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PUBLIC

To: Members of Pensions and Investments Committee

Monday, 3 June 2019

Dear Councillor,

Please attend a meeting of the **Pensions and Investments Committee** to be held at **10.00 am** on **Tuesday, 11 June 2019** in County Hall, Matlock, DE4 3AG, the agenda for which is set out below.

Yours faithfully,

Janie Berry

**JANIE BERRY**
**Director of Legal Services**

## A G E N D A

## PART I - NON-EXEMPT ITEMS

1. Apologies for Absence

   To receive apologies for absence (if any)

2. Declarations of Interest

   To receive declarations of interest (if any)

3. Minutes (Pages 1 - 12)

   To confirm the non-exempt minutes of the meeting of the Pensions and

Investments Committee held on 8 May 2019

To consider the reports of the Director of Finance and ICT on:

4. Investment Report (Pages 13 - 36)

5. Voting Activity (Pages 37 - 38)

6. Exclusion of the Public

To move "That under Regulation 21 (1)(b) of the Local Authorities (Executive Arrangements) (Access to Information) (England) Regulations 2000, the public be excluded from the meeting for the following items of business on the grounds that they involve the likely disclosure of exempt information as defined in Paragraph(s)… of Part 1 of Schedule 12A to the Local Government Act 1972"

**PART II - EXEMPT ITEMS**

7. Declarations of Interest

To receive declarations of interest (if any)

8. Minutes (Pages 39 - 44)

To confirm the exempt minutes of the meeting of the Pensions and Investments Committee held on 8 May 2019

To consider the exempt report of the Director of Finance and ICT on:

9. LGPS Central Limited - Presentation (Pages 45 - 64)

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**MINUTES** of a meeting of the **PENSIONS AND INVESTMENT COMMITTEE** held at County Hall, Matlock on 8 May 2019

**PRESENT**

Councillor N Atkin (in the Chair)

**Derbyshire County Council**

Councillors R Ashton, J Boult, P Makin, S Marshall-Clarke, R Mihaly, B Ridgway and G Wharmby (substitute Member)

**Derby City Council**

Councillor M Carr

**Derbyshire County Unison**

Mr M Wilson

Also in attendance – P Buckley, N Dowey, D Kinley, K Riley, N Smith and S Webster

Apologies for absence were received on behalf of Councillor J Perkins

**19/19** **PENSION BOARD MEMBER** The Chairman welcomed Mr Oliver Fishburn to the meeting. Mr Fishburn's proposed appointment to the Derbyshire Pension Board was due to be presented to the meeting of full Council on 15 May 2019.

**20/19** **MINUTES** **RESOLVED** that the minutes of the meeting held on 12 March 2019 be confirmed as a correct record and signed by the Chairman.

**21/19** **DERBYSHIRE PENSION FUND SERVICE PLAN** The Derbyshire Pension Fund Service Plan set out how the Pension Fund Team, which was made up of Investments staff and Pensions Administration staff, would contribute to the priorities of Derbyshire Pension Fund in 2019-20. The Service Plan, which was attached at Appendix 1 to the report, also described how these priorities would be delivered and how success would be measured.

The Plan also reported on progress against the objectives set out in the Fund's 2018-19 Service Plan and provided details of the services that were expected to be procured by the Fund up to 31 March 2021.

Members considered the Plan and asked that the planned development of a Climate Change Risk Strategy be included within the Plan.

**RESOLVED** that subject to the addition of the reference to development of the Climate Change Risk Strategy, the 2019-20 Service Plan be approved.

**22/19** **<u>RESPONSE TO THE 'LGPS FAIR DEAL – STRENGTHENING PENSION PROTECTION' POLICY CONSULTATION</u>** At the meeting on 12 March 2019, the Committee were informed of the Ministry of Housing, Communities and Local Government (MHCLG) consultation on proposals to amend the Local Government Pension Scheme (LGPS) regulations to provide greater pension protection for employees of LGPS employers who were compulsorily transferred to service providers.

Approval was granted at that meeting for a response to the consultation to be collated, and approval was delegated to the Director of Finance and ICT, in conjunction with the Chairman of the Committee. The Fund's response was submitted by the closing date of 4 April 2019 and was attached at Appendix 2 to the report.

Councillor Marshall-Clarke welcomed the report and thanked the Chairman of the Committee and the team of officers for the response.

**RESOLVED** that the Committee notes the Fund's response to the 'LGPS Fair Deal – Strengthening Pension Protection' policy consultation document issued by the Ministry of Housing, Communities and Local Government.

**23/19** **<u>REVIEW OF THE ADMINISTERING AUTHORITY DISCRETIONS POLICIES LOCAL GOVERNMENT PENSION SCHEME (LGPS)</u>** Under the LGPS Regulations, there were a number of areas where administering authorities and employers were permitted a level of discretion in the way they applied the rules locally for their employees and ex-employees who are/were members of the LGPS. Each LGPS administering authority and employer was required to agree and publish its policies around how these discretions would be applied. Additionally, the administering authority was required to exercise specific discretions relating to scheme members who were former employees of defunct employers.

Derbyshire Pension Fund's (the Fund) Administering Authority Discretions Policies were approved by the Committee at its meeting on 19 May 2014. The policies approved at that time related only to the mandatory policies which the Administering Authority were required by law to prepare and publish. Following changes to the LGPS introduced in The Local Government Pension Scheme (Amendment) Regulations 2018, a full review of the Fund's discretion policies had been undertaken.

Requirements when formulating policies and areas of discretion for administering authorities, were highlighted.

Where a member's employer or former employer had become defunct and ceased to be a Scheme employer (for example, it had gone into liquidation) Derbyshire County Council, as the administering authority, acted as the employer or former employer with respect to making decisions which the defunct employer would have been required to make, and as such, was required to publish its mandatory discretions.

To date, the Fund had applied Derbyshire County Council’s employer discretions policies in the circumstance of a ceased/defunct employer. However it was recognised that this was no longer appropriate as the funding position of an active scheme employer such as the County Council was different to that of an employer which had ceased to be a scheme employer and no longer participated in the scheme. The revised discretions policies recognised this difference.

The Local Government Pension Scheme (Amendment) Regulations 2018, which came into force on 14 May 2018, required the Local Government Pensions Committee (LGPC) to review the guidance it had previously issued in respect of discretions policies. Following its review, revised guidance had been published by the Local Government Pensions Committee (LGPC) in July 2018 and February 2019, relating to discretions for both administering authorities and employers. All participating scheme employers in Derbyshire Pension Fund had been asked to review their LGPS Employer Discretions Policies and submit their reviewed set of policies to the Pension Fund by 14 May 2019.

In order to assist employers, officers from the Fund included a discretions training session during the latest employer event held on 13 March 2019 which was attended by 41 employer representatives. Additionally, a guide to employer discretions, along with an example template of a set of policies, were published on the Fund’s website in January. All employers were notified about these resources in a newsletter issued on 4 February 2019.

In order to comply with the revised LGPC guidance, a full review of the administering authority discretions in place for the Fund had been undertaken which included discretions which applied to the administering authority’s role as employer where a member’s employer or former employer had become defunct. The proposed revised policies, which included all administering authority discretions, were included in the Statement of Policy on Administering Authority LGPS Discretions attached as Appendix 1 to the report. The policies would be reviewed upon a change in regulations or three years after their adoption, whichever was sooner.

A full list of administering authority and employer discretions was available on the LGPS Regulations and Guidance website managed by the LGA or from Derbyshire Pension Fund.

**RESOLVED** that the Committee, in its role as the administering authority of Derbyshire Pension Fund, approves the discretions policies set out in Statement of Policy on Administering Authority LGPS Discretions attached as Appendix 1 to the report.

**24/19** **TO PROVIDE DETAILS OF THE EMPLOYER DISCRETIONS IN THE LOCAL GOVERNMENT PENSION SCHEME (LGPS) REGULATIONS 2013** Mr Peter Buckley from the Human Resources Division attended the meeting to present the report. Following the introduction of the LGPS (Amended) Regulations 2018 which came into force on 14 May 2018 there were several employer discretions that required employers to publish their policy.

Employers were required to prepare, publish and keep under review a policy statement in relation to a number of mandatory scheme discretions. The Council's discretion policy statement was available on the Derbyshire County Council's website, however it must be reviewed and updated and be re-published by 14 May 2019. The report outlined changes to the currently published discretions policy.

The proposed LGPS discretions policy document had been updated to reflect the new and amended pension discretions and was attached at appendix 1 to the report. A summary of the changes were outlined and summary table attached at appendix 2 to the report, which highlighted the proposed changes.

The R85 was a complex protection for employees (and ex-employees) who were in the LGPS before 1 October 2006, and was the point when their age plus the time of their LGPS membership (in whole years) totalled 85. For most scheme members R85 only protected their pension benefits in respect of their membership before 1 April 2008 (i.e. 80$^{th}$s under the final salary arrangements), and was automatically applied at age 60 if the member met R85 before then. Where a member had met R85 and was retiring and drawing their pension after age 60, R85 applied in full.

However, where a member had met the rule of 85 and was retiring and drawing their pension between age 55 and 60, the employer could 'switch on' the R85 at a cost.

The R85 could be 'switched on' by the employer for:

- Current employees retiring
- Ex-employees with deferred benefits, retiring

- Ex-employees who had been awarded a tier ill health pension that was subsequently suspended.

The Council had previously published a discretion (reference No 5) in relation to R85 for a member voluntarily drawing benefits on or after age 55 and before age 60 for current contributing employees and leavers after 31/03/2014. As ‘switching on’ the R85 would incur a cost, the Council’s policy was not to ‘switch on’ the R85.

Under the amended regulations the Council was now required to publish its policy for deferred members and suspended tier 3 members voluntarily drawing benefits on or after age 55 and before age 60 for leavers. As ‘switching on’ the R85 would also incur a cost to the Council it was proposed that the Councils policy was not to “switch on” the R85.

HMRC rules relating to the earliest that someone could voluntarily retire and receive their pension changed in April 2010 from being age 50 to age 55, however some regulations in place before the change were still in force.

Due to this, the Council could grant a member aged over 50 and under 55 access to their pension, but it would be classed as an “unauthorised payment” for HMRC purposes and as such the individual would be subject to penal unauthorised payment charges of up to 55% but there was no cost to the Council for exercising this discretion.

**RESOLVED** to (1) approve the relevant changes to Derbyshire County Council’s discretions; and

(2) note that Councillors S Marshall-Clarke, R Mihaly and B Ridgway voted against this item.

**25/19 DERBYSHIRE PENSION FUND COMMUNICATIONS POLICY STATEMENT** Approval was sought for the draft Communications Policy Statement attached as Appendix 1 to the report.

Regulation 61 of the Local Government Pension Scheme Regulations 2013 required each Local Government Pension Scheme administering authority to produce and publish a policy statement describing how it communicated with its stakeholders. Derbyshire Pension Fund’s (the Fund) previous policy statement was published in 2015 and had been reviewed to reflect the developments since then in the Fund’s approach to communicating with its stakeholders. It was intended that the statement would be reviewed annually. It was agreed that a reference to local taxpayers and to the trade unions, as key stakeholders, would be included in the Communications Policy Statement.

**RESOLVED** that subject to the inclusion of a reference to local taxpayers and to the trade unions, the Communications Policy Statement be approved.

**26/19 <u>QUARTERLY PENSION ADMINISTRATION PERFORMANCE REPORT 1 JANUARY 2019 TO 31 MARCH 2019</u>** A report was presented from the Director of Finance & ICT on performance levels achieved by the pensions administration team of Derbyshire Pension Fund and other activity undertaken in the fourth quarter of 2018-19 (Q4).

Included in the report were details of performance data, including membership movements, backlog management, achievement against performance standards, employing authority performance, monthly contribution returns, new academies and admission bodies, and Application for Adjudication of Disputes Procedures cases; communications; governance; development, including procurement of replacement pensions administration system, and projects; and collaboration.

The statutory timescales against which performance was currently measured were set by The Occupational Pension Schemes Regulations 1996. Table 3 in the report captured performance against these targets in each quarter of 2018-19 so far.

The figures against 'Notification of Deferred Benefits' continued to reflect the low priority level attached to this work relative to work areas that resulted in immediate payments to Fund members. The dip in the figures for 'Transfers out paid' and 'Transfer out quotes' were the result of resource being allocated from that area to assist with the accurate migration of data from the UPM system to the Altair system ahead of implementation. Performance against the statutory timescales could not be measured during March 2019 due to the switch from UPM to Altair. Once the Altair system was fully established, it was intended to review the current approach to performance reporting and to adopt a more demanding set of targets.

There was a statutory requirement for employers to remit contributions by the 19th of the month following deduction from payroll. Employer performance in this area during Q4 was detailed in Table 4 to the report.

Due to the collation of responses a month after contributions were due, this report could only include a full set of figures from the first two months of Q4 2018/19. A late contribution return represented a statutory breach and each case was being recorded. Where remedial efforts, including charging, were not successful in improving employer performance, this evidence would be used in support of the submission of a report to The Pension Regulator.

It was reported that fourteen new academies had joined the Fund as scheme employers during Q4 2018-19 and five new admission bodies had also joined the Fund in Q4.

There had been three Application for Adjudication of Disputes Procedure cases presented to Pensions and Investment Committee for consideration during Q4.

An employer training event had been held at The Whitworth in Darley Dale on 13 March 2019 and the sessions focussed on two key areas, the valuation and employer discretions policies. The event was well attended and generally well received. Focussing in more detail on specific aspects of LGPS administration, rather than taking a generalist approach, was agreed to have been effective and may represent the way forward as the team developed its output.

Two Newsletters were issued to employing authorities in February 2019. The first included information on the 2018-2019 year end and fund valuation, the employer discretions policy, the Fund's Annual Report, new fair deal and ill health retirement. The second included an invitation to the employer training event on 13 March 2019, as well as information about a Pension Board vacancy, the year-end return and the LGPS employee contributions bands for 2019/2020.

The Pensions calculator service provided for Fund members on the Fund's website has proved very popular during 2018/19 with a total of 36,755 calculations carried out during the year. There had been a significant spike during the period that deferred and live Fund members received their Annual Benefit Statements.

During the period from 18 March 2019 to 15 April 2019, so overlapping into Q1 of 2019/20, a total of 607 calls had been received and the issues raised resolved by the team.

The Altair system successfully went live on 4 March 2019. As with all major new systems, there had been a number of initial issues to work through. The system supplier, Heywood, and the staff in the Pensions Team had worked well together in preparation for the implementation, and, since Go Live, had been resolving outstanding aspects of functionality. The Team had also been catching up with the backlogs of work created over the Go Live period. Members were provided with an update

**RESOLVED** to note the workloads and performance levels outlined in the report.

**27/19 THE RECORDING AND REPORTING OF STATUTORY BREACHES OF THE LOCAL GOVERNMENT PENSION SCHEME (LGPS) AND RELATED REGULATIONS** In compliance with the Pension Regulator's (TPR) Code of Practice 14 (CoP14), the Fund had had in place since 2015 an approved procedure for identifying, determining the material significance of, and reporting statutory breaches to TPR. (Appendix 1). Such breaches could be committed by the Fund, its employing authorities, or any of its stakeholders.

CoP14 also required public sector schemes to have in place a system to record breaches, even if they were not reported to TPR. Further to an exercise carried out with input from members of Derbyshire Pension Board, the Derbyshire Pension Fund Breaches Log (the Log) had been devised and implemented to cover all the aspects of managing statutory breaches. The Log had been devised to be a live, working document, in the manner of the Risk Register, in order to support continued transparency and consistency. An anonymised Log was attached as Appendix 2 to the report and the user guidance document was attached as Appendix 3.

It was intended that the Log would also support internal reporting on statutory breaches. Any additions or updates to the Log would be reported to the Pensions Office Management Team's monthly meeting, to the Derbyshire Pension Board's quarterly meeting, and in the Pensions Administration Performance report presented to Pensions and Investments Committee each quarter. This would ensure that all parties were fully informed of statutory breaches and should assist in reducing their recurrence.

**RESOLVED** to note the processes being used by Derbyshire Pension Fund to identify, record and report statutory breaches of the LGPS and related Regulations.

**28/19** **<u>DERBYSHIRE PENSION FUND RISK REGISTER</u>** The Risk Register was kept under constant review by the risk owners, with quarterly review by the Director of Finance & ICT. A copy of both the Summary and Main Risk Registers were presented. Changes from the previous quarter were highlighted. The Risk Register had the following three High Risk items:-

(1) Fluctuations in assets and liabilities (Risk No.15)
(2) LGPS Central – performance deterioration/lost cost savings or duplicated costs caused by LGPS Central transition delays (Risk No.30); and
(3) Impact of McCloud judgement (Risk No.39)

There was an inevitable risk for any pension fund that assets may be insufficient to meet liabilities and fluctuate from one valuation to the next, principally reflecting external risks around both market returns and the discount rate used to value the Fund's liabilities. Whilst the Fund had a significant proportion of its assets in growth assets, the newly agreed Strategic Asset Allocation Benchmark introduced a lower exposure to growth assets with the aim of protecting the improvement in the Fund's funding level following strong market gains since the triennial valuation in March 2016. The very strong performance of the UK bond market at the end of March 2019, on concerns surrounding Brexit, would have had a negative effect on the Fund's liabilities at the 31 March 2019 valuation date.

The transition of the Fund's assets into the products offered by LGPS Central Ltd. (LGPSC) was likely to take several years and there was a risk of performance deterioration and/or lost costs savings or duplicated management costs caused by transition delays. The Fund continued to take a meaningful role in the development of LGPSC, and had input into the design of the potential product offering to ensure that it would allow the Fund to implement its investment strategy. A Product Development Protocol was being developed jointly by the Partner Funds and LGPSC to ensure that all parties were involved at every stage of the product development lifecycle.

The transition into the Global Equity sub-fund by other Partner Funds was now complete and the transition process and costs were currently being analysed to see what lessons could be learnt from the first multi-Partner Fund transition.

Investment performance would be monitored closely by Fund officers and would be reported to the Pensions and Investment Committee and to the LGPS Central Joint Committee.

The McCloud case related to transitional protections given to scheme members in the judges and firefighters schemes which were found to be unlawful by the Court of Appeal on the grounds of age discrimination. The Government had applied to the Supreme Court for permission to appeal. It was anticipated that the outcome of the case could be accepted as applying to all public service schemes. The Government Actuary's Department was currently undertaking an initial review to assess the overall impact of the McCloud judgement on the public sector pension schemes. Fund officers would continue to follow closely the developments in the McCloud case and the implications for the LGPS, taking into consideration updates from the Scheme Advisory Board, the Local Government Association, the Government's Actuary's Department and the Fund's Actuary.

Risk No. 39, the impact of the McCloud judgement, was a new addition to the Risk Register. The risk relating to the implement of the replacement pensions administration system had been removed from the Risk Register following 'Go Live' on 4 March 2019. The residual risks relating to the implementation, primarily concerned with the additional backlogs caused by the migration, had been included in Risk No. 33 (Failure of pensions administration systems to meet service requirements/information not provided to stakeholders as required).

**RESOLVED** to note the risk items identified in the Risk Register.

**29/19** **TREASURY MANAGEMENT STRATEGY** Derbyshire Pension Fund (the Fund) traditionally adopted the same Treasury Management Strategy as the County Council which placed security of capital and liquidity ahead of investment return. Council approved the Treasury Management Strategy attached at Appendix 1 to the report on 6 February 2019. For operational purposes, the Fund predominantly used the same list of counterparties as the County Council and had agreed a joint limit with the Council for each counterparty. Due to the Fund's differing liquidity requirements, it did not invest in Pooled Funds (other than Money Market Funds) for treasury management purposes.

The Fund's current benchmark allocation to cash was 2% (about £100m at current asset values). The Fund generally needed to retain a higher level of instant access funds than the County Council. A major buying opportunity in the market could require immediate access to significant sums of cash for investment. Equally, it may be desirable to hold a higher defensive cash allocation because market valuations had become stretched or cash was held in order to meet future commitment drawdowns. The Fund's actual cash allocation at 31 March 2019 was 7.9%, equating to £389.6m. Future commitments at 31 March 2019 totalled some £450m, of which £85m was drawn-down immediately following the period end. The recommended Treasury Management Strategy requirements for 2019/20 were highlighted.

**RESOLVED** that the Treasury Management Strategy be approved.

**30/19** **EXCLUSION OF THE PUBLIC** **RESOLVED** that the public be excluded from the meeting during the Committee's consideration of the remaining items on the agenda to avoid the disclosure of the kind of information detailed in the following summary of proceedings:-

**SUMMARY OF PROCEEDINGS CONDUCTED AFTER THE PUBLIC HAD BEEN EXCLUDED FROM THE MEETING**

1. To confirm the exempt minutes of the meeting held on 12 March 2019 (contains exempt information)

2. To consider the exempt reports of the Director of Finance and ICT on:-

   (a) Summary of Appeals and Ombudsman Escalations during 2018-19
   (contains information relating to any individual)

   (b) Determination by the Pension Ombudsman
   (contains information relating to any individual)

   (c) Global Sustainable Equities
   (contains information relating to the financial or business affairs of any particular person (including the Authority holding that information))

(d) US Equities
(contains information relating to the financial or business affairs of any particular person (including the Authority holding that information))

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**Agenda Item No. 4(a)**

**DERBYSHIRE COUNTY COUNCIL**

**PENSIONS AND INVESTMENTS COMMITTEE**

**11 June 2019**

**Report of the Director of Finance & ICT**

# INVESTMENT REPORT

## 1 Purpose of the Report

To review the Fund's asset allocation, investment activity since the last meeting, long term performance analysis and to seek approval for the investment strategy in the light of recommendations from the Director of Finance & ICT and the Fund's independent adviser.

## 2 Information and Analysis

### (i) Report of the External Adviser

A copy of Mr Fletcher's report, incorporating his view on the global economic position, factual information for global market returns, the performance of the Fund and his recommendations on investment strategy and asset allocation, is attached as Appendix 1.

### (ii) Asset Allocation and Recommendations Table

The Fund's latest asset allocation as at 30 April 2019 and the recommendations of the Director of Finance & ICT and Mr Fletcher, in relation to the Fund's new strategic asset allocation benchmark, which became effective on 1 January 2019, are shown in the table overleaf.

The table also shows the recommendations of the Director of Finance & ICT, adjusted to reflect the impact of future investment commitments. These commitments (existing plus any new commitments recommended in this report) relate to Private Equity, Multi-Asset Credit, Property and Infrastructure and total around £356m. Whilst the timing of drawdowns will be lumpy and difficult to predict, the In-house Investment Management Team (IIMT) believe that these are likely to occur over the next 18 to 36 months.

| Asset Category | Old Benchmark | New Benchmark | Fund Allocation | Fund Allocation | Permitted Range | Benchmark Relative Recommendation | | Recommendation | | Adjusted for Commitments (1) | Benchmark Sterling Return | Benchmark Sterling Return |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | | | 31/1/19 | 30/4/19 | | AF 11/6/19 | DPF 11/6/19 | AF 11/6/19 | DPF 11/6/19 | DPF 11/6/19 | 3 Months to 31/3/19 | 3 Months to 30/4/19 |
| **Growth Assets** | **62.0%** | **57.0%** | **57.9%** | **59.0%** | **+/- 8%** | **+2.0%** | **(0.1%)** | **59.0%** | **56.9%** | **58.9%** | **n/a** | **n/a** |
| UK Equities | 25.0% | 16.0% | 17.9% | 18.1% | +/- 4% | - | +1.0% | 16.0% | 17.0% | 17.0% | 9.4% | 7.8% |
| Overseas Equities: | 33.0% | 37.0% | 40.0% | 38.1% | +/- 6% | +2.0% | +0.1% | 39.0% | 37.1% | 37.1% | n/a | n/a |
| North America | 12.0% | 12.0% | 10.9% | 11.4% | +/- 4% | (2.0%) | (2.0%) | 10.0% | 10.0% | 10.0% | 11.3% | 10.3% |
| Europe | 9.0% | 8.0% | 9.8% | 10.2% | +/- 3% | - | (0.5%) | 8.0% | 7.5% | 7.5% | 8.0% | 9.1% |
| Japan | 5.0% | 5.0% | 6.4% | 6.4% | +/- 2% | +1.0% | +1.0% | 6.0% | 6.0% | 6.0% | 4.5% | 3.0% |
| Pacific ex-Japan | 4.0% | 4.0% | 5.1% | 5.2% | +/- 2% | +1.0% | +1.2% | 5.0% | 5.2% | 5.2% | 8.6% | 6.5% |
| Emerging Markets | 3.0% | 5.0% | 5.0% | 4.9% | +/- 2% | +2.0% | (0.1%) | 7.0% | 4.9% | 4.9% | 7.9% | 5.4% |
| Global Sustainable | - | 3.0% | - | - | +/- 2% | - | +0.5% | 3.0% | 3.5% | 3.5% | 9.6% | 8.6% |
| Private Equity | 4.0% | 4.0% | 2.8% | 2.8% | +/- 2% | - | (1.2%) | 4.0% | 2.8% | 4.8% | 9.6% | 8.0% |
| **Income Assets** | **18.0%** | **23.0%** | **15.9%** | **18.1%** | **+/- 6%** | - | **(3.5%)** | **23.0%** | **19.5%** | **24.0%** | **n/a** | **n/a** |
| Multi-Asset Credit | 4.0% | 6.0% | 3.7% | 4.5% | +/- 2% | - | (0.5%) | 6.0% | 5.5% | 7.5% | 1.0% | 1.0% |
| Infrastructure | 5.0% | 8.0% | 4.0% | 5.7% | +/- 3% | - | (1.9%) | 8.0% | 6.1% | 8.2% | 0.7% | 0.7% |
| Direct Property (3) | 5.0% | 5.0% | 4.8% | 4.6% | +/- 2% | +1.0% | (0.4%) | 5.0% | 4.6% | 4.6% | 0.3% | 0.3% (2) |
| Indirect Property (3) | 4.0% | 4.0% | 3.4% | 3.3% | +/- 2% | (1.0%) | (0.7%) | 4.0% | 3.3% | 3.7% | 0.3% | 0.3% (2) |
| **Protection Assets** | **18.0%** | **18.0%** | **17.5%** | **16.9%** | **+/- 5%** | **(2.0%)** | **(1.1%)** | **16.0%** | **16.9%** | **16.9%** | **n/a** | **n/a** |
| Conventional Bonds | 5.5% | 6.0% | 5.7% | 5.4% | +/- 2% | (1.0%) | (0.6%) | 5.0% | 5.4% | 5.4% | 3.4% | 0.7% |
| Index-Linked Bonds | 6.5% | 6.0% | 5.7% | 5.6% | +/- 2% | (1.0%) | (0.4%) | 5.0% | 5.6% | 5.6% | 5.9% | 3.8% |
| Corporate Bonds | 6.0% | 6.0% | 6.1% | 5.9% | +/- 2% | - | (0.1%) | 6.0% | 5.9% | 5.9% | 5.0% | 2.6% |
| **Cash** | **2.0%** | **2.0%** | **8.7%** | **6.0%** | **0 – 8%** | **-** | **+4.7%** | **2.0%** | **6.7%** | **0.2%** | **0.1%** | **0.1%** |

(1) Recommendation adjusted for investment commitments at 30 April 2019 and presumes all commitments are funded from cash.
(2) Benchmark Return for the three months to 31 March 2019.
(3) The maximum permitted range in respect of Property is +/- 3%.

The table above reflects the following three categorisations:

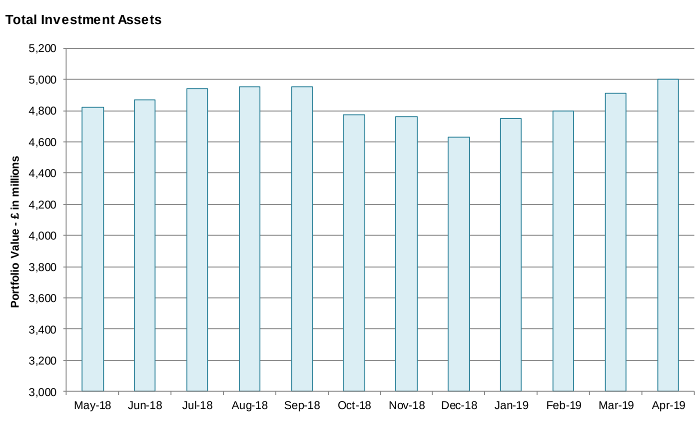
- **Growth Assets**: largely equities plus other volatile higher return assets such as private equity;
- **Income Assets**: assets which are designed to deliver an excess return, but with more stable return patterns than Growth Assets because income represents a large proportion of the total return of these assets; and
- **Protection Assets**: lower risk government or investment grade bonds.

Relative to the new benchmark, the Fund as at 30 April 2019, was overweight in Growth Assets and Cash, and underweight in Income Assets and Protection Assets.

If all of the Fund's commitments (existing plus any new commitments recommended in this report) were drawn-down, the cash balance would reduce by 5.8% to 0.2%. However, in practice as these commitments are drawn-down, they will be partly offset by new net cash inflows from dealing with members, investment income, distributions from existing investments and changes in the wider asset allocation.

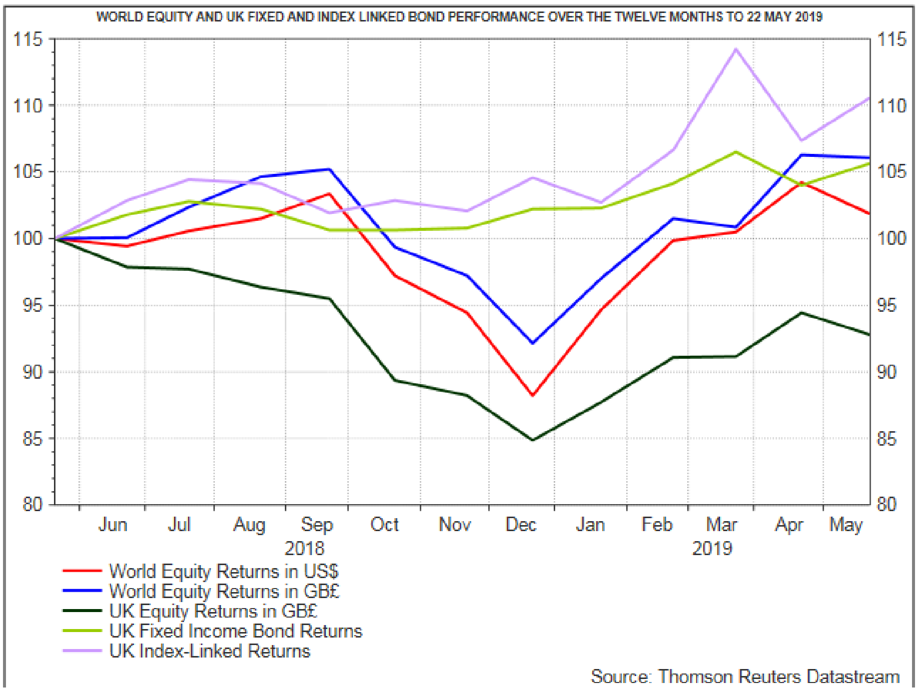
### (iii) Total Investment Assets

The value of the Fund's investment assets rose by £253.5m (5.3%) between 31 January 2019 and 30 April 2019 to in excess of £5.0bn for the first time, comprising a non-cash market gain of around £230m, partly offset by cash inflows from dealing with members & investment income of around £20m. Over the twelve months to 30 April 2019, the value of the Fund's investment assets has risen by £249.2m (5.2%), comprising a non-cash market gain of around £135m, an unexpected advanced contribution payment of £25m and cash inflows from dealing with members & investment income of around £90m. A copy of the Fund's valuation is attached at Appendix 2.




The Fund's valuation can fluctuate significantly in the short term, reflecting market conditions and supports the Fund's strategy of focusing on the long term.

## (iv) Market returns over the last 12 months




The chart above shows market returns for Global Equities in Sterling and the US dollar, UK Equities, UK Fixed Income and UK Index Linked bonds for the twelve months to 22 May 2019.

Global Equity markets generally rose between May and August 2018, reflecting robust US earnings growth and some easing in the trade tensions between the US and China, with returns for Sterling investors also benefiting from a stronger US$.  Global Equity markets then sold-off sharply in Q4 2018, with the quarter recording a 10.5% fall in sterling terms. Investor confidence was impacted by a number of factors, including concerns over the sustainability of US economic growth; an indication from the US Federal Reserve that there was scope for further interest rate rises; worries over a slowdown in China; and fears of a global trade war.

Equity markets subsequently recovered strongly in Q1 2019, with the FTSE All World Equity Index returning +12.2% in US Dollar terms; +9.6% in Sterling terms.  Whilst global economic data moderated in the quarter, optimism that trade relations between the US and China might improve, together with a more dovish tone from the US Federal Reserve, lifted equity markets. Although this optimism continued in April 2019 (FTSE World Equity Index up +3.4% in US Dollar terms; +3.4% in Sterling terms), equity market have been weaker in May 2019 (FTSE World Index down 4.4% in US Dollar terms between 1 May and 22 May 2019; down 1.6% in Sterling terms with the local currency impact partly been offset by a weaker GB£) as concerns about US – China trade relations resurfaced.

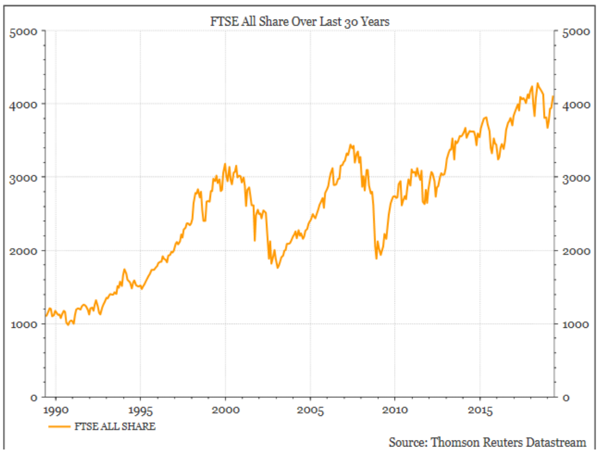
Bonds generally traded sideways between May and September 2018 before yields fell (i.e. prices rose) in Q4 2018, prompted by a general ‘‘risk-off’’ environment. Notwithstanding the recovery in equity markets in Q1 2019, 10 year government bond yields fell further over the quarter (UK -0.28%; US -0.28%; German -0.31%; and Japanese -0.08%) reflecting the impact of moderating economic data, which led central banks (including the US Federal Reserve) to push a more dovish policy stance. The US Federal Reserve removed its signal of interest rate rises for 2019, while the European Central Bank pushed its first forecast interest rate rise from the summer to the end of 2019. Politics also played a significant role, with continued uncertainty around US-China trade developments increasing demand for safe haven bonds. In the UK, government bond yields (gilts and index-linked bonds) also fell sharply in March 2019 in response to the Brexit impasse. UK index-linked bond yields were briefly impacted by uncertainty around the implications of a House of Lords inquiry into the way that the retail price index is calculated and index extensions, but the lack of progress on Brexit and in world trade talks dominated sentiment towards the asset class.

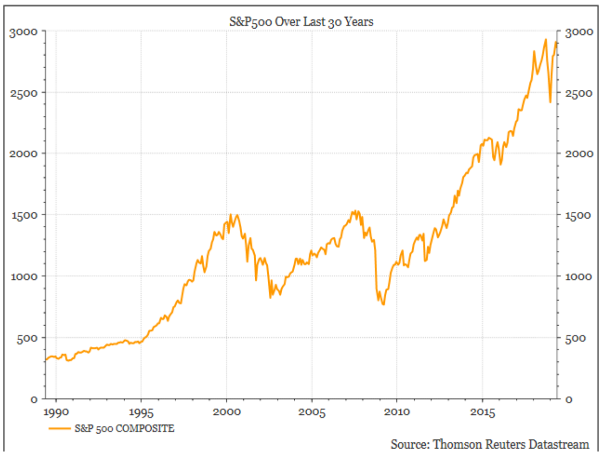
Corporate bond credit spreads narrowed over the quarter, with Sterling investment grade credit outperforming UK government bonds as dovish shifts from central banks contributed to the relative attractiveness of corporate debt relative to sovereign bonds.

UK 10 year government bond yields rose in April 2019 (i.e. prices fell) after the EU agreed to extend the article 50 deadline to 31 October 2019 (reducing the short term probability of a ‘‘no deal’’ exit from the EU), but fell again in May 2019, prompted by a general ‘‘risk-off’’ environment and continued political uncertainty. The announcement that Prime Minister May would be stepping down as leader of the Tory party on 7 June 2019 increased market forecasts of the probability of a “no deal” Brexit.

To put the fall in bond yields since September 2018 into context, the 10 year US Treasury yield has fallen by 74 basis points from 3.06% at 30 September 2018 to 2.32% at 24 May 2019, whereas the 10 year UK gilt yield has fallen by 63 basis points from 1.57% to 0.96% over the comparable period. Furthermore, it should be noted that the US yield curve ‘‘inverted’’ at the end of March 2019; this unusual situation, where short-dated bonds yield more than longer-dated bonds, is often seen as an indicator of a potential recession.

Asset class weightings and recommendations are based on values at the end of April 2019, and are relative to the new strategic asset allocation benchmark which will became effective on 1 January 2019. Many global stock markets are still trading close to all-time highs, despite the recent weakness in May 2019, and it should be noted that recent asset class returns (see charts below which show the long term performance of the FTSE All Share and S&P 500 Composite) remain well in excess of long term averages.




## (v) Longer Term Performance

Figures provided by Portfolio Evaluation Limited show the Fund's performance over 1, 3, 5 and 10 years to 31 March 2019.

| Per annum | DPF | Benchmark Index |
|---|---|---|
| | | |
| 1 year | 5.6% | 5.6% |
| 3 year | 10.1% | 9.5% |
| 5 year | 8.4% | 8.0% |
| 10 year | 10.5% | 10.4% |

The Fund performed in line with the benchmark over the last twelve months, and out-performed the benchmark over all other time periods.

## (vi) Category Recommendations

| | Old Benchmark | New Benchmark | Fund Allocation | Permitted Range | Recommendation | | Benchmark Relative Recommendation | |
|---|---|---|---|---|---|---|---|---|
| | | | 30 Apr-19 | | AF | DPF | AF | DPF |
| Growth Assets | 62.0% | 57.0% | 59.0% | ± 8% | 59.0% | 56.9% | +2.0% | (0.1%) |
| Income Assets | 18.0% | 23.0% | 18.1% | ± 6% | 23.0% | 19.5% | - | (3.5%) |
| Protection Assets | 18.0% | 18.0% | 16.9% | ± 5% | 16.0% | 16.9% | (2.0%) | (1.1%) |
| Cash | 2.0% | 2.0% | 6.0% | 0 – 8% | 2.0% | 6.7% | - | +4.7% |

*Presumes all commitments are funded from cash

The new strategic asset allocation benchmark reflects a re-balancing of the Fund's assets from Growth Assets to Income Assets, and also introduces a new 3% allocation to Global Sustainable Equities.

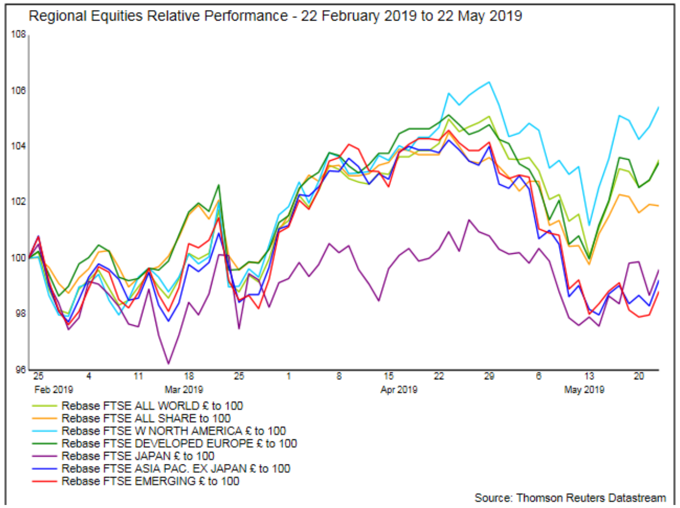
At an overall level, the Fund was overweight in Growth Assets at 30 April 2019, and underweight in Income Assets and Protection Assets, although if commitments waiting to be drawn down were taken into account, the Fund would move to a neutral position in Income Assets. The table on page 2 assumes that all new commitments will be funded out of the current cash weighting; in practice as private market commitments are drawn down they are likely to be funded partially out of cash and partially by distributions (income and capital) from existing investments and sales of public market assets. The Fund has progressively reduced its exposure to Growth Assets over the last two years, as equity valuations have become increasingly stretched, and increased the allocation to Income Assets and Protection Assets.

The IIMT recommendations reflected in this report, continue to build on this trend, with an additional 2.1% reduction in Growth Assets (UK Equities -1.1%; North American Equities -1.4%; European Equities -2.7%; Japanese Equities -0.4%; and Global Sustainable Equities +3.5%), a 1.4% increase in Income Assets (Multi-Asset Credit +1.0% and Infrastructure +0.4%), and a 0.7% increase in cash. The IIMT note that the recommendations are subject to market conditions, which could be significantly impacted in the short term by Brexit uncertainty, and flexibility will be required to respond to the resultant market conditions.  Furthermore, a proportion of the equity sales will be dependent on the investment of the proposed new 3.5% allocation to Global Sustainable Equities which is subject to the completion of satisfactory due diligence on several potential investment managers.

The IIMT continues to recommend a defensive cash allocation, believing that public markets continue to trade on rich valuations and appear too sanguine about the level of global political risk which has increased rather than diminished in recent months. Furthermore, as noted above, the cash weighting will be reduced as the Fund's current commitments are drawn down.

**(vii) Growth Assets**

At 30 April 2019, the overall Growth Asset weighting was 59.0%, up from 57.9% at 31 January 2019, reflecting relative market strength. Net divestment in the period was minimal.



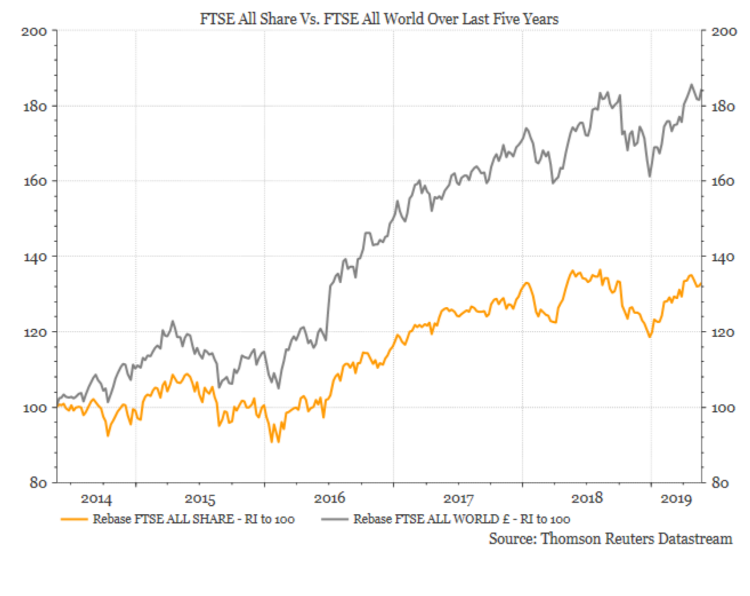

The IIMT recommendations below would reduce the overall Growth Asset weighting by 2.1% to 56.9%, 0.1% underweight relative to the benchmark. The IIMT believe that a small underweight position is warranted due to rich equity valuations, the increasingly late cycle nature of the global economy and the increased levels of market volatility.

The Chart opposite shows the relative regional equity returns since 22 February 2019. Global Equity markets returned +9.6% in Sterling terms in Q1 2019 (12.2% in local currency terms and the best quarter since 2012), and 11.5% in 2019 YTD (10.9% in local currency).

Q1 2019 returns were positive across all regions and reversed a decline of a similar magnitude in Q4 2018. In local currency terms, North American Equities were the best performer, returning 13.9%. Several other regions reported double-digit increases in local currency including European Equities (12.7%), Asia Pacific ex-Japan (11.1%) and Emerging Market Equities (10.4%). The worst performing major market was Japan with a Q1 2019 local currency return of 7.8% reflecting a the impact of a stronger ¥ on exports and weaker corporate earnings. Optimism that US – China trade relations might improve, together with a more dovish tone from the US Federal Reserve, lifted equity markets. Although this optimism continued in April 2019 (FTSE World Equity Index up 3.4% in Sterling terms), global equity market have been weaker in May 2019 (FTSE World Index down 1.6% in sterling terms) as concerns about US – China trade relations resurfaced.

## United Kingdom Equities

| DPF Weightings | |
|---|---|
| Old Neutral | 25.0% |
| New Neutral | 16.0% |
| | |
| Actual 30.4.19 | 17.9% |
| AF Recommendation | 16.0% |
| IIMT Recommendation | 17.0% |
| | |
| **Benchmark Returns** | |
| Q1 19/20 to date | 0.4% |
| Q4 18/19 | 9.4% |
| 1 Year | 6.4% |
| 3 Years (pa) | 9.5% |
| 5 Years (pa) | 6.1% |




Whilst there were minimal transactions in the period, relative market strength increased the weighting in UK Equities from 17.9% at 31 January 2019 to 18.1% at 30 April 2019; 2.1% overweight relative to the benchmark.

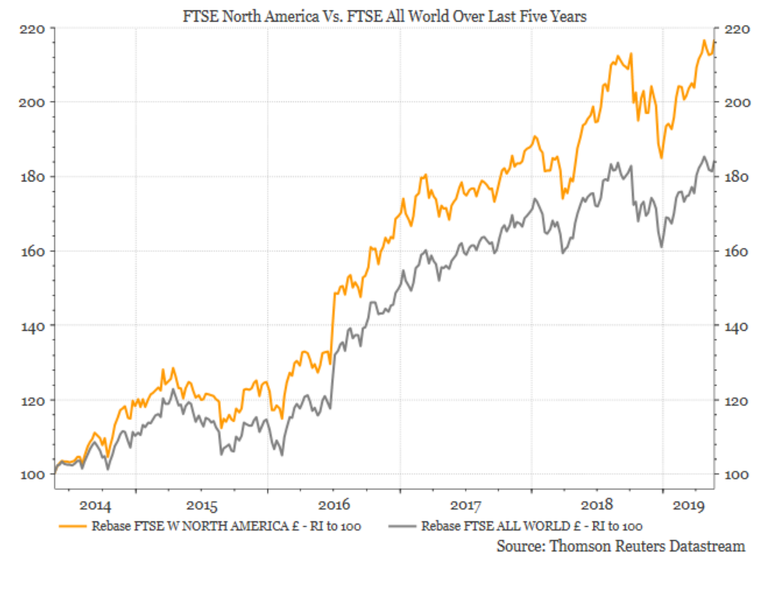
Mr Fletcher recommends a neutral weighting of 16% in UK Equities and notes that whilst progress is being made to bring the UK allocation down, this will take time.

UK GDP growth accelerated to 0.5% in Q1 2019 (1.8% on an annualised basis) from 0.2% in Q4 2018 (1.4% on an annualised basis) and the labour market remains relatively robust. However, political uncertainty has increased with the forthcoming election of a new leader for the Conservative Party further heightening uncertainty about the outcome of the Brexit negotiations. The IIMT believes that the current 2.1% overweight position relative to the new benchmark is difficult to justify against a background of continued Brexit induced market volatility. However, the IIMT recommends a 1.0% overweight position against the new benchmark (a 1.1% reduction of the current allocation) as UK equity valuations and dividend yields are attractive on both an absolute basis and on a relative basis compared to other equity markets.

The IIMT notes that the recommendation is subject to market conditions, which could be heavily impacted in the short term by Brexit developments and flexibility will be required to respond to the resultant market conditions.

## North American Equities

| DPF Weightings | |
|---|---|
| New Neutral | 12.0% |
| Old Neutral | 12.0% |
| | |
| Actual 30.4.19 | 11.4% |
| AF Recommendation | 10.0% |
| IIMT Recommendation | 10.0% |
| | |
| **Benchmark Returns** | |
| Q1 19/20 to date | 2.8% |
| Q4 18/19 | 11.3% |
| 1 Year | 17.5% |
| 3 Years (pa) | 17.1% |
| 5 Years (pa) | 15.8% |




There were no transactions in the three months to April 2019, but relative market strength increased the weighting to 11.4% at 31 January 2019, 0.6% underweight.

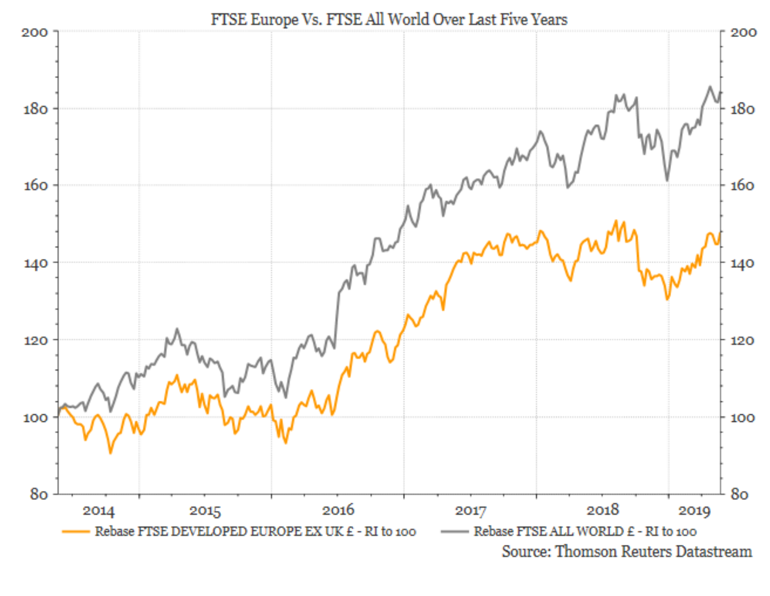
Mr Fletcher notes that because of the past strong performance of the US market on both an absolute and relative basis, and the relatively weaker future prospects, profits should be taken from the region.  As a result, Mr Fletcher recommends that the weighting is reduced to 10% (2.0% underweight).

The IIMT concurs with Mr Fletcher and believe that whilst the US continues to show resilient economic (Q4 2019 annualised GDP growth of 3.2%) and employment (non-farm payrolls rose by 263,000 in April 2019) growth, supported by tax cuts, less regulation and the repatriation of cash, the economy is now late cycle and US equity valuations appear increasingly stretched. There is little room for earnings to disappoint on the downside and the increased tension in the on-going US – China trade negotiations has increased the already elevated political uncertainty.

The IIMT believes that the recent sharp rise in the US equity market following the weakness in Q4 2018 (+13.8% YTD in local currency terms, 14.4% in Sterling terms) represents an opportunity to ‘‘lock-in’’ in some profit, and recommends reducing the current weighting by 1.4% to 10.0%, a 2.0% underweight position.

## European Equities

| DPF Weightings | |
|---|---|
| Old Neutral | 9.0% |
| New Neutral | 8.0% |
| | |
| Actual 30.4.19 | 10.2% |
| AF Recommendation | 8.0% |
| IIMT Recommendation | 7.5% |
| | |
| **Benchmark Returns** | |
| Q1 19/20 to date | 2.9% |
| Q4 18/19 | 8.0% |
| 1 Year | 2.7% |
| 3 Years (pa) | 11.0% |
| 5 Years (pa) | 7.0% |




There were no transactions in the three months to April 2019, but relative market strength increased the weighting to 10.2% at 30 April 2019, 2.2% overweight against the benchmark.

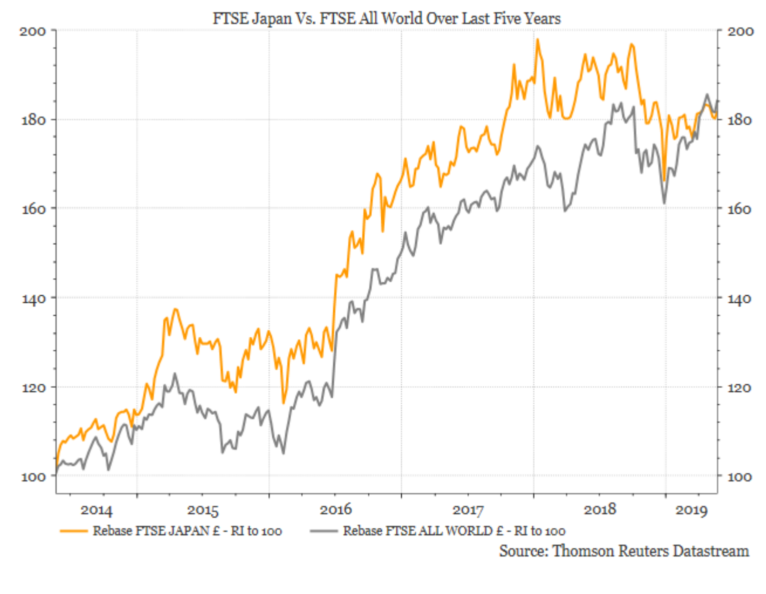
Mr Fletcher recommends a neutral position of 8%., noting that both the German and Italian economies returned to growth in Q1 2019, whereas France saw growth stagnate. Spain also saw its growth rate accelerate, helping to offset the weaker outcome for the Netherlands and Belgium whose economies were impacted by Brexit concerns. Mr Fletcher notes that because of the region's reliance on exports, it could suffer if the US - China trade negotiations are not resolved amicably.

The IIMT recommends a 0.5% underweight allocation of 7.5% to European Equities. Whilst the European Central Bank continues to support the Eurozone economy via accommodative monetary policy, the Eurozone economy has slowed significantly over the last three quarters (albeit growth did pick-up to 0.4% in Q1 2019). Combined with on-going political uncertainty, demonstrated by the recent European Union parliamentary elections which saw the long-established centre-right and centre-left blocs increasingly lose their combined majorities, and with the potential impact caused by Brexit, these factors are likely to cause periods of heightened uncertainty and volatility.

Furthermore, sluggish inflation and the inability of the European Central Bank to increase interest rates from their current record lows, means that there is little flexibility to lower rates to stimulate growth should economic growth remain subdued.

## Japanese Equities

| **DPF Weightings** | |
|---|---|
| Old Neutral | 5.0% |
| New Neutral | 5.0% |
| | |
| Actual 30.4.19 | 6.4% |
| AF Recommendation | 6.0% |
| IIMT Recommendation | 6.0% |
| | |
| **Benchmark Returns** | |
| Q1 19/20 to date | 0.6% |
| Q4 18/19 | 4.5% |
| 1 Year | (0.9%) |
| 3 Years (pa) | 12.3% |
| 5 Years (pa) | 11.7% |




There were no transactions in the three months to April 2019 and the weighting remained unchanged at 6.4%; 1.4% overweight against the benchmark.

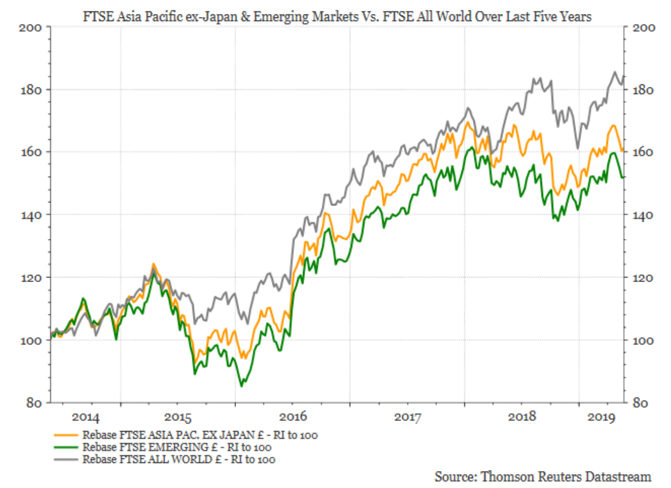
Mr Fletcher notes that whilst the Japanese market continues to disappoint, he likes its defensive characteristics and continues to recommend a 1% overweight allocation of 6%.

The IIMT notes that the Japanese economy continues to remain reasonably resilient (Q1 2019 GDP growth of 0.5%; 2.1% on an annualised basis), and this should allow Prime Minister Abe to press ahead with is on-going political and structural reforms.  The IIMT believes that the long term story in Japan remains intact, with structural changes in governance, the labour market and productivity.  Furthermore, valuations remain attractive relative both to their historical ranges and other developed markets, and the diversifying and defensive qualities of the Japanese market (e.g. the safe-haven status of the ¥) provide investment support.

However, the IIMT notes that Japanese corporate earnings have weakened and the strength of the Japanese ¥ may adversely impact on exports. Whilst an overweight position remains appropriate, the IIMT recommend that the allocation is reduced by 0.4% to 6.0%; 1.0% overweight overall.

## Asia Pacific Ex-Japan and Emerging Market Equities

| DPF Weightings | Asia-Pac | EM |
|---|---|---|
| Old Neutral | 4.0% | 3.0% |
| New Neutral | 4.0% | 5.0% |
| | | |
| Actual 30.4.19 | 5.2% | 4.9% |
| AF Recommendation | 5.0% | 7.0% |
| IIMT Recommendation | 5.2% | 4.9% |
| | | |
| **Benchmark Returns** | **Asia-Pac** | **EM** |
| Q1 19/20 to date | (2.5%) | (3.2%) |
| Q4 18/19 | 8.6% | 7.9% |
| 1 Year | 4.0% | 1.9% |
| 3 Years (pa) | 14.7% | 14.5% |
| 5 Years (pa) | 9.3% | 9.8% |




Relative market strength meant that the Fund's allocation to Asia Pacific Ex-Japan Equities increased to 5.2% at 30 April 2019 (1.2% overweight relative to the benchmark), whereas relative market weakness reduced the Emerging Market allocation to 4.9% (0.1% underweight relative to the benchmark).

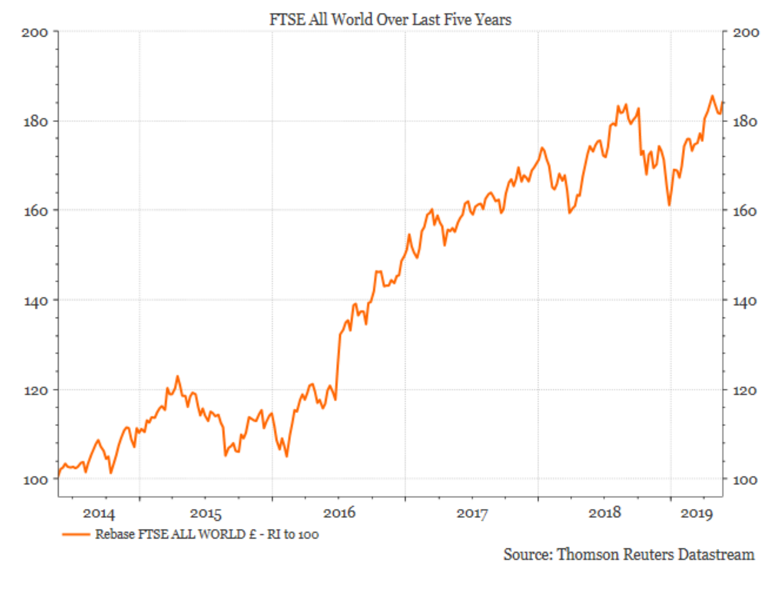
Mr Fletcher notes that the reasons for being overweight in these two markets remain unchanged (i.e. these economies represent a significant proportion of global growth and are growing, on average, roughly twice as fast as developed economies and have positive domestic macro fundamentals), and believes that both markets remain attractive on both a valuation and long term return basis. Mr Fletcher recommends a 1% overweight position in Asia Pacific Ex-Japan, and a 2% overweight position in Emerging Markets (i.e. 3% on a combined basis).

The IIMT continues to believe in the long term growth potential of these regions, but notes that the short-term outlook is less clear, and analysts' earnings forecasts for 2019 have been downgraded. There are signs of an economic slowdown driven by the threat of a global trade war, the strength of the US$ and concerns about a slow-down in the Chinese economy.

As a result, the IIMT recommends that the Fund maintains the Asia Pacific Ex-Japan weighting at 5.2% (1.1% overweight) and the Emerging Market weighting at 4.9% (0.1% underweight); 1.1% overweight on a combined basis.

## Global Sustainable Equities

| DPF Weightings | |
|---|---|
| Old Neutral | - |
| New Neutral | 3.0% |
| | |
| Actual 30.4.19 | - |
| AF Recommendation | 3.0% |
| IIMT Recommendation | 3.5% |
| | |
| **Benchmark Returns** | |
| Q1 19/20 to date | 1.7% |
| Q4 18/19 | 9.6% |
| 1 Year | 10.7% |
| 3 Years (pa) | 14.9% |
| 5 Years (pa) | 12.5% |




The new strategic asset allocation benchmark includes a 3% allocation to Global Sustainable Equities, and Mr Fletcher recommends a 3% neutral allocation. The Pensions and Investments Committee has recently approved the use a non-DCC framework to appoint two or three investment managers to manage the planned allocation on a discretionary basis and the IIMT is currently carrying out due diligence on the potential investment managers. The IIMT is positive about the long term growth prospects for the asset class and recommends a 0.5% overweight allocation of 3.5%, whilst noting that the completion of the necessary due diligence is likely to take several months and some flexibility will be required around the timing of any investment.

## Private Equity

| DPF Weighting | | | | | |
|---|---|---|---|---|---|
| Old New | New Neutral | Actual 30.4.19 | Committed 30.4.19 | AF Recommendation | IIMT Recommendation |
| 4.0% | 4.0% | 2.8% | 4.8% | 4.0% | 2.8% |
| | | | | | |
| **Benchmark Returns** | | | | | |
| Q1 19/20 to date | Q4 18/19 | 1 Year | 3 Years (pa) | 5 Years (pa) | |
| 0.5% | 9.6% | 7.4% | 10.5% | 6.8% | |

The Private Equity allocation remained unchanged between 31 January 2019 and 30 April 2019 at 2.8%; 4.8% on a committed basis.

Mr Fletcher recommends a neutral weighting of 4% in Private Equity. The IIMT continues to seek out opportunities which offer higher returns than public markets, including co-investment and secondary funds, and recommends that the current invested and committed weightings are maintained while opportunities are assessed.

The IIMT notes that private equity multiples have increased over the last few years, and are now approaching record highs, particularly in respect of large and mega cap deals. The IIMT believes that future commitments should be targeted towards small and mid-cap private equity managers, with a focus on investing in companies with strong secular trends, scalable business models (e.g. operational level and growth through bolt-on acquisitions), robust cash flows, and sustainable capital structures.

### (viii) Income Assets

At 30 April 2019, the overall weighting in Income Assets was 18.1%. The IIMT recommendations below would take the overall Income Asset weighting to 19.5%, and the committed weighting to 24.0%.

### Multi Asset Credit

| **DPF Weighting** | | | | |
|---|---|---|---|---|
| Old Neutral | New Neutral | Actual 30.4.19 | AF Recommendation | IIMT Recommendation |
| 4.0% | 6.0% | 4.5% | 6.0% | 4.5% |
| | | | | |
| **Benchmark Returns** | | | | |
| Q1 19/20 to date | Q4 18/19 | 1 Year | 3 Years (pa) | 5 Years (pa) |
| 0.6% | 1.0% | 3.8% | n/a | n/a |

Net investment of £47m (£40m in February; £5m in March; and £2m in April 2019) was partly offset by relative market weakness and the Fund’s weighting increased to 4.5% at 30 April 2019; 6.5% on a committed basis versus a neutral weight of 6%.

Mr Fletcher recommends a neutral 6% allocation to Multi-Asset Credit in order to increase the diversified opportunity set going forward. Mr Fletcher believes that investing in shorter duration sub-investment grade high-yield bonds and emerging market debt could protect the Fund from the potential scale of negative returns that gilts could experience should interest rates rise. He also believes that this lower interest rate risk, combined with the recent widening of credit spreads, has made these assets more attractive.

The IIMT continues to remain positive about the long-term attractions of this asset class, but notes that high yield bond yields have rallied strongly in YTD19 following a sharp ‘‘risk-off’’ fall in Q4 2018. The IIMT believes that the scope for further spread compression has reduced, and notes that some parts of the Multi-Asset Credit portfolio are likely to under-perform in a ‘‘risk-off’’ environment. The IIMT continues to prefer a bias towards defensive forms of credit (e.g. senior secured corporate or infrastructure debt with low default rates) with strong covenants, floating rate protection and a yield pick-up, whilst noting that both multiples and leverage are rising and investment needs to be supported by robust due diligence.

The IIMT recommends increasing the invested weighting by a further 1.0% to 5.5% in the upcoming quarter; 7.5% on a committed basis, albeit the IIMT notes that this recommendation should be subject to market conditions at the time. Whilst this implies the pension fund will be 1.5% overweight should all the commitments be drawn-down, in practice it is unlikely that the commitments will be fully drawn, and some of the existing closed-ended investments have now entered their distribution phase (i.e. returning cash to investors).

**Property**

| DPF Weighting | | | | |
|---|---|---|---|---|
| Old Neutral | New Neutral | Actual 30.4.19 | AF Recommendation | IIMT Recommendation |
| 9.0% | 9.0% | 7.9% | 9.0% | 7.9% |
| | | | | |
| **Benchmark Returns** | | | | |
| Q1 19/20 to date | Q4 18/19 | 1 Year | 3 Years (pa) | 5 Years (pa) |
| Not Available | 0.3% | 4.3% | 6.0% | 9.4% |

There was no net investment in the period and relative market weakness reduced the weighting to 7.9% at 30 April 2019, with Direct Property accounting for 4.6% (0.4% underweight) and Indirect Property accounting for 3.3% (0.7% underweight). The committed weight was 8.3% at 30 April 2019.

Mr Fletcher notes that the property market continues to provide diversified returns for the Fund and that the Direct Property Manager has outperformed. Mr Fletcher continues to recommend a neutral overall allocation to Property, with a preference for a 1% overweight position in Direct Property and a 1% underweight in Indirect Property. Mr Fletcher recognises that it will take time to build the property allocation to a neutral position.

The IIMT recommends maintaining the current 4.8% allocation to Direct Property while the Property Manager continues to seek out attractive propositions, with a focus on those sectors with the best performance outlook (in particular the industrial sector), strong tenants and rent reviews linked to RPI & CPI.  The IIMT continues to assess indirect property opportunities, with a focus on vehicles invested in specialist areas which provide strong covenants and sustainable rental growth. The IIMT recommends maintaining the Indirect Property weighting at 3.3% (3.7% on a committed basis), whilst actively investigating further investment opportunities in this asset class.

**Infrastructure**

| DPF Weighting | | | | | |
|---|---|---|---|---|---|
| Old Neutral | New Netural | Actual 30.4.19 | Committed 30.4.19 | AF Recommendation | IIMT Recommendation |
| 5.0% | 8.0% | 5.7% | 8.2% | 8.0% | 6.1% |
| | | | | | |
| **Benchmark Returns** | | | | | |
| Q1 19/20 to date | Q4 18/19 | 1 Year | 3 Years (pa) | 5 Years (pa) | |
| 0.5% | 0.7% | 2.8% | 2.5% | 2.0% | |

Investment in the three months to April 2019 totalled £89m, and the invested weighting increased to 5.7%. The committed weight totalled 8.2% at 30 April 2019.

Mr Fletcher recommends a neutral weighting of 8% relative to the benchmark, acknowledging that this will take time to achieve.

The IIMT believes that Infrastructure is an attractive asset class, with a bias towards core infrastructure assets which offer favourable risk-adjusted returns, predictable long term cash flows which are often linked to inflation, and low correlation to other major asset classes. The IIMT continues to assess future investment opportunities in line with these objectives, and also recommends that rising levels of political and regulatory risk are managed through increased levels of geographical diversification.

The IIMT recommends increasing the invested weighting by 0.4% to 6.1% in the upcoming quarter, in anticipation of commitment draw-downs.

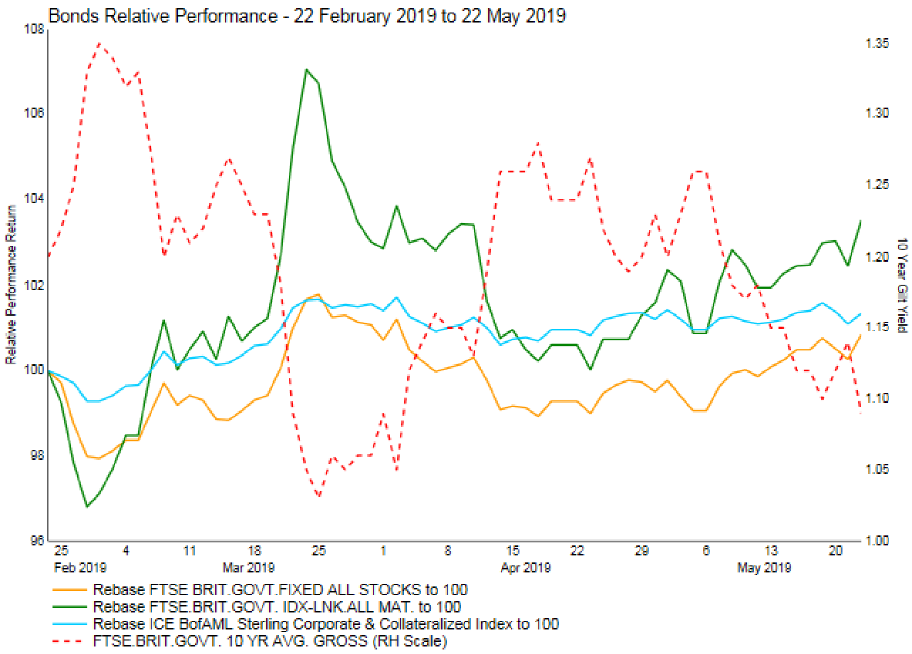
## (ix) Protection Assets

The weighting in Protection Assets at 30 April 2019 was 16.9%, down from 17.5% at 31 January 2019, reflecting lower relative (albeit positive) market returns. There were no transactions in the period.

The IIMT recommendations below maintain the weighting at 16.9%.

The Chart opposite shows the relative bond returns in respect of UK Conventional Bonds, UK Index-Linked Bonds and UK Corporate between 22 February 2019 and 22 May 2019.

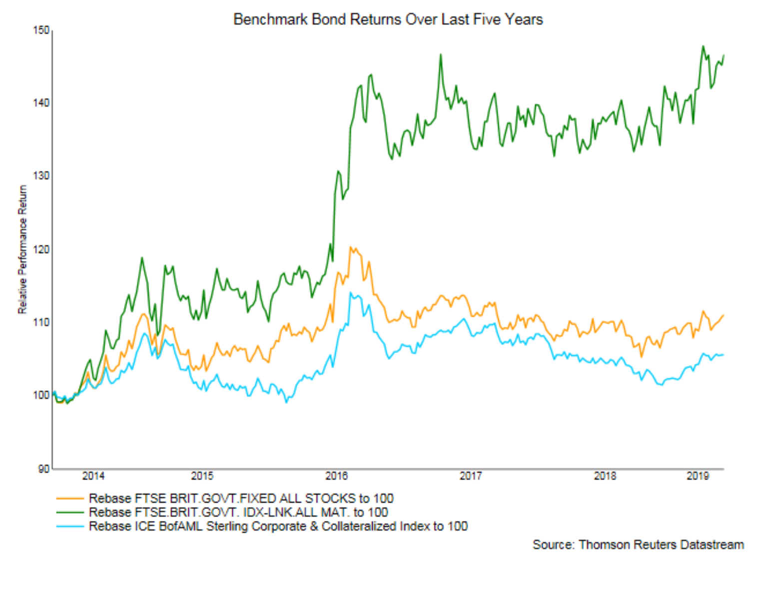
UK 10 year government bond yields fell (i.e. price rose) sharply in March 2019 as uncertainty about the UK's departure from the EU intensified and the UK Government's Withdrawal Agreement failed to gain approval in the House of Commons.  Yields subsequently rose in April 2019 after the EU agreed to extend the article 50 deadline to 31 October 2019; reducing the short term probability of a ''no deal'' exit from the EU but fell again in May 2019, prompted by a general ''risk-off'' environment and continued UK political uncertainty.



Source: Thomson Reuters Datastream

## Conventional Bonds

| DPF Weightings | |
|---|---|
| Old Neutral | 5.5% |
| New Neutral | 6.0% |
| | |
| Actual 30.4.19 | 5.4% |
| AF Recommendation | 5.0% |
| IIMT Recommendation | 5.4% |
| | |
| **Benchmark Returns** | |
| Q1 19/20 to date | 0.5% |
| Q4 18/19 | 3.4% |
| 1 Year | 3.7% |
| 3 Years (pa) | 3.6% |
| 5 Years (pa) | 5.5% |



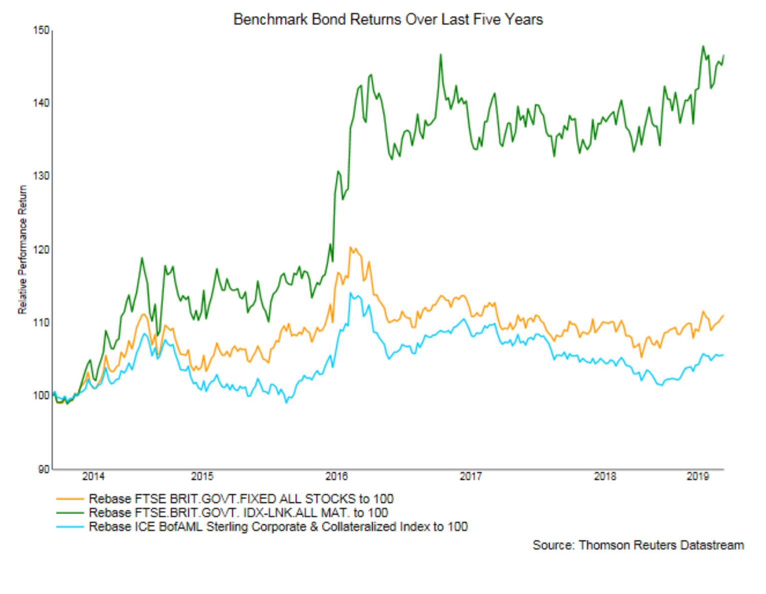

Whilst there were no transactions in the period, relative market weakness reduced the weighting in Conventional Bonds to 5.4% at 30 April 2019.

Mr Fletcher recommends a 1.0% underweight position of 5.0% against the benchmark. Mr Fletcher notes that fundamentally little has changed since the time of the last Committee with respect to this asset class. The global economy continues to grow at a reasonable pace and inflation appears benign. Equity markets have recovered and bond yields have fallen; the fall in bond yields has been helped by the US Federal Reserve deciding to pause monetary tightening and to make Quantitative Tightening data dependent. As a result, Mr Fletcher believes that the best of the news for bond markets is already priced into the current level of yields. Mr Fletcher finds it difficult to believe that government bond yields can fall further below their current levels over the medium term, nor that credit spreads will substantially narrow further. Whilst there is scope for volatility generated by economic data and the US – China trade negotiations, Mr Fletcher believes that by the end of the next twelve months bond yields will have drifted higher (lowering prices).

The IIMT agrees that conventional sovereign bonds do not appear to offer good value at current levels. However, they are diversifying assets and continue to afford greater protection than other asset classes in periods of market uncertainty – as demonstrated in the recent Q4 2018 global equity market sell-off and during periods of heightened Brexit uncertainty. The IIMT recommends maintaining the current weighting of 5.4%, 0.6% underweight relative to the benchmark.

## Index-Linked Bonds

| **DPF Weightings** | |
|---|---|
| Old Neutral | 6.5% |
| New Neutral | 6.0% |
| | |
| Actual 30.4.19 | 5.6% |
| AF Recommendation | 5.0% |
| IIMT Recommendation | 5.6% |
| | |
| **Benchmark Returns** | |
| Q1 19/20 to date | 1.4% |
| Q4 18/19 | 5.9% |
| 1 Year | 5.5% |
| 3 Years (pa) | 8.3% |
| 5 Years (pa) | 8.9% |



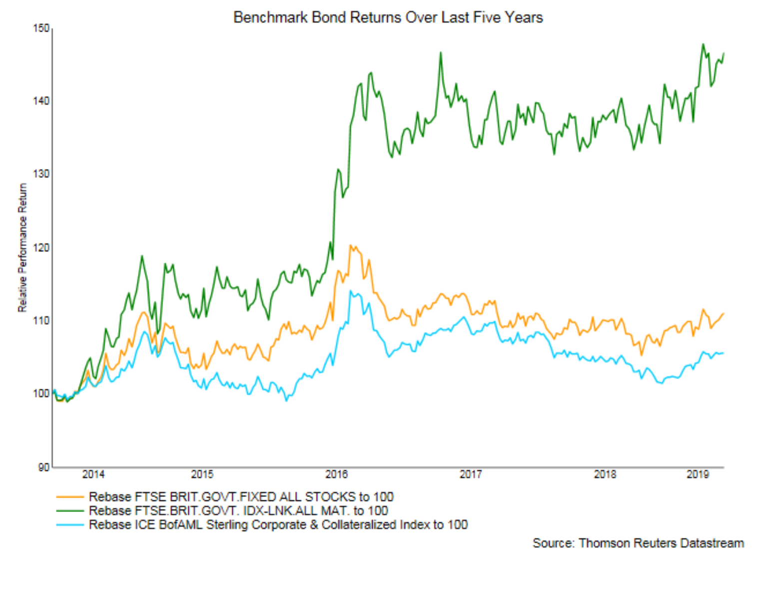

Relative market weakness reduced the weighting in Index Linked Bonds to 5.6% at 30 April 2019. There were no transactions in the period.

Mr Fletcher notes that UK Index-Linked gilts have now become even more expensive, and the long duration of these bonds increases the risk of adverse returns in a rising yield environment. Mr Fletcher believes that it is appropriate to be underweight in this asset class, and recommends a 1.0% underweight position of 5%, and that the Fund should continue to hold some US TIPS (US Index Linked Bonds) as well as UK Index Linked. Although Mr Fletcher notes that the cost of hedging the currency risk needs to be taken into consideration when investing in bonds outside the UK.

The IIMT agrees with Mr Fletcher regarding the current value of UK Index-Linked Bonds and recommends that the current 0.4% underweight position of 5.6% against the benchmark is maintained, with the current exposure to US TIPS (around 20% of the Index-Linked portfolio) being maintained due to the greater potential for price appreciation in US Index Linked Bonds.

## Corporate Bonds

| DPF Weightings | |
|---|---|
| Old Neutral | 6.0% |
| New Neutral | 6.0% |
| | |
| Actual 30.4.19 | 5.9% |
| AF Recommendation | 6.0% |
| IIMT Recommendation | 5.9% |
| | |
| **Benchmark Returns** | |
| Q1 19/20 to date | 0.6% |
| Q4 18/19 | 5.0% |
| 1 Year | 4.0% |
| 3 Years (pa) | 5.5% |
| 5 Years (pa) | 6.0% |




Whilst there were no transactions in the period, relative market weakness reduced the weighting in Corporate Bonds at 30 April 2019 to 5.9%; 0.1% underweight relative to the benchmark.

Mr Fletcher notes that the current outlook for the investment grade non-government bond market is uncertain. Spreads have narrowed on stronger equity markets and the perceived end of monetary tightening has provided a duration benefit. Mr Fletcher notes that should government bond yields rise, so will investment grade credit yields, albeit the shorter duration of investment grade bonds relative to government bonds, should afford some protection provided defaults are avoided. However, despite these reservations, Mr Fletcher recommends a neutral allocation of 6% to investment grade credit because the ‘‘bigger risk’’ is in longer duration government bonds especially Index-Linked Bonds.

The IIMT believe that the current average credit spread, of around 120 basis points over sovereign bonds, is increasingly insufficient to compensate for the increased default and volatility risk. As a result, the IIMT recommend that the current 0.1% underweight allocation of 5.9% is maintained.

### (x) Cash

The cash weighting at 30 April 2019 was 6.0%, 4.0% overweight relative to the benchmark.

Mr Fletcher notes that whilst the high cash balance has helped moderate poor performance at a time of volatility, there is no requirement to carry such a high cash balance. Mr Fletcher acknowledges that much of the cash held is committed to fund managers that have yet to draw-down their allocations for investments, and further draw-downs will reduce the level of cash.

The IIMT notes that markets have experienced several bouts of volatility over the past twelve to eighteen months, and continues to believe that public markets are trading on rich valuations despite increasing levels of global political risk and the increasing maturity of the US economic expansion.

Against this background, the IIMT recommends a defensive cash allocation of 6.7%. The IIMT is actively investigating options for reducing the cash allocation, and notes a continued emphasis on making commitments to more attractively priced illiquid markets. Furthermore, it should be noted that the cash weighting will reduce as private market commitments are drawn down.

## 3 Other Considerations

In preparing this report the relevance of the following factors has been considered: financial, legal and human rights, human resources, equality and diversity, health, environmental, transport, property and prevention of crime and disorder.

## 4 Background Papers

Files held by the Investment Section.

## 5 Officer's Recommendations

5.1 That the report of the external adviser, Mr Fletcher, be noted.

5.2 That the asset allocations, total assets and long term performance analysis in this report be noted.

5.3 That the strategy outlined in the report be approved.

PETER HANDFORD

Director of Finance & ICT

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**Agenda Item No. 4(b)**

**DERBYSHIRE COUNTY COUNCIL**

**PENSIONS and INVESTMENTS COMMITTEE**

**11 June 2019**

**Report of the Director of Finance & ICT**

**VOTING ACTIVITY**

## 1 Purpose of the Report

To review Derbyshire Pension Fund's (the Fund) voting activity for the period 28 February 2019 to 24 May 2019.

## 2 Information and Analysis

Details of the Fund's voting activity for the period 28 February 2019 to 24 May 2019 are shown in Appendix 1. The Fund's votes against management proposals are shown in Appendix 2 and the total shareholder votes for these proposals are set out below. With the exception of the Micro Focus International Plc resolution and the two Informa Plc resolutions, each of the resolutions set out in Appendix 2 were subsequently passed.

| Resolution | Votes For | Votes Against |
|---|---|---|
| | | |
| CC Japan Income & Growth Trust Plc: Resolution 13 | 86.81% | 13.17% |
| Micro Focus International Plc: Resolution 3 | 49.67% | 50.33% |
| Segro Plc: Resolution 3 | 53.30% | 46.70% |
| Brendon Group Plc: Resolution 9 | 90.89% | 9.11% |
| Barclays Group Plc: Resolution 2 | 70.79% | 29.21% |
| Schroders Plc: Resolution 3 | 87.99% | 12.01% |
| InterContinental Hotels Group Plc: Resolution 2 | 83.95% | 16.05% |
| Standard Chartered Plc: Resolution 4 | 63.80% | 36.20% |
| Standard Life Aberdeen Plc: Resolution 5 | 57.98% | 42.02% |
| Informa Plc: Resolution 5 | Resolution Withdrawn | |
| Informa Plc: Resolution 12 | Resolution Withdrawn | |

The Micro Focus International Plc resolution related to the approval of the Directors' Remuneration Report. The Fund's third party institutional voting service provider raised a number of concerns in respect of the remuneration policy (see Appendix 2) and recommended that investors voted against the resolution. Amanda Brown, Chair of the Remuneration Committee commented ''we acknowledge and respect the concerns of our shareholders and have already committed to undertake a thorough review of our reward strategy this year with the objective of putting a new policy to shareholders at the 2020 AGM. The Remuneration Committee will continue to consult closely with shareholders throughout this process, and reflect very carefully on any issues that arise''.

The two Informa Plc resolutions related to the re-election of Cindy Rose and David Wei as Directors to the Board. The Fund's third party institutional voting service provider raised a number of concerns in respect of re-elections (see Appendix 2) and recommended that investors voted against the resolutions. Both resolutions were withdrawn prior to the meeting and Informa Plc noted that ''Cindy Rose and David Wei chose not to stand for re-election to the Board, so as to focus on their other professional commitments''.

## 3 Other Considerations

In preparing this report the relevance of the following factors has been considered: financial, legal and human rights, human resources, equality and diversity, health, environmental, transport, property and prevention of crime and disorder considerations.

## 4 Officer's Recommendation

That the report be noted.

PETER HANDFORD

Director of Finance & ICT

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of the Local Government Act 1972.



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of the Local Government Act 1972.

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