Bath & North East Somerset Council	
MEETING:	**AVON PENSION FUND INVESTMENT PANEL**
MEETING DATE:	**11 September 2020**
TITLE:	**Review of Investment Performance for Periods Ending 30 June 2020**
WARD:	ALL
AN OPEN PUBLIC ITEM	
List of attachments to this report: Appendix 1 – Fund Valuation Appendix 2 – Mercer Performance Monitoring Report Appendix 3 – Brunel Quarterly Performance Report	

1. THE ISSUE

1.1. This paper reports on the performance of the Fund's investment managers and seeks to update the Panel on routine aspects of the Fund's investments. The report contains performance statistics for period ending 30 June 2020.

1.2. The report focuses on the performance of the individual investment managers and the implementation of the investment strategy. The full performance report with aggregate investment and funding analysis will be reported to the Committee meeting on 25 September 2020.

1.3. This quarter the Mercer risk monitoring report that usually forms Exempt Appendix 4 to this report (and covers the performance of the Liability Driven Investing and Equity Protection Strategies) is included in Item 9 – Annual Review of Risk Management Strategies.

2. RECOMMENDATION

2.1. **Notes information as set out in the reports.**

2.2. **Identifies any issues to be notified to the Committee.**

3. FINANCIAL IMPLICATIONS

3.1. The returns achieved by the Fund for the three years commencing 1 April 2019 will impact the next triennial valuation which will be calculated as at 31 March 2022. The returns quoted are net of investment management fees.

4. INVESTMENTS UPDATE

A – Fund Performance

4.1. The Fund's assets increased by £489m (c.10.9%) in the quarter ending 30 June 2019 giving a value for the investment Fund of £4,955m. Appendix 1 provides a breakdown of the Fund valuation and allocation of monies by asset class and managers.

4.2. The second quarter of this year saw a strong rebound in markets. Risk assets, with the exception of property, performed strongly as a whole and defensive assets delivered low single digit returns, Sterling weakened marginally over the quarter against the US Dollar, Yen and Euro. Further information on asset class performance can be found on page 9 of Appendix 2.

4.3. The Fund's overall performance relative to benchmarks is unavailable at the time of publishing. Full performance data will be reported to the Pensions Committee on 25 September 2020.

B – Investment Manager Performance

4.4. A detailed report on the performance of each investment manager has been produced by Mercer – see pages 22 to 41 of Appendix 2.

4.5. Brunel reports on the performance of the assets they manage on behalf of the Fund. The report for each Brunel portfolio can be found in Appendix 3. Mercer continue to provide quarterly commentary and analysis of all the Fund's mandates and at the strategic total fund level.

4.6. Manager total returns over the quarter were positive for all assets, with the exception of the property mandates. Equities in particular performed strongly due to co-ordinated central bank action. The Fund's DGF, Multi-Asset Credit and Fund of Hedge Funds strategies also performed well. Over the year, returns were mixed as some managers were not able to recover all of the losses incurred earlier in the year. Of the mandates with a 3-year track record most outperformed their respective benchmarks and performance targets with property mandates again the exception.

C – Risk Management Framework Quarterly Monitoring Report

4.7. A detailed report of the performance of the Fund's risk management strategies is presented in Exempt Appendix 1 to Item 9: Annual Review of Risk Management Strategies.

5. INVESTMENT STRATEGY AND PORTFOLIO REBALANCING

5.1. **Asset Class Returns versus Strategic Assumptions:** Developed market equity returns over the last 3 years were 8.8% p.a., ahead of the assumed strategic return of 8.1% p.a. on the same basis. The 3-year return from emerging market equities was 4.6%; below the assumed 3-year return of 8.7%. Over the 3-year period index-linked gilts returned 7.6% p.a. versus an assumed return of 2.2%. The 3-year UK property return of 3.9% p.a. lags its assumed return of 5.75%, due to continued recent uncertainty.

5.2. **Rebalancing:** There was no rebalancing activity during the quarter.

5.3. **Private Markets Investments:** At 30 June 2020 34% of the Fund's cycle 1 £115m commitment to Brunel's renewable infrastructure portfolio had been deployed and 32% of the Fund's £345m commitment to the secured income portfolio had been deployed. The pace of capital deployment across both asset classes has slowed due to managers deferring acquisitions as a result of the pandemic. The current best estimate suggests further capital will not be called until late 2020 for the long-lease property funds. Capital calls are expected to resume sooner for the infrastructure portfolio. The operational infrastructure element of the secured income portfolio has not been affected to the same extent as the long-lease property assets and the Fund's entire commitment of £94m to the underlying manager has been called following the acquisition of a renewable energy plant.

5.4. **Responsible Investment (RI) Activity:** During the quarter Brunel published their first Responsible Investment and Stewardship Outcomes Report, which evidences policy commitments on ESG risk integration, engagement and stewardship activities. The report seeks to meet the requirements of the new Financial Reporting Standards – Stewardship Code 2020 as well as the EU Shareholder Rights Directive and has been critical in forming the framework for our own Responsible Investment Annual Report, which will be reported to Committee at their next meeting.

5.5. Elsewhere, the shareholder resolution that Brunel co-filed with ShareAction requesting that Barclays publish a plan to phase out the provision of financial services to non-Paris aligned oil and gas companies led to the company publicly stating an ambition to become net zero by 2050. The shareholder resolution itself won significant minority support.

5.6. Human capital, a priority theme for the Fund, was the subject of two new engagement initiatives targeting workplace mental health and modern-day slavery. Specifically, Brunel joined investors representing $2.2tn in co-signing letters to FTSE100 companies asking that formal mental health workplans are established during the period of disruption brought about by the pandemic. Secondly, the Find it, Fix it, Prevent it campaign backed by the Principles for Responsible Investment, undertakes engagement with an aim to push for better public policy to facilitate effective corporate action on modern day slavery, to promote better processes for addressing slavery across supply chains and to develop better data for investors to act on modern day slavery. The initiative has so far received the backing of investors representing £3.5tn.

5.7. Finally, Brunel released their annual Carbon Metrics report which revealed that Brunel listed equity portfolios in aggregate are 15.4% more efficient in terms of carbon intensity than the broader market; Brunel's work on climate change has been recognised as they were named 'Pension Fund of the Year' at the recent Environmental Finance Sustainable Investments Awards.

5.8. **Voting and Engagement Activity:** Hermes engaged with 425 companies held by Avon in the Brunel segregated portfolios on a range of 1,135 ESG issues. Environmental topics featured in 16.7% of engagements, 80% of which related directly to climate change. Social topics featured in 14.7% of engagements, where human capital, human rights and diversity featured prominently. Of the 51.1% of Governance related engagements most focussed on executive remuneration and board diversity. Over the last quarter Hermes made voting recommendations at 394 meetings (5,622 resolutions). At 232 meetings they recommended opposing one or more resolutions. Over 60% of the issues Hermes voted against management on comprised board structure and remuneration. Aggregate voting data across all the Fund's investment managers will be reported to Committee at their next meeting.

5.9. **Revised Strategic Benchmark:** Following the conclusion of the 2019/20 investment strategy and the resultant asset allocation changes, Officers have been working with Mercer and the Fund's Custodian to revise the strategic benchmark that the Fund uses to benchmark total performance and identify where its managers are either adding or detracting value. To date the Fund's Custodian has not been able to factor the Fund's currency overlay programme into the strategic benchmark, which means aggregate level reporting is presented both including and excluding currency hedging in order to highlight the impact of the currency hedge and show performance relative to a like-for-like benchmark. Separately, the return from the LDI mandate, up until this point, has been manually added back into the strategic benchmark by Mercer. Due to the highly customised nature of the LDI mandate the Custodian has historically been unable to source an accurate proxy for the strategy and going forwards will use the change in the NAV as we seek to simplify the performance reporting process and ensure the greatest degree of consistency between the Fund's asset allocation and the strategic benchmark. These changes have been agreed and will be adopted from 3Q20. Officers and Mercer continue to work with the Custodian to explore options for integrating the Fund's FX overlay programme into the strategic benchmark in a cost-efficient manner. The revised composite benchmark can be seen in the below table:

Asset Class	**Benchmark used**	**Weight**
Global Equity	MSCI World	12.00%
Global sustainable equity	MSCI ACWI	10.00%
Low carbon passive equity	MSCI World LC Target	10.00%
EM Equities	MSCI Emerging Markets TR GD	5.50%
Diversified Returns	GBPSONIA+4%	10.00%
MAC	GBP3MLIBOR +4%	6.00%
UK Property	MSCI/AREF UK Quarterly Property Fund Index	3.75%
Overseas Property	MSCI Global Quarterly Property Fund Index	3.75%
Secured Income	CPI+2%	10.00%
Core Infrastructure	GBP3MLIBOR+5%	5.00%
Renewable Infrastructure	CPI+4%	5.00%
Private Debt	GBP3MLIBOR +4%	5.00%
Corp Bonds	Custom	2.00%
LDI	Custom	12.00%
FX Hedge	TBC	--
Total	--	100.00%

6. RISK MANAGEMENT

6.1. The Avon Pension Fund Committee is the formal decision-making body for the Fund. As such it has responsibility to ensure adequate risk management processes are in place. It discharges this responsibility by ensuring the Fund has an appropriate investment strategy and investment management structure in place that is regularly monitored. The creation of an Investment Panel further strengthens the governance of investment matters and contributes to reduced risk in these areas.

7. EQUALITIES

7.1. A proportionate equalities impact assessment has been carried out using corporate guidelines and no significant issues have been identified.

8. CLIMATE CHANGE

8.1. The Fund is implementing a digital strategy across all its operations and communications with stakeholders to reduce its internal carbon footprint in line with the Council's Climate Strategy. The Fund acknowledges the financial risk to its assets from climate change and is in the process of addressing this through its strategic asset allocation to Low Carbon Equities and renewable energy opportunities. The strategy is monitored and reviewed by the Committee.

9. OTHER OPTIONS CONSIDERED

9.1. None

10. CONSULTATION

10.1. The Council's Monitoring Officer and Section 151 Officer have had the opportunity to input to this report and have cleared it for publication.

Contact person	Nathan Rollinson, Investments Manager (Tel. 01225 395357)
Background papers	Data supplied by Mercer, Brunel & State Street Performance Measurement
Please contact the report author if you need to access this report in an alternative format	