Northern Powerhouse Pool Submission Document

1. Exec Summary

1.1 Purpose of document

1.1.1 This document is a joint submission to Government from Tameside Metropolitan Borough Council, Wirral Metropolitan Borough Council and City of Bradford Metropolitan District Council, the respective administering authorities of the Greater Manchester Pension Fund, Merseyside Pension Fund and West Yorkshire Pension Fund ("the Funds")

1.1.2 The administering authorities have signed a Memorandum of Understanding (attached as Appendix A to this submission) which sets out, at a high-level;

i) how the Funds will work together to form a Collective Asset Pool ("the Pool") which meets the criteria released by Government on 25 November 2015 and;
ii) the expected operation of the Pool when established.

1.1.3 The remainder of this document provides the rationale behind the proposed structure and operation of the Pool. This has been developed by drawing on the knowledge and experience of the Funds' officers and committees, via high-level financial modelling undertaken by PwC (summary report attached as Appendix B) and legal advice from Squire Patton Boggs (attached as Appendix C).

1.2 Benefits that the Pool will deliver

- All funds in the Pool will make new infrastructure commitments via an expanded Greater Manchester/LPFA infrastructure vehicle. Subject to committee approval the capacity of this vehicle will be expanded to approximately £1bn during 2016. This will enable investment in larger infrastructure investments on a direct basis.
- The significant internal resource and experience of the participating funds will enable the Pool to start making collective investments well in advance of Government timescales – cost savings will therefore start to be delivered from an early stage.
- Once Government approval to the Pool is obtained we will quickly implement the collective monitoring and benchmarking of legacy illiquid assets, generating improvements in governance and costs savings above the requirements set out in the Criteria and Guidance.
- As a result of the above, we expect cost savings to emerge from Summer 2016 onwards, with estimated savings of around £30m per annum on alternative/illiquid assets.
- Expectation of being lowest cost pool in the LGPS on a like-for-like basis.

1.2.2 The Pool remains open to other funds to join us on the basis of the Memorandum of Understanding contained within this submission, and this will remain the case up until we submit our final proposals in July 2016. This will enable other LGPS funds to share in the benefits outlined above.

1.3 Contents

2. Background

2.1 Government's proposal

2.2.1 In the Summer Budget in July 2015, the Government issued an appeal to Local Government Pension Scheme (LGPS) administering authorities to pool their investments to significantly reduce costs, while maintaining or improving overall investment performance. The Government invited administering authorities to come forward with their own proposals to meet common criteria to delivering savings. These proposals would need to be 'sufficiently ambitious'.

As part of the Autumn Budget in November 2015, Department for Communities and Local Government (DCLG) released the Investment Reform Criteria that the pooling arrangements should have regard to in developing the pooling proposals. These are:

1. **Asset pools that achieve the benefits of scale:** There will be at most 6 asset pools, each of which should be at least £25bn of Scheme assets in size.

2. **Strong governance and decision making:** At a local level, the governance structure should provide authorities with assurance that their investments are being managed appropriately by the pools, in line with the stated investment strategy and in the long-term interests of their members. At a pool level, the governance structure should ensure that risk is adequately assessed and managed, investment implementation decisions are made with a long-term view, and a culture of continuous improvement is adopted.

3. **Reduced costs and excellent value for money:** Proposals should explain how the pool will deliver substantial savings in investment fees, both in the near term and over the next 15 years, while at least maintaining overall investment performance.

4. **An improved capacity to invest in infrastructure:** Proposals should explain how infrastructure will feature in authorities' investment strategies and how the pooling arrangements can improve the capacity and capability to invest in this asset class.

2.2 Overview of Funds

2.2.1 <u>Greater Manchester Pension Fund ('GMPF')</u>

GMPF is the UK's largest LGPS fund. The Fund has assets of £17.6bn at 31 March 2015, with over 340,000 members across more than 400 contributing employers.

GMPF has an excellent long-term investment track record – GMPF is ranked 5th over 25 years by WM within their Local Authority Universe at 31 March 2015. Performance (gross of fees) to 31 March 2015 is summarised in the table below:

GMPF Annualised investment returns				
1 year	**5 years**	**10 years**	**20 years**	**25 years**
11.7%	8.3%	8.4%	8.3%	9.0%

Listed-securities are generally managed externally via large low-cost multi-asset mandates. Private market assets, with the exception of property, are generally managed internally.

GMPF employs approximately 16 designated investment staff plus legal and accounting support.

GMPF has for many years made direct local infrastructure investments and more recently has experience of investing in collaboration with others funds (such as the infrastructure partnership with LPFA).

2.2.2 Merseyside Pension Fund ('MPF')

Merseyside Pension Fund has assets of £6.5bn and provides the Local Government Pension Scheme for the Merseyside region, delivering pensions' administration, investment and accounting on behalf of the 5 Merseyside District Councils, 145 other employers and over 128,000 scheme members.

The Fund has a ten strong experienced and professionally qualified internal investment team which has delivered consistently good performance by employing a combination of internal and external management and active and passive strategies. This has been achieved with lower risk than the typical LGPS fund. The Fund has a long track record of investing in Alternatives, including infrastructure and has a substantial direct property portfolio.

Performance (gross of fees) to 31 March 2015 is summarised in the table below:

MPF Annualised Investment returns			
1 year	**5 years**	**10 years**	**20 years**
12.6%	8.6%	7.9%	8.1%

2.2.3 West Yorkshire Pension Fund ('WYPF')

WYPF is the UK's 4th largest LGPS fund. The Fund has assets of £11.3bn at 31 March 2015, with over 260,000 members across more than 400 contributing employers.

WYPF has the lowest investment management cost of all LGPS Funds of £11.49 per member or 0.026% of funds under management.

WYPF has an excellent long-term investment track record and it ranked 11th over 20 years, and 15th over 25 years by WM within their Local Authority Universe at 31 March 2015. Performance to 31 March 2015 is summarised in the table below:

WYPF Annualised investment returns				
1 year	**5 years**	**10 years**	**20 years**	**25 years**
11.8%	8.3%	8.3%	8.3%	8.8%

WYPF is almost entirely in-house managed. The active, long term, low risk, low turnover approach has been central to the achievement of low cost outperformance, and high funding levels compared to the average LGPS fund.

The team of 14 investment professionals actively manage equity portfolios in virtually all countries where markets are investable. Bond portfolios covering domestic and overseas government and corporate bonds are actively managed. In addition a diverse portfolio of alternative assets including infrastructure, property, and private equity are managed by way of unitised investments. The WYPF also invests directly in property.

The investment team is stable and investment managers typically have 20 years investment experience. Particular strength is found in the long term stock selection performance vs the market in several equity and bond portfolios whilst maintaining low risk.

2.2.4 Relative investment performance and costs

All 3 funds have strong long-term investment performance and are ranked in the top quartile of LPGS funds on a 20-year basis. When analysed net of investment costs the relative performance will be stronger still due to the relatively low investment management costs of the funds.

Investment cost per member for 2014/15 taken from the DCLG website are:-

Fund	**Rank**	**Investment cost - £ per member 2014/15**
West Yorkshire	1	11.49
Greater Manchester	3	39.01
Merseyside	28	105.41
All England		142.28

2.3 Project POOL

2.3.1 Officers of the Funds all had significant involvement in the work of Project POOL which was the report from LGPS funds to Government supported by Hymans Robertson. This included sitting on the steering group of the project and leading individual asset-class workstreams.

2.3.2 Many aspects of the Pool's proposed operation are in line with the recommendations set out in the Project Pool report.

3. Investment Philosophy

3.1 Like mindedness

3.1.1 The long-term vision of the Pool is to provide participating funds with access to a range of internal and external investment management and related services at low cost, to enable the participating funds to continue outperforming their benchmark and reduce costs to fund employers and local tax-payers.

3.1.2 The Funds have a combined assets base of £35bn as at 31 March 2015. The intention is that the vast majority of the assets will be managed and monitored from initial formation by the Pool.

3.1.3 The proportion of assets in the pool that are internally managed is expected to increase over time.

3.1.4 LGPS funds exist to meet the benefit promises made to members (i.e. the liabilities). The nature of the liabilities influences the asset allocation of each fund. All funds acknowledge that asset allocation is the dominant determinant of portfolio risk and return.

3.1.5 Markets can be inefficient. Risk premia exist for equity, credit, duration, illiquidity, inflation and volatility. The key principles of the investment approach are a long-term perspective and to maintain simple arrangements with a relatively low number of managers and low manager and portfolio turnover.

3.1.6 The pension committees of the participating funds will retain responsibility for liabilities, setting the strategic asset allocation of their fund, funding strategy statement and appropriate strategy documents.

3.1.7 Subject to continuing to meet best practice and mandates being of sufficient size to ensure low cost, participating funds will also retain the ability to select asset class (equity, bonds, property etc…including multi-asset), territory (UK, Europe, US etc.. or global) style (value, growth etc…) and whether managed actively or passively. For an initial period, participating funds will have the discretion to determine whether a mandate is managed internally by the Pool – as the Pool contains significant capacity and experience in this area or by an external manager. This will enable participating funds who have not previously used internal management to gain comfort of its operation and vice versa.

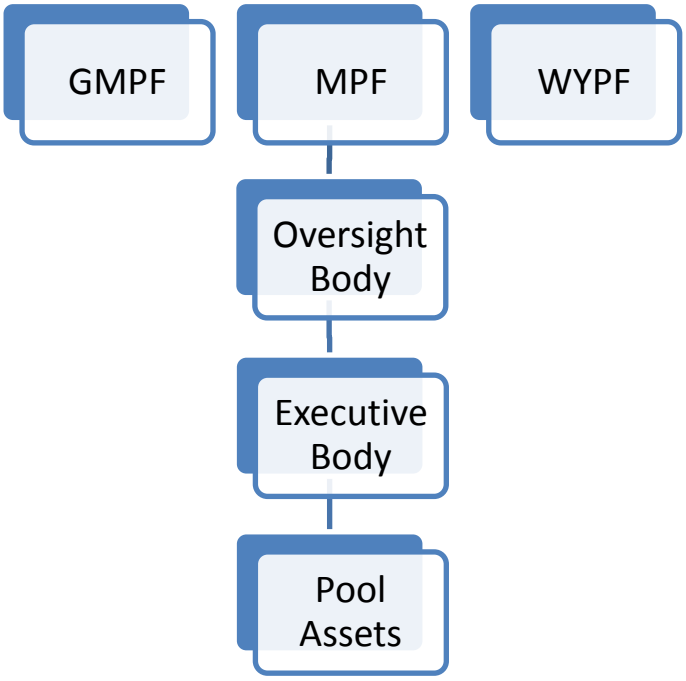
4. Structure and Governance

4.1 Overview

4.1.1 The proposed governance structure for the Pool is an oversight board, consisting primarily of representatives of the participating funds' pension committees, which will define key strategic objectives and provide scrutiny to an executive body of officers who will make the investment management decisions. Both the oversight board and the executive body will work closely with independent advisors.

4.1.2 This structure is designed to maintain democratic accountability for the investment outcomes of each of the participating funds, whilst ensuring all investment decisions are made by individuals with appropriate knowledge and experience.

4.1.3 The structure is set out in the diagram below.



4.2 Oversight body

4.2.1 Following consideration of all available options and obtaining external advice, it is proposed that the oversight body will be a joint committee, with equal representation from each participating fund.

4.2.2 The administering authorities have experience of joint committee working, for example in the creation of combined authorities in their respective regions and the devolution of health spending and have been impressed by the progress made in these areas.

4.2.3 The flexibility of the joint committee approach will allow speedy implementation of the Pools' investment objectives, such as further investment into infrastructure and will allow collaboration with other pools or national initiatives.

4.2.4 The relative simplicity and familiarity with the joint committee approach will enable focus on the areas of pooled working which can deliver material financial benefits, primarily the management of alternative/illiquid assets.

4.3 Executive body and choice of operating model

4.3.1 This body will make the decisions on manager selection and the legal vehicles and structures in which to implement funds' asset allocation decisions. Between February and July further work will be undertaken to determine the most appropriate form for the executive body.

4.3.2. As evidenced in section 2 of this submission, due to the existing scale and simplicity of management arrangements, the funds in the Pool already deliver low-cost management of listed securities either via internal management or via large external mandates (WYPF manages approximately £9bn of listed securities internally and GMPF's largest external mandate is c£6bn – these mandates are significantly larger than any other LGPS pool will realistically achieve in the short to medium term).

4.3.3 Long term performance has also been strong, with all 3 funds being in the top quartile of LGPS funds in terms of performance over 20 years. This is on a gross of fees basis. On a net of fees basis the outperformance will be stronger still.

4.3.4 This impressive track record highlights both the existing expertise and robustness of governance within the Funds.

4.3.5 Whilst there may be some scope via pooling to reduce these costs further and potentially harness an additional governance dividend, it is expected that the biggest benefits from pooling for the Funds will be in the management of alternative/illiquid assets such as property, private equity and infrastructure (including local investments) and the ability to increase allocations to these asset classes via further developing capacity and capability. All 3 funds have significant experience of investing in these asset classes on a direct basis and are well placed to move quickly in developing their collaborative approach, which will best be facilitated by a simple joint-committee structure.

4.3.6 Based on the Funds' knowledge and experience, the conclusions of Project Pool and the professional advice received (see appendices B and C to this submission), our understanding is that alternative/illiquid assets can be held more effectively outside of an Authorised Contractual Scheme ('ACS') structure (for example via limited partnerships), primarily due to their illiquid nature.

4.3.7 The Funds also have experience of creating appropriate legal structures for specific investments – for example GMPF's Matrix Homes project – building 240 homes for sale and rent, was managed via a limited partnership structure.

4.3.8 Using limited partnerships provides 'legal pooling' – for example the GLIL infrastructure partnership between GMPF and LPFA discussed in more detail later in this submission is an entity in its own right rather than a wrapper for two underlying LGPS funds (and is viewed in the market as such).

4.3.9 These limited partnerships would be managed by the Exec Body of the Pool and investors would have day-to-day involvement in their management.

4.3.10 The most appropriate operating model for the management of the Pool's listed securities is less clear. The main options being considered are:

a) An Authorised Contractual Scheme ('ACS');
b) The creation of a FCA Authorised Asset Management Company which would be owned by the Funds;
c) Developing a formal 'shared-service' arrangement which enables the legal ownership of funds' assets to remain unchanged, but still harnesses the benefits of the pooled approach. This could include one of the participating funds obtaining FCA Authorisation to act as an asset manager (similar to the South Yorkshire Pension Fund's authorisation to manage the assets of the South Yorkshire Passenger Transport Fund).

4.3.11 Regardless of which operating model is ultimately chosen, the governance and investment decision making will be comparable to a FCA regulated vehicle. Further detail on the Pool's decision making arrangements is provided in section 4.6 below.

4.4 Authorised Contractual Scheme ('ACS')

4.4.1 It appears that the ACS structure is favoured by some other LGPS pools, and has already been implemented by the London CIV. An ACS appears to be a good structure for consolidating relatively small external mandates to generate scale and material cost savings, but for the reasons set out above, this is not something that adds material value in this Pool.

4.4.2 The benefit of an ACS structure over the other models appears to be a preferential rate of taxation on equity dividends in some territories (principally France and Sweden), although the Funds' allocations to these markets are relatively low and there is no certainty that this preferential tax treatment will continue to exist. It is less tax efficient in emerging markets, a likely area of increased allocations, than other structures.

4.4.3 The analysis provided by PwC (see Appendix B) indicates additional costs in the set-up and transfer of assets into an ACS of approximately £13m.The ongoing costs of operating an ACS are broadly comparable to the alternatives, with the tax benefits referred to above offsetting higher operating costs.

4.4.4 From a practical perspective, the additional work and longer timescales required to implement an ACS structure could take focus away from areas where real value can

be added, primarily in the management of alternative/illiquid assets and in particular investing in infrastructure.

4.4.5 Our understanding is that there are also legal constraints which restrict the ability to hold ‘life insurance-wrapped’ passively managed securities in an ACS.

4.5 Advantages of alternative models to an ACS

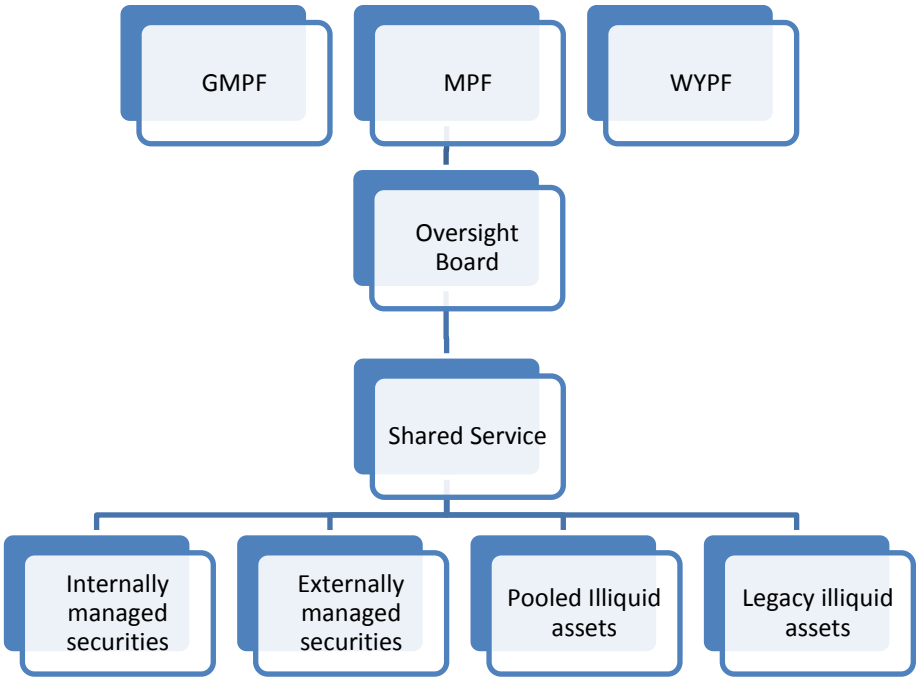
4.5.1 Any material scope for cost savings in the management of listed assets is likely to be obtained from managing a greater proportion of listed securities internally. Based on the legal advice received (attached as Appendix C to this submission) this may be achieved by creating formal ‘shared service’ arrangements between the Funds or by one or more of the funds in the pool seeking FCA authorisation as an asset manager (option c) in 4.3.10 above). Alternatively this could be achieved by establishing an asset management company owned by the participating administering authorities (option b) in 4.3.10 above).

4.5.2 An advantage of option c) is that resource will remain available to manage the diverse range of alternative/illiquid assets which will be retained by the participating funds, in the short to medium term, to avoid exit penalties and charges on change of ownership.

4.5.3 In addition, internal expertise would be retained to advise the Funds’ committees on asset allocation and help provide robust challenge to the external asset allocation advice which the committee receives. It is widely accepted that asset allocation is the primary factor in determining investment returns. Further detail on how this shared service structure may operate is provided in the section below. The Pool would welcome the opportunity to develop this further in conjunction with Government over the next few months

4.6 Shared Service Structure

4.6.1 The structure is set out in the diagram below



4.6.2 The shared service structure is used both to allocate to external managers and to manage assets directly. The key element of the structure is that the individual funds have investment mandates with the pooled/shared investment management service. These are drawn from existing arrangements, and rely on key tools of investment guidelines and a compliance manual. This structure will ensure standards that are consistent with an FCA regulated entity without losing the cost effectiveness and alignment of interests that this management structure provides.

4.6.3 The Funds have a long history of clear and controlled delegation to officers for investment management and this structure is an extension of this. The controls in place and quality of resources available are consistent with an FCA regime.

4.6.4 A role of the oversight board is to oversee the operations of the shared service in a similar manner to a scrutiny committee in local government. The board would ensure compliance of the shared service team with the investment guidelines and compliance manual.

4.6.5 Investment staff are retained in their current employment with their existing authority, but will work as part of a combined Pool investment team. The combined team would be managed using a matrix structure with a Chief Investment Officer ('CIO') for each fund responsible for the relationship with that fund and also leading on various areas of investment activity for the Pool.

4.6.6 The CIO group would be responsible for day to day management of the service and investment decision making, with key strategic decisions such as staffing budgets set by the oversight board.

4.6.7 For a transitional period, investment staff below CIO level would be allocated to specific asset classes and would work on the management of both new pooled investments, legacy illiquid assets and the reporting to the oversight board and the Funds' committees. This ensures the highest quality management across each

fund's entire asset base and also ensures an orderly transition of illiquid assets into the Pool. The table below shows an example illustration (not exhaustive) of the types of activity that would be allocated to CIOs. Specific individuals would also be allocated to compliance and risk roles in a similar manner to an FCA regulated entity. Over time, the location of the management of individual asset classes would evolve to centres of excellence as these emerge.

	CIO GMPF	CIO MPF	CIO WYPF
Internal equities			
External Equities			
Infrastructure			
Property			
Private Equity			
Compliance			
Accounting			
Risk			

4.6.8 In the shared service model, increasing the proportion of listed securities that are managed internally could be achieved by all funds appointing a common custodian who could undertake 'block-trading' of securities under instruction from the Pool Executive Body. How this arrangement meets with FCA requirements is covered in the legal advice attached as Appendix C to this submission. The move to a common custodian is also likely to generate a cost saving to the Pool.

4.7 Initial conclusions

4.7.1 The vehicle used to manage the listed securities of the Pool is unlikely to have a material impact on the Pool's performance. However, an ACS is not currently the Pool's preferred option due to:

i) the significant costs involved in its set-up, in particular the costs of transferring assets to the new vehicle;
ii) the relative ease of implementation of the alternative structures to an ACS is considered to allow greater focus on:
   a. the pooled management of alternative/illiquid investments. This is where material cost savings can be obtained;
   b. increasing investment in infrastructure.

4.7.2 Over the period up to the July submission, the Pool will explore available options in more detail and will welcome further discussion with Government in this area.

4.8 Timeline of implementation

4.8.1 As outlined in this document, one of the key aims of the Pool is simplicity. This allows the Pool to focus on driving cost savings whilst maintaining or improving performance and increasing investment in infrastructure.

4.8.2 The proposed time-table for implementation of the pooled arrangements is shown below

Pre Submission

19 Feb	Submission of initial document
Feb - April	Business Planning - Forming of groups of officers at all levels in investment teams to analyse existing arrangements (internal and external portfolios) and internal resources (staffing systems) against the requirements for the Pool
	Further discussion with Government
	MPF and WYPF to consider becoming partners in GLIL infrastructure vehicle and discussions to continue with other pools on using GLIL infrastructure vehicle
May	Consideration of draft Business Plan by the Funds
June	Finalisation of Business Plans and commissioning of any required external work/advice
15 July	Individual and joint submissions to Government

Post Submission Summary

2016	Establish the combined team and focus arrangements for collective investment in alternative/illiquid assets going forward. Existing fund assets remain in the ownership of existing funds at this stage.
	Progress discussions with other pools to work collaboratively in respect of certain asset classes.
2017	Review of Investment management arrangements in listedsecurities
	Combined, multi-site but with centres of excellence, investment team established.
2018	Pooling of management of listed securities focusing on simple, large scale and cost effective structures of internal and external management
Post 2018	Run off of remaining illiquid investments in alternatives retained by funds.

4.9 Management of Alternative/Illiquid assets

4.9.1 The experience in the Pool is potentially a national leader on collective investment in illiquid alternatives.

4.9.2 The Pool's approach to alternative/illiquid assets, will broadly follow the recommendations of Project POOL, which also reflects the Pool's approach to

infrastructure. The most significant allocations are currently in property, private equity and 'Special Opportunities' (including hedge funds).

4.9.2 Infrastructure investment is covered in detail in Section 6 of this submission as it is an important differentiator in our approach to pooling compared to other pools and an area where we believe we have built significant capacity and capability.

4.9.3 The Pool is seeking simplicity in its operating model in order to focus attention on the management of these asset classes as this is where the greatest cost savings are likely to be achieved (given the economies of scale that the Funds already have in listed securities).

4.9.4 The broad approach for the management of each asset class is as follows:

Property

Initially, 'virtual' pooling for existing holdings of direct (building) assets. A tender process will be undertaken across all existing mandates to try and achieve fee reductions through economies of scale. There will be no transfer of existing properties but a long-term approach of managing out the portfolios will be developed. The appointed manager would also run a new pooled portfolio alongside the existing portfolios where new purchases would be made, this could be via a Limited Liabilty Partnership ('LLP') structure. (See Project POOL report for further detail).

Using the same manager across all the Pool's portfolios will ensure alignment of interests.

The expected approach to new investments would be to hold direct property, but in-direct investments may be required for efficient portfolio construction. The aims will be to reduce fees through economies of scale and improve investment performance over time through combining teams and strengthening processes.

Private Equity

Existing assets would remain in the individual funds' ownership, but would be monitored via the Pool investment team. New investments would be made collectively through a LLP structure The aims will be to reduce fees through economies of scale (larger commitments and ability to co-invest) and improve investment performance over through combining teams and strengthening process.

Special Opportunities

Special Opportunities covers a variety of investments that do not naturally fit within mainstream fund assets. It could for example reflect short-term opportunities where there have been market dislocations and/or there are early mover advantages. Such investments are primarily asset allocation decisions and thus individual funds decide the allocation.

Existing assets would remain in the individual funds' ownership. New investments may be made collectively through an LLP structure. The aims would be to reduce fees through economies of scale with bigger mandates to external investment

managers. The breadth and expertise in the pool may result in more suitable opportunities being identified.

Local Investments

Local investments generally have twin aims of generating commercial returns and supporting the local economy. Examples include GMPF's residential housing developments and social impact investments. Investments are typically made via limited partnerships.

The expectation is that these investments would continue to be held by the individual fund, but management would be undertaken by the Pool as a whole to develop resources and experience in this area.

5. Costs and Savings

5.1 Background

5.1.1 The Funds believe that control of costs is important from the perspective of maximising risk adjusted returns. This applies to both:

(i) The costs of administering the pool investments;

(ii) The underlying investment management costs.

5.1.2 This concept does not always mean the absolute minimisation of costs; for example, certain investment classes, such as private equity and infrastructure, have higher cost than others, such as bonds, but are expected to deliver higher returns. Active investment management has a higher cost than passive but should deliver additional returns. Portfolio construction requires a balance of assets and management approach to control risk, returns and costs to meet the ultimate objective.

5.1.3 Due to the scale of the participating funds and the simplicity of arrangements, this pool will likely have the lowest costs of any of the LGPS Pools at the outset. Given this, the scope for father savings, particularly in management of liquid securities is limited and there will be a focus on saving costs in alternative assets.

5.2 2012/13 Data and comparison to present

5.2.1 The Pool is currently working on calculating 2012/13 investment costs on a consistent basis, including transaction costs and the cost of some underlying investment vehicles. This is important for targeting savings from alternative assets and will be included in the July submission in detail

5.2.2 The table below shows a comparison of the costs of the Funds on a % of Assets Under Management ('AUM') basis from 2012/13 to 2014/15 and the national average.

	GMPF	MPF	WYPF	Combined Pool	National Average
2012/13	0.092%	0.209%	0.019%	0.090%	0.229%
2014/15	0.076%	0.197%	0.026%	0.083%	0.349%

5.3 Alternative/illiquid assets

5.3.1 The pool believes that significant savings can be made in the management of alternative/illiquid assets by using improved in-house capability and the skills of the Pool to undertake more co-investment and direct investment. However we are still working on how to measure costs on a consistent basis for a current base line. The Pool is also continuing to work on how it will manage alternatives in the future and therefore accurate calculation of projected savings is not possible at this stage.

5.3.2 Based on GMPF's current investment of £2bn in these assets, a conservative estimate of the potential saving is £7m per annum. However, the current investments strategy that is in the process of being implemented over the next 3 to 4 years

envisages a doubling of investment to these areas and on a like-for-like basis this would yield savings estimated at £17m per annum, again evaluated on a reasonably prudent basis. The equivalent figures for WYPF are £6m and £8m.

5.3.3 Assuming a proportionately similar cost saving for MPF it is therefore envisaged that savings of around £30m per annum could be achieved via the pooled management of alternative/illiquid assets.

6. Infrastructure

6.1 Background

6.1.1 The Funds note the Government's criteria relating to infrastructure. Funds are asked to state in their response the following:

- The proportion of their fund currently allocated to infrastructure, both directly and through funds, or "fund of funds".
- How they might develop or acquire the capacity and capability to assess infrastructure projects, and reduce costs by managing any subsequent investments directly through the pool(s), rather than existing fund, or "fund of funds" arrangements.
- The proportion of their fund they intend to invest in infrastructure, and their ambition in this area going forward, as well as how they have arrived at that amount.

6.1.2 This section sets out how the criteria will be met by the Pool, referring to Project POOL and other collaboration.

6.2 Current Position

6.2.1 The current position of each Fund is set out below.

		GMPF	MPF	WYPF	**Total**
Direct	Allocated	1.5% £250m			**0.7% £250m**
	Committed	0.4% £60m	0.5% £30m		**0.3% £90m**
	At Work	0.1% £17m	0.2% £15m		**0.1% £32m**
Funds	Allocated	4% £680m		3.0% £325m	**3.0% £1,005m**
	Committed	2.8% £469m	4.2% £272m	3.3% £366m	**3.0% £1,107m**
	At Work	1.3% £224m	3.4% £220m	2.4% £271m	**2.0% £716m**
Total	Allocated	5.5% £930m		3.0% £325m	**3.5% £1,255m**
	Committed	3.1% £529m	4.7% £302m	3.3% £366m	**3.3% £1,197m`**
	At Work	1.7% £241m	3.6% £235m	2.4% £271m	**2.2% £747m**

`% are of whole Fund as at 31 December 2015

6.3 Developing capacity and capability in infrastructure

6.3.1 The Funds all made active contributions to Project POOL and are in broad agreement with the key conclusions of the infrastructure section of the report, including:

- Infrastructure assets that are most attractive to pension funds are established infrastructure projects delivering steady income streams that rise with price inflation (since LGPS pension payments increase with inflation). There will also be demand for some higher risk-return assets as reflected in existing portfolios held by the funds in the pool.
- Improved access and lower cost is most likely to be achieved through a national platform accessible to all the LGPS asset pools.
- Further work is required to determine how the national platform should be established and whether it builds on or runs alongside any existing arrangements. Government can assist the investment in infrastructure by ensuring that there is a pipeline of projects that are suitable for investment by the LGPS.
- The creation of an LGPS infrastructure 'Clearing House' will enable a meaningful dialogue with Government in the period leading up to the formal inception of the pools. The Clearing House could source, undertake due diligence and aggregate investment opportunities in the interim period.

6.3.2 This Pool envisages that in addition to commitments to the national pool, there would be some investment by LGPS pools alongside the national pool, either as co-investment opportunities or separately, where appropriate due to location, scale, local knowledge, existing relationships or other factors, but with the national pool providing a clear lead.

6.3.3 Ahead of the pooling agenda, GMPF, which has a long track record of investing in infrastructure funds, has developed capacity to invest in direct infrastructure opportunities through its joint venture with the London Pension Fund Authority ('LPFA'). This vehicle is currently known as GLIL but is due to be renamed. Both funds have committed £250m each to make investments up to £150m. The first investment has been made and due-diligence is being concluded on a number of other opportunities.

6.3.4 This vehicle has been designed to be extended to accommodate other funds and could form part of the national solution. The intention of the Pool and its existing collaborative partners is to promote the concept of an LGPS owned entity with both direct investment capacity and to facilitate the clearing house concept. It is felt that GLIL could form part of the foundations of this.

6.3.5 At present the collaborative partners include LPFA directly; this would quickly be extended to include WYPF and MPF. In addition the "Borders to Coast" Pool has expressed an interest in working with us and has agreed the key features set out below. Much more work is needed on governance structures and it is intended to be very much a collaborative approach with all of the LGPS. If the number of parties investing in GLIL became such that it is impractical for all parties to be actively involved in the decision making process then the vehicle will seek the appropriate level of FCA authorisation.

6.3.6 The key features of this proposal as an investment vehicle and 'clearing house' are:

<u>GLIL Vehicle</u>

- A clear governance structure with decision making devolved from funds' pension committees to officers with a clear investment mandate including risk and return parameters and allowable investment types.
- All contributing pools participating in decision making.
- A number of sub funds targeting assets on the basis of direct or indirect risk/return targets and UK/overseas.
- An appropriately resourced internal transaction team to appraise opportunities
- Use of external resources as appropriate using economies of scale to reduce costs.

Clearing House

This could have the ability to speak for the LGPS as a whole within pre-agreed parameters. The general concept is to avoid loss of value through LGPS pools competing against each other for infrastructure deals. It would then perform roles including:

- Identifying infrastructure projects suitable for direct investment by LGPS pools;
- Performing initial due diligence and present the projects to LGPS pools;
- Gather together the necessary funding commitments from LGPS pools;
- Complete the full due diligence process and act as agents for LGPS pools in the investment.

6.3.7 To provide capacity and capability in a cost effective manner the Clearing House could be supported by the GLIL vehicle in terms of resourcing with costs recovered through a mechanism of charging for investments made.

6.3.8 The Northern Powerhouse Pool specifically would look to support this proposal and the other partners would look to commit both capital and further internal management resources as soon as possible. One of the key strengths of the Pool is its internal management capacity and this is demonstrated in this proposed solution to the infrastructure criteria.

6.4 Future allocation

6.4.1 The Funds are open to further investment in infrastructure and will look to achieve an allocation of 10% of fund value in the medium term subject to identification of investment opportunities that meet the required risk adjusted returns to meet their liabilities. The additional investments would be made via the GLIL vehicle directly and then the Clearing House when available.