

Report for: ACTION



<b>Contains Confidential or Exempt Information</b>	NO – Part I
<b>Title</b>	Developing Markets Investment Strategy
<b>Responsible Officer(s)</b>	Nick Greenwood Pension Fund Manager
<b>Contact officer, job title and phone number</b>	Nick Greenwood Pension Fund Manager 01628 796701
<b>Member reporting</b>	Investment Working Group
<b>For Consideration By</b>	Berkshire Pension Fund and Pension Fund Advisory Panels
<b>Date to be Considered</b>	18 January 2016
<b>Implementation Date if Not Called In</b>	Not applicable
<b>Affected Wards</b>	None

### REPORT SUMMARY

- Attached to this report is a paper considered by and approved by the Investment Working Group regarding the development of a multi-asset approach to investing in Developing Markets. It seeks Panel's approval for this strategy and authority for Officers to implement it after consultation with the Investment Working Group on specific investment opportunities

### If recommendations are adopted, how will residents, fund members and other stakeholders benefit?

Benefits to residents and reasons why they will benefit	Dates by which residents can expect to notice a difference
1. A clear strategy on investment in Developing Markets will ensure that exposure to these markets is well diversified.	31 <sup>st</sup> March 2017

## 1. DETAILS OF RECOMMENDATIONS

### RECOMMENDATION: That Panel:

- i. **Approve the Developing Markets Investment Strategy at Annex 1**
- ii. **Authorise Officers to implement it after consultation with the Investment Working Group on specific investment opportunities.**

## 2. REASON FOR RECOMMENDATION(S) AND OPTIONS CONSIDERED

Details of the proposed strategy are at Annex 1. For the avoidance of doubt Developing Markets encompasses all countries other than those recognised as Developed Markets (that is North America, Western Europe, Japan, Australia and New Zealand).

Members are requested to note that the private debt proposal mentioned in the annex was not proceeded with given concerns over its exposure to commodity based borrowers.

<b>Option</b>	<b>Comments</b>
Agree and implement proposed strategy	<b>Recommended by Officers and the Investment Working Group</b>
Do not agree the strategy	Not recommended as this could result in undue concentration in one asset class
Authorise Officers to implement the strategy after consultation with the Investment Working Group on specific investment opportunities	<b>Recommended by Officers on the grounds that this is the most efficient way of implementing the strategy</b>
Do not authorise Officers to implement the strategy after consultation with the Investment Working Group on specific investment opportunities	Not recommended as this would slow implementation and require Panel to approve every investment.

## 3. KEY IMPLICATIONS

### 3.1

<b>Defined Outcomes</b>	<b>Unmet</b>	<b>Met</b>	<b>Exceeded</b>	<b>Significantly Exceeded</b>	<b>Date they should be delivered by</b>
Strategy Implemented	Strategy not implemented	Strategy Implemented	Strategy Implemented by 30 Sept 2017	Strategy Implemented by 31 March 2017	31 March 2018

#### **4. FINANCIAL DETAILS**

Investments to be funded from cash-flow (including capital cash-flows as private funds return capital) and by sale/redemption of existing investments as and when appropriate

#### **5. LEGAL IMPLICATIONS**

5.1 None

#### **6. VALUE FOR MONEY**

6.1 Wherever possible the investment team will negotiate to minimise asset managers' fees.

#### **7. SUSTAINABILITY IMPACT APPRAISAL**

7.1 Not applicable

#### **8. RISK MANAGEMENT**

8.1

<b>Risks</b>	<b>Uncontrolled Risk</b>	<b>Controls</b>	<b>Controlled Risk</b>
Developing Markets exposure concentrated in too few asset classes	High	Diversify exposure across asset classes	Medium
Developing Markets exposure concentrated in too few countries/locations	High	Diversify exposure across countries/locations	Medium
Poor selection of asset managers	Medium	Due diligence on managers	Low

#### **9. LINKS TO STRATEGIC OBJECTIVES**

9.1 Forms part of the Fund's overall investment strategy

#### **10. EQUALITIES, HUMAN RIGHTS AND COMMUNITY COHESION**

10.1 Not required

#### **11. STAFFING/WORKFORCE AND ACCOMMODATION IMPLICATIONS**

11.1 None

#### **12. PROPERTY AND ASSETS**

12.1 None

**13. ANY OTHER IMPLICATIONS**

13.1 None

**14. CONSULTATION**

14.1 Investment Working Group

**15. TIMETABLE FOR IMPLEMENTATION**

15.1 As opportunities arise

**16. APPENDICES**

16.1 Annex 1 (attached)

**17. BACKGROUND INFORMATION**

17.1 Annex 1 (attached)

## Annex 1 - Developing Markets Investment Strategy

### Proposal for a Multi-Asset Approach

The IWG at its meeting on 30th January 2015 resolved that the Fund should increase its Developing Markets exposure towards a target of 25% of the Fund's net assets.

This paper presents a proposed solution for creating such a multi-asset approach to Developing Markets and recommends a timetable for implementation.

The table below shows the Fund's current exposure to Developing Markets which has slipped below 15% of the total. This is due to two factors – the sale of the Nomura Small Company fund (reinvested in RWC dividend growth mandate) and the decline in Emerging Market Equity markets relative to other asset classes.

Asset Class	Market Value £m	Uncalled Cash £m	Weighting % (Whole Fund)	Developing Markets Asset Allocation % (Current Value)	Developing Markets Asset Allocation % (including uncalled amounts)
Emerging Market Equities	160.2		9.5	64.8	61.7
Frontier Markets Equities	56.7		3.4	23.0	21.9
Private Equity	7.1	11.2	0.4	2.9	7.0
Infrastructure	15.2	1.1	0.9	6.1	6.3
Property	8.0		0.5	3.2	3.1
Absolute Return					
<b>Totals</b>	<b>247.2</b>	<b>12.3</b>	<b>14.7</b>	<b>100.0%</b>	<b>100.0%</b>

The key fundamentals that investment in these markets should focus on include:

- The population of SE Asia exceeds that of the rest of the world
- Most (not all admittedly) developing markets are forecast to have faster GDP growth than Developed markets
- Infant mortality in developing markets is falling
- Increasing urbanisation – by 2025 47% of global GDP growth is forecast to be from 440 expanding cities in developing countries (source).?
- Forecast of 1 billion new urban consumers in developing markets by 2025 with an expected annual consumption of \$10 trillion.(source)?
- Increasing demand for food, water and energy.

Whilst emerging and frontier market listed equities will give exposure to these themes the increasing globalisation of world stock-markets does mean that many such listed

stocks have only modest exposure to their domestic markets. This does suggest that private equity (focussed on the consumer, urbanisation and increasing demand for food, water and energy) may offer higher exposure.

The table below gives a recommended broad asset allocation for a multi-asset developing market portfolio:

<b>Asset Class</b>	<b>Current Weighting (after outstanding calls)</b>	<b>Current Value £m</b>	<b>Proposed Target</b>	<b>Proposed Value £m</b>	<b>Range</b>
Listed Equity	83.6%	216.9	50%	170.0	35-75%
Private Equity	7.0%	18.3	7.5%	25.0	5-25%
Infrastructure	6.3%	16.3	10%	34.0	5-15%
Property	3.1%	8.0	10%	34.0	5-15%
Bonds	0.0%		15%	52.0	0-30%
Absolute Return	0.0%		7.5%	25.0	0-15%
<b>Total</b>		<b>259.5</b>		<b>340.0</b>	

### **Next steps**

**Listed Equities** – Long term aim is a reduction, however, following recent weakness it was considered that no reduction should be made at this time but that a search for an emerging markets equity dividend growth manager should be commenced during Quarter 4 2015 with a target of funding in Spring/Summer 2016.. Officers suggest a mandate value of £75m with a target income of £3 million growing by UK CPI over the next 5 years.

**Private Equity** – With headroom of £7.7 million (approx. \$12 million) Officers should be requested to review opportunities and report to IWG when suitable opportunities are found.

**Infrastructure** – Officers to review opportunities and report to IWG when suitable opportunities are found.

**Property** – We should engage with Aviva and advise them that the Fund would like to allocate an additional £26 million to Emerging Market real estate. The conversation with Aviva should also include the potential for raising some of this additional capital from the existing Aviva Funds of Funds.

**Bonds** – Largely dependent on timing – the Fund previously appointed Stone Harbour after a search in 2008 and it would be relatively simple to reinvest with them. Potential investments in Private Debt should also be considered as and when suitable opportunities arise

**Absolute Return** – Whilst there are many hedge fund managers based in Emerging Markets (particularly Hong Kong, Singapore and South Africa) most are “global” rather

than Emerging Market managers. Officers should research the universe and report to IWG in 2016.