

CAMBRIDGESHIRE PENSION FUND



INVESTMENT SUB COMMITTEE

Date: 12th September 2019

Report by: HEAD OF PENSIONS

Subject	Private Equity Update
Purpose of the Report	To update the Investment Sub Committee on progress with the four year programme of private equity commitments approved in June 2018.
Recommendations	That the Investment Sub Committee: <ol style="list-style-type: none"> Note the Private Equity Funds to which the Fund will subscribe in year 2 of the approved 4 year programme.
Approve	Name: Richard Perry, Pension Services Financial Manager Tel: 07717 360604 Email: RPerry@Northamptonshire.gov.uk

1. Purpose of the report

- 1.1. To update the Investment Sub Committee on progress with the four year programme of private equity commitments approved in June 2018.

2. Background –strategy for Alternative assets

- 2.1. The Fund's allocation to Alternative assets of 20%, compared to 13% previously, was confirmed in the revised Strategic Asset Allocation approved by the Pension Fund Committee on 28th March 2019. The allocation was notionally split by class of Alternative asset as shown in the table below.

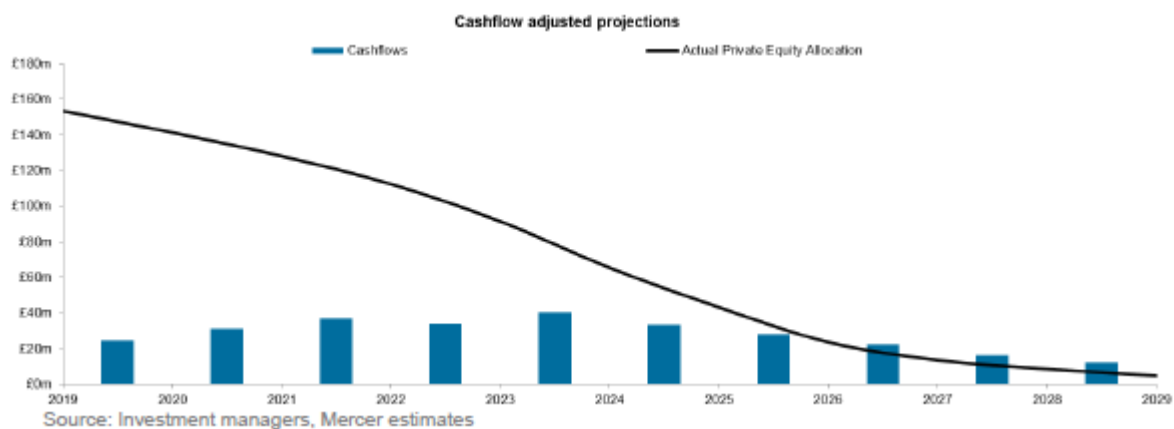
	% of the Fund
Loans	2
Private Equity	7
Local investing	5
Infrastructure	6
Total Alternatives	20

- 2.2. The notional allocation to Private Equity of 7% is an increase on the previous strategic allocation of 5% and compares to actual investments at 31 March 2019 of 4.6% (£145.7m), which comprised investments with Adams Street Partners (ASP) and Harbourvest Partners (HV) with a range of different maturities.
- 2.3. The full valuation and undrawn commitments to Alternatives at 31st March 2019 are shown below (commitments include new Funds added since 1 April 2019):-

Fund	Valuation at 31 st Mar 2019	Undrawn commitment at 31 st Mar 2019	Total at 31 st Mar 2019	Total at 31 st Mar 2019	Notional strategic allocation
	(GBPm)	(GBPm)	(GBPm)	(% of fund)	(% of fund)
Adams Street	84.5	50.1	134.6		
Harbourvest	61.2	56.6	117.8		
Total Private Equity	145.7	109.7	252.4	7.9	7.0
Loans – M & G	60.4	-	60.4	1.9	2.0
C & C Bank	81.1	-	81.1		
Cambridge Building Society	15.0	-	15.0		
East of England Economic Development Fund (Foresight)	-	50.0 *	50.0		
Total Local Investing	96.1	50.0	146.1	4.6	5.0
Infrastructure equity - Equitix	35.0	0.3	35.3		
Infrastructure equity - Partners Group	38.6	26.3	64.9		
Infrastructure equity - UBS	16.8	1.1	17.9		
Infrastructure equity - IFM	-	60.0	60.0		
Infrastructure equity - JP Morgan		61.4	61.4		
Infrastructure Debt - Allianz	12.9	15.5	28.4		
Infrastructure Debt - AMP	19.9	38.5 *	58.4		
Total Infrastructure	123.2	203.1	326.3	10.3	6.0
Total Alternatives	425.4 (13.3% of total Fund)	359.8	785.2	24.5%	20.0%

* - includes new commitment made in June/July 2019.

- 2.4. The total invested for Alternatives at 31 March 2019 of 13.3% is below the target allocation of 20% which reflects recent increase in strategic allocation and the time delay in identifying new managers and for the manager to deploy cash.
- 2.5. When undrawn commitments are considered, the allocations appear to be above the target holding for Alternatives. This measure taken in isolation does not give the full picture, however, as the Fund's private equity portfolio is relatively mature, at the stage where many of the early year investments are returning cash at a faster rate than new investments are making calls for cash. An 'over commitment' is necessary to reach and maintain the target allocation when older investments within the asset class are maturing and returning funds, and the total value of the Fund is expected to increase.
- 2.6. To demonstrate the maturity of the Fund's allocation to private equity and how quickly the invested value is eroded, Mercer have modelled the profile of the Fund's private equity investments assuming that no new commitments are made.



- 2.7. This paper introduces a more in depth review by Mercer of the Fund's private equity programme looking at how existing investments are diversified by geography, stage of investment vehicle and type. This leads on to an analysis of the options available for new commitments from the four managers currently used by ACCESS funds (Adams Street, Harbourvest, Pantheon and Partners Group) and the suitability of these for new investment by the Fund.
- 2.8. It is noted that the ACCESS pool is developing proposals for managing Alternative assets in a pool environment, but plans are at an early stage and it is unlikely that any new investment options will be available until 2020/21 at the earliest.

3. Background - Private equity programme

- 3.1. In June 2018, the Investment Sub Committee (ISC) resolved unanimously to:
- 3.1.1. approve a programme of new commitments to Private Equity over the years 2018-19 to 2021-22 of up to £240M;
 - 3.1.2. delegate to the Head of Pensions, in consultation with the Chairman, the timing of new commitments and selection of Private Equity funds from the following managers: Adams Street, Harbourvest, Pantheon and Partners Group.
- 3.2. In December 2018, new commitments of \$40m (c. £30m) each were made to global private equity funds managed by Adams Street and Harbourvest.
- 3.3. The impact of the increase in the strategic allocation from 5% to 7% will be to increase

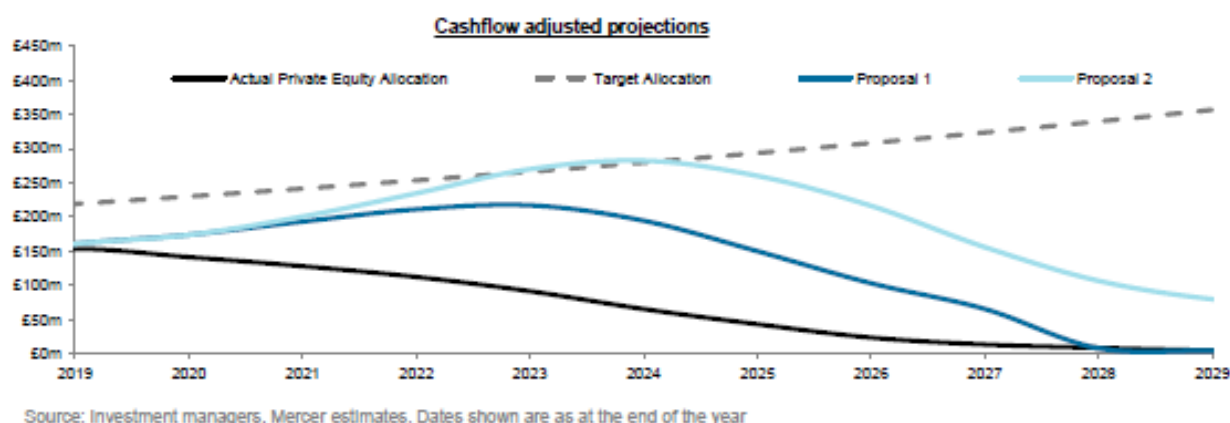
the recommended level of commitments above the annual rate implied in the 4 year plan previously approved and therefore exhaust the aggregate commitments of £240m more quickly than originally anticipated.

4. Review of existing portfolio

- 4.1. Mercer have analysed the Fund's existing commitments to the 22 vintages invested with ASP and 13 vintages invested with HV.
- 4.2. The analysis shows that:
 - 4.2.1. Geographically, the portfolio currently sits within the expected ranges for North America and Europe, but is slightly underweight in Asia/Emerging Markets, which is broadly where Mercer would expect;
 - 4.2.2. By investment stage, 64% of the portfolio is allocated to buyout-focussed strategies, with a material allocation to venture capital investments (c. 29%);
 - 4.2.3. Investment type is mainly primary investment strategies (c. 79%), followed by secondary investments (c. 16%) and direct/co-investments (5%).
- 4.3. As a result Mercer recommend that the Fund should continue to allocate globally (using secondary opportunities in the short-term and primaries to build/maintain the longer-term allocation), although the portfolio should continue to be monitored annually to ensure suitable diversification.

5. Private equity proposal

- 5.1. Mercer have modelled the forecast cash flows of the fund's existing commitments with ASP and HV and have also modelled two options showing the impact of the Fund making new commitments of:
 - 5.1.1. An allocation of c. £150m is made over two years starting September 2019 (c.£75m or c.\$95m p.a.);
 - 5.1.2. An allocation of c. £300m is made over four years starting September 2019 (c.£75m or c.\$95m p.a.).



- 5.2. As a result, Mercer's recommendation to the Head of Pensions is to:
 - 5.2.1. allocate c.£75m p.a. (c.\$95m p.a.) to private equity. It is noted that this annual level of annual commitment is out of line with the delegated budget of £240m over 4 years, but is recommended in order to grow the value invested towards the increased strategic allocation of 7%.

5.2.2. continue to allocate globally (using secondary opportunities in the short-term and primaries to build/maintain the longer-term allocation);

5.2.3. continue to be monitor the portfolio annually to ensure suitable diversification and to review progress towards the 7% strategic allocation.

5.3. Regarding manager and fund selection, Mercer have reviewed the products currently available from the four named managers taking into account the diversification by geography and investment stage that the Fund requires.

5.4. Mercer advise that the easiest and most cost effective way to achieve this exposure, is via the annual global flagship products that the Fund's two existing managers offer, namely the Adams Street - 2019 Global Program and the Harbourvest - 2019 Global Fund. The allocation should be split equally between the two managers.

5.5. Note that whilst Mercer would be comfortable in theory with investing with any of the four named managers, from a governance perspective, it would be advantageous to allocate to Adams Street and HarbourVest, given the existing relationships.

5.6. The Head of Pensions has consulted with the Chairman and agreed to implement the new commitments recommended by Mercer.

5.7. A further review of the Private Equity portfolio will be presented to the ISC in 2020.

6. Recommendation

6.1. That the Investment Sub Committee:

6.1.1. Note the Private Equity Funds to which the Fund will subscribe in year 2 of the approved 4 year programme.

7. Relevant Pension Fund Objectives

<i>Objective 1</i> Have robust governance arrangements in place, to facilitate informed decision-making, supported by appropriate advice, policies and strategies, whilst ensuring compliance with appropriate legislation and statutory guidance.
<i>Objective 3</i> Ensure the relevant stakeholders responsible for managing, governing and administering the Fund, understand their roles and responsibilities and have the appropriate skills and knowledge to ensure those attributes are maintained in a changing environment.
<i>Objective 5</i> Continually monitor and manage risk, ensuring the relevant stakeholders are able to mitigate risk where appropriate.
<i>Objective 18</i> Put in place a Strategic Asset Allocation ensuring it is appropriately maintained taking into account the Funding Strategy.

8. Finance & Resources Implications

- 8.1. The costs associated are contained within the presentations.

9. Risk management

- 9.1. The ISC have the Authority to review and maintain the asset allocation of the Fund within parameters agreed with the Pension Fund Committee and the authority to appoint and terminate investment managers to the Fund. In both proposing the strategy to the Pension Fund Committee and implementing the strategy the ISC are advised by external profession Investment Consultants, Mercer Ltd.
- 9.2. The risks associated with implementing the strategy have been captured in the Fund's risk register as detailed below.

Risk register	Risk mitigated	Residual risk
Investment (Risk 4)	Fund assets are not sufficient to meet obligations and liabilities as they become payable.	Amber
Investment (Risk 19)	Failure to act upon expert advice or risk of poor advice.	Green
Investment (Risk 23)	Investment decisions and portfolio management may not maximise returns or be performed in accordance with instructions provided.	Green

- 9.3. The Fund's full risk register can be found on the Fund's website at the following link:
<https://pensions.cambridgeshire.gov.uk/app/uploads/2019/05/RiskRegisterCPF.May2019.pdf>

10. Communication Implications

- 10.1. None.

11. Legal Implications

- 11.1. Legal advice will be sought as required.

12. Consultation with Key Advisers

- 12.1. This paper has been produced in conjunction with the Fund's Investment Consultants, Mercer.

13. Alternative Options Considered

- 13.1. Included in the paper.

14. Background Papers

14.1. None.

15. Appendices

15.1. Appendix A – Review of Private Equity Portfolio – August 2019 – Exempt paper.

Checklist of Key Approvals	
Is this decision included in the Business Plan?	Not applicable.
Will further decisions be required? If so, please outline the timetable here	Not applicable.
Is this report proposing an amendment to the budget and/or policy framework?	No.
Has this report been cleared by Chief Finance Officer/Section 151 Officer?	Yes. Sarah Heywood.
Has this report been cleared by Head of Pensions?	Yes. Mark Whitby.
Has the Chairman of the Pension Fund Committee been consulted?	Yes. Cllr Rogers.
Has this report been cleared by Legal Services?	Yes. Fiona McMillan.