

**CAMBRIDGESHIRE  
PENSION FUND**



**Pension Fund Board**

**18 December 2014**

**Report by: THE DEPUTY HEAD OF PENSIONS**

<b>Subject:</b>	<b>Investment Strategy Review.</b>
<b>Purpose of the Report</b>	To consider proposals to improve the Fund's investment strategy.
<b>Recommendations</b>	<p><b>That the Pension Fund Board:</b></p> <ol style="list-style-type: none"> <li>1. Approve the updated Investment strategy as recommended by the Investment Sub Committee.</li> <li>2. Delegate authority to the Investment Sub Committee to determine whether the UK Fixed Interest allocation is moved into Index Linked Gilts.</li> <li>3. Note that two days will be set aside in February 2015 for members of the Investment Sub Committee to receive presentations from fund managers, selected from the Mercer investment database in conjunction with Officers of the Fund.</li> </ol>
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**1 Background**

- 1.1 The Investment strategy of the Fund is approved by the Pensions Board with the Investment Sub Committee (ISC) being responsible for the delivery of the Strategy. This paper provides a health check of the current investment portfolio and recommends improvements.
- 1.2 The Investment Sub Committee reviewed the investment strategy of the Fund following the 2013 actuarial valuation and made a recommendation to reduce equities in order to increase the level of alternative assets
- 1.3 Following the appointment of a new investment consultant, Mercer Limited, the investment strategy has been reviewed and their recommendations and

views were presented to the Investment Sub Committee on 20 November 2014. Mercer's report to the ISC attached as an Appendix.

- 1.4 The Investment Sub Committee has considered Mercer's views and recommends an update to the Fund's asset allocation as part of its investment strategy.

## 2 Current strategy health check

- 2.1 Mercer expect the current strategy of 64% equities, 24% alternatives and 12% bonds to be supportive of the funding arrangements in place as part of the 2013 actuarial valuation. Whilst comfortable that the strategy is in line with the funding plan from a return perspective, Mercer suggest this is reviewed in more detail as part of the 2016 valuation discussions, with a specific focus on the levels of risk that are embedded within the return assumptions.

- 2.2 **Equities**- The current global equity structure (nine different managers / mandates) is complex with a mixture of regional and global equity mandates – and a degree of overlap. The Fund should be clear on its long term “beliefs” around equities and equity managers. Most notably, including views on active versus passive; the “types” of active and passive, and the complexity of the structure given governance and fees.

In consideration of these views, Mercer's recommendation is to re-focus the portfolio by ensuring managers are “best in class” and focusing on the strategic rationale for each mandate in the Fund. In short, they believe this can be achieved by focusing on better use of passive and more focused, high conviction active mandates, with a preference for global rather than regional mandates.

- 2.3 **Bonds**- Bonds in the context of the Fund can have two roles, return generation or risk reduction. The current portfolio is structured with a significant focus on returns. Mercer advocates that the Fund looks to maximise returns, to the extent they are required as part of the funding strategy; but to achieve this at the lowest level of risk.

Mercer's recommendation is for a plan to be put in place to reallocate to index linked gilts, in order to provide protection against inflation, as and when it becomes affordable to do so (i.e. bonds are more attractive and / or the funding level has improved). The UK element of the current bond portfolio should be used as a basis for this change.

- 2.4 **Alternatives / diversification** -The Fund has already achieved a reasonable degree of diversification through the existing allocations to property, infrastructure, private equity and loans.

Mercer's recommendation is to bring the existing alternative holdings together into a “real assets” portfolio and build this out over time, noting the intention to allocate an additional 9%. Consideration should be given to how to structure the portfolio (aims, roles etc) before considering individual asset classes.

- 2.5 Mercer have proposed a plan to review each of these areas in turn over the next twelve months and make proposals to the Investment Sub Committee for implementing the strategy.
- 2.6 Two days have been set aside in February 2015 for members of the Investment Sub Committee to select appropriate fund managers to deliver this strategy. This will be arranged as a joint event in partnership with members of the Northamptonshire Investment Sub Committee who are undertaking a similar exercise.

### 3 The Investment Strategy Update

- 3.1 The table below shows the current and the proposed asset allocations that will form the update to the investment strategy:

Asset Class	Current %	Proposed %	Range %
<b>Equities</b>	<b>64</b>	<b>64</b> (initially but noting the desire to reduce in favour of alternatives)	<b>59 – 69</b> (noting that there will be initial ranges around UK until the passive portfolio is restructured)
Passive	20	22	
UK	10	10	
Regional	5	-	
Global	12	25	
European	12	-	
Emerging Markets	5	7	
<b>Bonds</b>	<b>12</b>	<b>12</b>	<b>9-15</b>
Global	7	7	
UK Fixed Interest	5	-	To delegate authority to the ISC to determine whether UK Fixed Income is moved into Index Linked Gilts
UK Index Linked	-	5	
<b>Alternatives</b>	<b>24</b>	<b>24</b> (initially but noting the desire to increase)	<b>No formal range</b> (noting the costs of trading illiquid assets)
<b>Total</b>	<b>100</b>	<b>100</b>	

### 4 Recommendation

- 4.1 To approve the updated Investment strategy as recommended by the Investment Sub Committee.
- 4.2 To delegate authority to the Investment Sub Committee to determine whether the UK Fixed Interest allocation is moved into Index Linked Gilts.

- 4.3 To note that two days will be set aside in February 2015 for members of the Investment Sub Committee to receive presentations from fund managers, selected from the Mercer investment database in conjunction with Officers of the Fund.

## 5 Relevant Pension Fund Objectives

Perspective	Outcome
<b>Funding and Investment</b>	<ul style="list-style-type: none"><li>To ensure that the Fund is able to meet its liabilities for pensions and other benefits with the minimum, stable level of employer contributions.</li><li>To ensure that sufficient resources are available to meet all liabilities as they fall due.</li><li>To maximise the returns from its investments within reasonable risk parameters.</li></ul>

## 6 Finance & Resources Implications

- 6.1 There will be transitions related cost if the investment strategy is approved by the Pension Board. Officers will work on budgets once the strategy is agreed.

## 7 Risk Implications

- a) Risk(s) associated with the proposal

Risk	Mitigation	Residual Risk
That the proposals do not improve the risk and return profile of the Fund.	Professional advice has been sought with an evaluation of the proposals with the rationale for change explained.	Amber

- b) Risk(s) associated with not undertaking the proposal

Risk	Risk Rating
That the Fund is operating less efficiently in terms of risk / return profile and cost.  Operating more risk than necessary could have downside implications for funding levels.	Red

## 8 Communication Implications

- 8.1 Any changes to the investment strategy will be reflected in the publicly available Statement of Investment Principles, Business Plan and Annual Report.

## **9 Legal Implications**

- 9.1 There are no legal implications with the recommendations. Legal advice will be sought as appropriate when implementing asset allocation changes.

## **10 Consultation with Key Advisers**

- 10.1 The report was produced in consultation with Mercer Limited.

## **11 Alternative Options Considered**

- 11.1 No applicable.

## **12 Background Papers**

- 12.1 Previous papers presented to the Investment Sub Committee at its meeting on 20th of November 2014.

## **13 Appendices**

- 13.1 Appendix A – Investment strategy report presented at the 20th of November 2014 ISC.

Checklist of Key Approvals	
Is this decision included in the Business Plan?	
Will further decisions be required? If so, please outline the timetable here	
Is this report proposing an amendment to the budget and/or policy framework?	
Has this report been cleared by the Deputy Head of Pensions?	Yes, Mark Whitby -24/11/2014
Has this report been cleared by the Section 151 Officer / Chief Finance Officer?	Yes, Chris Malyon – 25/11/2014
Has the Chairman of the Pension Fund Board been consulted?	Yes – Councillor Hickford - 26/11/2014
Has this report been cleared by Legal Services?	No legal implications directly from this report. Advice will be sought at the next stage should the recommendations be approved.