other public sector funded schemes

All will become clear… … …

… … … but when?



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