

**City of Westminster Pension Fund**  
Strategy Consideration

June 2019

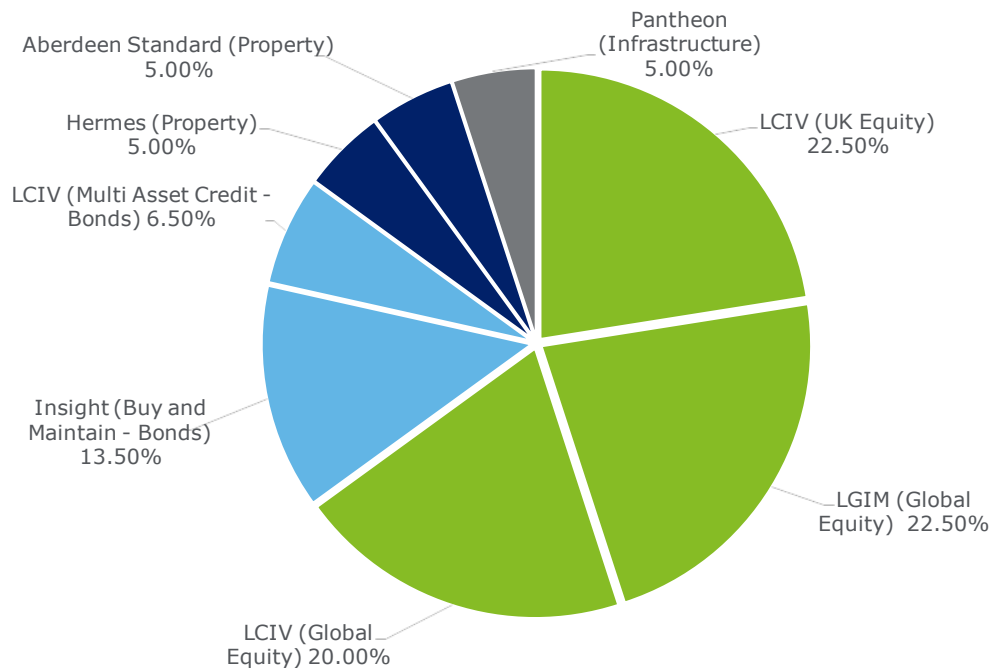
## Introduction

This report has been prepared for the City of Westminster Pension Fund Committee (“the Committee”) and is a discussion piece on the future investment strategy of the City of Westminster Pension Fund (“the Fund”). The Fund is due to receive £170m through a forward funding agreement, which should bring the funding position to a surplus. The Fund is also currently part through its triennial actuarial valuation. Both of which should be taken into consideration by the Committee when considering strategy changes as well as the more immediate issue of where to invest additional funds as and when they are received.

## Current Investment Strategy

### Current strategic asset allocation

As at 31 March 2019, the Fund’s investment strategy contains an asset mix of equities, bonds, property and infrastructure. The Fund invests in seven strategies with the strategic asset allocation of equities 65%, fixed income 20%, property 10% and infrastructure 5%, as shown below.



The table below shows the current asset allocation (as at 31 March 2019) as well as the strategic benchmark asset allocation of the Fund.

| Asset Class    | Current Asset Allocation (%) | Benchmark Allocation (%) |
|----------------|------------------------------|--------------------------|
| UK Equity      | 20.8                         | 22.5                     |
| Global Equity  | 48.3                         | 42.5                     |
| Fixed Income   | 20.7                         | 20.0                     |
| Property       | 9.3                          | 10.0                     |
| Infrastructure | 1.0                          | 5.0                      |
| <b>Total</b>   | <b>100.0</b>                 | <b>100.0</b>             |

Figures may not sum due to rounding

During the first quarter of 2019, the Fund committed \$91.5m to the Pantheon Global Infrastructure III. As can be seen from the table above, the Fund has a 1.0% allocation to infrastructure as at 31 March 2019, however this allocation will reach 5% as the Pantheon Fund draws down the allocation over the coming years.

Based on the current strategic allocation of the Fund we estimate the median return would be 5.4% p.a. with a standard deviation of 12.0% p.a.

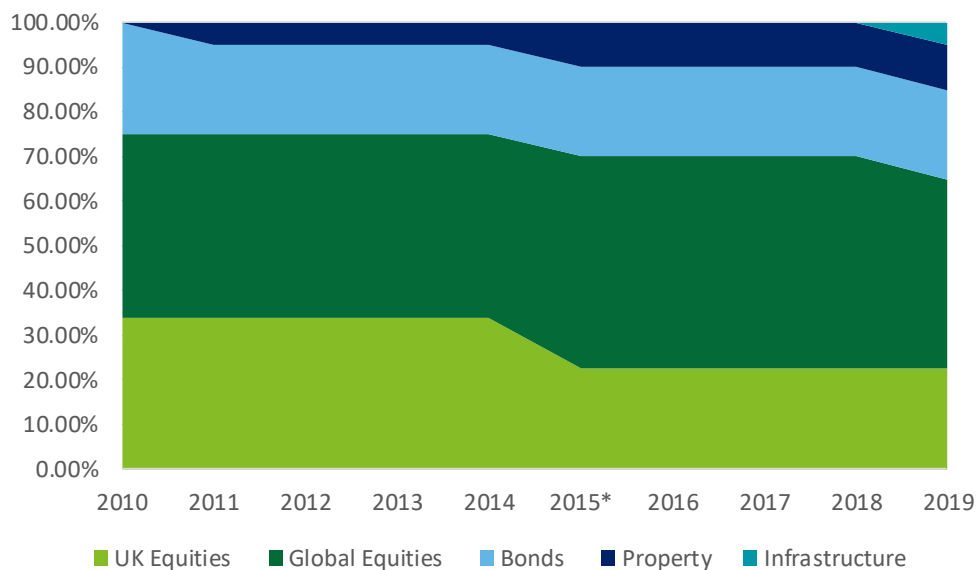
### Historic Investment Strategy

#### Historic strategic asset allocation

The strategic asset allocation of the Fund has evolved over time to reflect its risk and return requirements. Historically the Fund has had a high allocation to return seeking assets, most notably equities and property. This strategic allocation gives the Fund a larger return potential; however, the Fund also bears a higher amount of risk as a result. Overall since the first quarter of 2010 the Fund’s strategic allocation to equity has fallen, with bond allocation remaining the same. Property and Infrastructure allocations have increased as they have been implemented to add diversification investment strategy.

| Asset Class           | Strategic asset allocation (% as at 31 March of year) |      |      |      |      |                   |      |      |      |      |
|-----------------------|---|------|------|------|------|-------------------|------|------|------|------|
|                       | 2010  | 2011 | 2012 | 2013 | 2014 | 2015 <sup>1</sup> | 2016 | 2017 | 2018 | 2019 |
| <b>UK Equity</b>      | 33.8  | 33.8 | 33.8 | 33.8 | 33.8 | 22.5              | 22.5 | 22.5 | 22.5 | 22.5 |
| <b>Global Equity</b>  | 41.2  | 41.2 | 41.2 | 41.2 | 41.2 | 47.5              | 47.5 | 47.5 | 47.5 | 42.5 |
| <b>Fixed Income</b>   | 25.0  | 20.0 | 20.0 | 20.0 | 20.0 | 20.0              | 20.0 | 20.0 | 20.0 | 20.0 |
| <b>Property</b>       | -   | 5.0  | 5.0  | 5.0  | 5.0  | 10.0              | 10.0 | 10.0 | 10.0 | 10.0 |
| <b>Infrastructure</b> | -   | -    | -    | -    | -    | -                 | -    | -    | -    | 5.0  |

<sup>1</sup>During the first quarter of 2015, the Fund underwent a strategy review in which 5.0% of the allocation was to be invested in either a property or infrastructure. This was later invested back into equity.



### Thoughts and observations

#### Future strategy considerations

The Fund’s last funding valuation was at 31 March 2016, showing a funding level of 80%. On a basis consistent with the 2016 valuation, the Fund Actuary has estimated that the funding level as at 31 December 2018 is 95%, with a deficit of £79m.

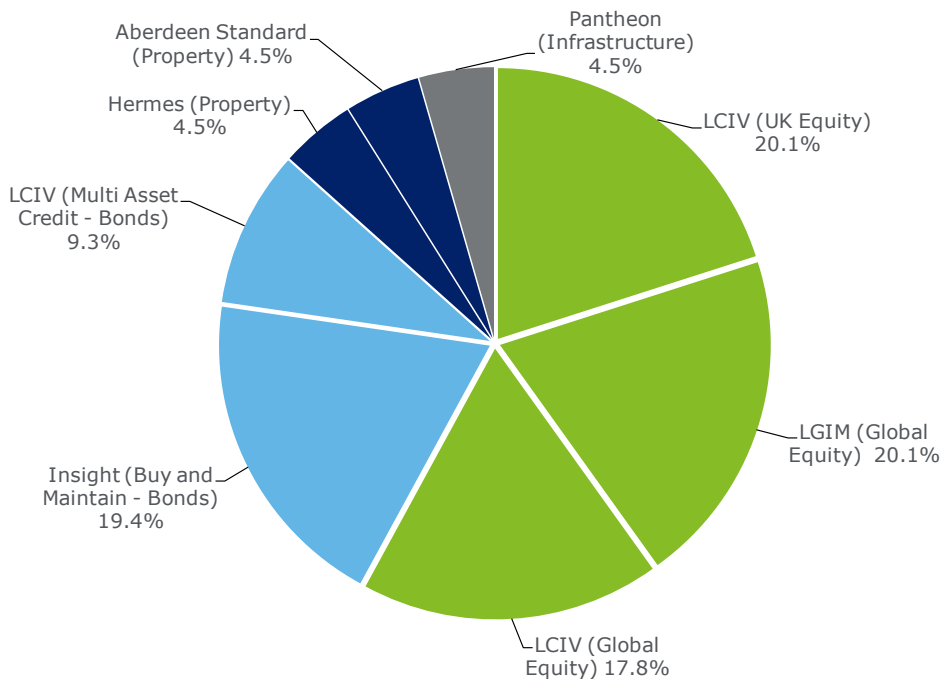
The Fund is expecting a £170m payment over the next 12 months (£20m in Q2 2019 and £150m in Q2 2020) through a forward funding agreement, which is expected to take the overall funding position into surplus. While the investment strategy should be considered more thoroughly following the final actuarial valuation, the Committee must also consider where to allocate these funds as and when they are received. We have outlined some options below for consideration and discussion at the next Pension Fund Committee Meeting.

1. Use the funds to invest across the current strategic asset allocation.

The Fund is currently running a lot of equity risk, which would not be appropriate for a funding position of above or near 100%. There would also be significant transaction costs of investing across all asset classes as well as a delay to getting money invested (c. 6-12 months for property and c. 24 – 36 months for infrastructure).

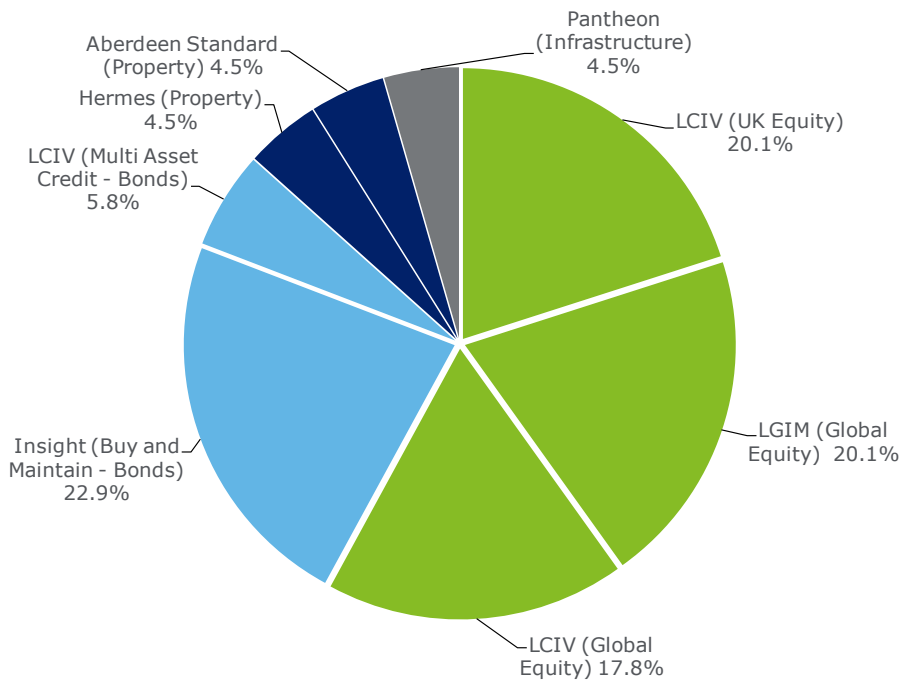
2. De-risk the Fund by investing in fixed income.

Both the buy and maintain credit and multi-asset credit strategies are relatively liquid and could take additional investments. If the Fund were to invest the forward funding capital into fixed income in the same split as is currently in place (two-thirds buy and maintain and one third multi-asset credit), we estimate the resulting portfolio would have an expected return of 5.2% p.a. with a standard deviation of 11.3% p.a. The overall allocation as a result of this is shown in the pie chart below.



3. De-risk the Fund further by invest in buy and maintain credit only.

The Fund's buy and maintain credit carries the lowest expected risk (and return), investing in investment grade liquid credit only with the aim of holding securities until maturity. The expected yield is 1%-1.5% above that of UK government bonds. If the Fund were to invest the forward funding capital into buy and maintain credit only, we estimate the resulting portfolio would have an expected return of 5.1% p.a., with a standard deviation of 11.1%. The overall allocation as a result of this is shown in the pie chart below.



**Estimated Asset Allocation**

| Asset class    | Current strategic asset allocation (%) | Estimated asset allocation following de-risking (%) |
|----------------|--|---|
| UK Equity      | 22.5                                   | 20.1  |
| Global Equity  | 42.5                                   | 37.9  |
| Fixed Income   | 20.0                                   | 28.7  |
| Property       | 10.0                                   | 8.9   |
| Infrastructure | 5.0                                    | 4.5   |
| <b>Total</b>   | <b>100.0</b>                           | <b>100.0</b>  |

**Conclusion**

The Fund’s current allocation to equity is high, and although investing the forward funding capital in fixed income will reduce the equity allocation (to c. 60%), there may still be scope to reduce this further.

If the Fund were to reduce the equity allocation and invest this as well as all of the forward funding capital in buy and maintain credit, this may reduce the expected return by too great an extent.

The Committee may wish to consider other fixed income asset classes that still achieve the desired de-risking of the overall strategy while also delivering a level of return, and importantly income, required by the Fund. Asset classes such as private debt/illiquid credit are areas which may be worth considering.



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