AGENDA ITEM 11i

THE HIGHLAND COUNCIL

Minutes of Meeting of the **Investment Sub Committee** held remotely on Friday 17 September, 2021 at 10.30 a.m.

PRESENT

Mr R Bremner
Mrs H Carmichael
Mr R Gale
Mr B Lobban
Mr D Louden
Mr P Saggers
Mr B Thompson

Non Member in attendance

Ms P Hadley

Officials in attendance:-

Mr E Foster, Head of Corporate Finance and Commercialism, Resources & Finance Service
Mrs M Grigor, Finance Manager (Corporate Budgeting, Treasury and Taxation), Resources & Finance Service
Ms C Stachan, Accountant, Resources & Finance Service
Mr D Haas, Inverness City Area Manager, Communities and Places Service
Mr A MacInnes, Administrative Assistant, Performance & Governance Service

Also in attendance :-

Mr K Ettles, AON, Investment Principal and Actuary
Mr R Fea, Pension Board observer
Mr D Bloch , Mr C Fowler , Mr N Broadhead, Mr A Davies, representatives of CVC (Item 8 only)

Mr B Thompson in the Chair

1. Apologies for Absence

Apologies for absence were intimated on behalf Mr C Nicolson, Mr E Macniven and Mr J Gibson, Pension Board observer.

2. Declarations of Interest

There were no declarations of interest.

3. Minutes of Last Meeting

There had been circulated minutes of the meeting of the Sub Committee held on 11 June, 2021 the terms of which were **APPROVED**.

4. Exclusion of the Public

The Sub-Committee **RESOLVED** that, under Section 50A(4) of the Local Government (Scotland) Act 1973, the public be excluded from the meeting for the following items on the grounds that they involved the likely disclosure of exempt information as defined in Paragraph 6 of Part I of Schedule 7A of the Act.

In terms of Standing Order 9, the Sub Committee **AGREED** to alter the running order of the remainder of the agenda to facilitate CVC Credit Partners attendance at the meeting. The running order was as follows:- Items 5a, 7, 8, 5b, 6.

5. Investment Activity Update and Performance Report

(a) There had been circulated to Members only Report No INV/10/21 by the Head of Corporate Finance and Commercialism detailing Pension Fund investment matters for the quarter to 30 June, 2021 and any significant events since that date.

Attention was drawn to capital advances to the Funds private equity investment; training opportunities available to Members; investment strategy review including confirmation that the sub committee had appointed Robeco to manage the Fund's multi-asset credit mandate and Kohlberg Kravis Roberts to manage the Fund's Infrastructure mandate. In terms of the appointment of a Private Credit Manager, this would be considered as a separate item at the meeting (item 8). A Property Debt Manager appointment would be considered at a future meeting. The transition of the Baillie Gifford Global Alpha equities being invested to the Baillie Gifford Global Alpha Aligned fund was highlighted.

In relation the Sub Committee's decision to disinvest from the Pyford holding, it was explained that a decision on where this disinvestment should be invested was still to be made and this would be considered at item 7 of the meeting, equity strategy implementation. Thereafter, a new equity manager would require to be appointed.

The recent Responsible Investing workshop held for members of the Pensions Committee and Pension Board was commended and thanks for this were extended to AON for arranging this.

The Sub Committee **NOTED** the report.

(b) There had been circulated to Members only report No. INV/1/21 by the Fund's Investment Advisor setting out Pension Fund investment performance for the quarter ended 30 June, 2021.

The report was summarised, with a return of 4.6% for Quarter 2, underperforming the benchmark by 0.3%. Equities, corporate bonds and property all performed extremely well on the back of improved economic data, increased global Covid-19 vaccinations and increased estimates for global growth forecasts. Longer term performance remained strong. Other issues covered included the market summary for the quarter to 30 June, 2021, strategic asset allocation, fund asset allocation, fund performance against benchmarks, and the performance of individual fund managers.

Members commented on the prospects of future commercial property returns given that businesses may continue to allow their employees to work from home and therefore there may be a surplus of commercial properties on the market. It was explained that there were changes in the property sector at present with a slowdown in demand for commercial office accommodation and some sectors doing extremely well such as industrial units. The view from property managers on commercial office accommodation was that this sector would still offer respectable returns as while more employees were working from home, businesses still needed a Hub office for employees to work in. Also, some of these properties were being developed into other types of property, so the property market would continue to evolve.

The Sub-Committee **NOTED** the report.

6. Inverness Common Good and Associated Funds Investment Report

There had been circulated to Members only Report No. INV/12/21 by the Investment Advisor, which set out Common Good and Associated Funds investment performance for the quarter ended 30 June, 2021.

The report was summarised, with a key point being that all the Funds had delivered positive absolute performance in this quarter and outperformed their respective benchmarks. Over the longer term (3 and 5 year periods), all of the Funds that had been in place that long, had outperformed their benchmarks and delivered excess returns.

The Sub-Committee **NOTED** the report.

7. Equity Strategy Implementation

There was circulated to Members only Report No. INV/13/21 by the Investment Advisor with recommendations for the equity strategy implementation.

By way of background, the Sub Committee at its meeting in March, 2021 considered recommendations for the future composition of the Fund's equity portfolio. The Sub Committee approved the recommendations, with the exception that it was decided not to reduce the allocation to the Baillie Gifford global equities and decided to retain the allocation at its current level. Officers were asked to provide further advice on the future composition of the equity portfolio and the advice was set out in the report by the Investment Advisor and concluded with a summary of options and a recommendation.

In discussion, it was highlighted that the recommendation was that the Fund's equity allocation is fully invested in global equities, 50% managed by Baillie Gifford in the Global Alpha Paris Accord fund and 50% managed by a mixture of a new global fund manager (active manager) and Legal and General (passive manager) (20%/30% spilt) and the latter would both take account of the responsible investing process being taken into account at present.

It was queried why it was proposed to divest in Baillie Gifford UK equities at a time when most investment commentators were saying that the UK offered good value compared to other markets across the world. It was explained that the aim was to have an equity strategy that would serve the fund well in the long term. Given the more mature nature of the UK equity market, its longer term prospects were less attractive than the opportunities available on a global basis. It was also highlighted that Baillie Gifford could still invest in some UK equities as part of their global investments should they feel that was the most attractive market. The upper limit of investments Baillie Gifford could make in UK equities as part of their global investments would be checked and information provided to Cllr Thompson.

A significant move from active funds to passive funds was being proposed and a view was expressed that preference was for a new global equity manager to be an active manager to give a greater chance of outperformance. However it was advised that it was not just about outperformance of markets, but underperformance had to be considered as well and moving funds into passive investments would mean less risk and as the Fund was so well funded at present, it would be prudent to take less risk now.

It was clarified that the Sub Committee did not have to take a decision at this meeting on the 50% of global equities managed by a mixture of a new global fund manager and Legal and General. This could be made at the next meeting when a new manager was recommended. It was proposed that for the next meeting more information be submitted on passive and active management.

Members were comfortable on what was proposed on Baillie Gifford in respect of maintaining 50% of the equities allocation with them in the Global Alpha market. Members were also content that a new responsible investment manager is identified. Members were keen to have an element of passive management and keen to understand how to incorporate responsible investing into that.

Thereafter, the Sub-Committee **AGREED:-**

i to reduce the allocation to Baillie Gifford UK equities from 15% to nil and increase the allocation to the Baillie Gifford global equities to 50% so that overall Baillie Gifford still manage 50% of the Fund's future equity assets.

ii to identify and recommend a new responsible investment manager; and

iii Officers recommend a split between the new responsible investment manager and the passive equity manger, Legal and General.

At this point, the meeting was adjourned for a short comfort break and the *meeting resumed at 11.40 a.m.*

8. Investment Strategy

Andrew Davies, Neale Broadhead, Chris Fowler and Daniel Bloch representatives of CVC Credit Partners were in attendance to give a presentation on their European Direct Lending Responsible investment strategy. In this connection, there was circulated to Members only the Presentation slides.

It was recommended that CVC was appointed to manage the Fund's Private Credit mandate (5% of Fund's portfolio).

In summary, CVC provided loans to medium sized businesses across Europe in exchange for fees and annual interest payments and the capital was repaid at the end of the loan. There was significant analysis and due diligence of companies undertaken before loans were made. The CVC team explained how they went about the due diligence and manage risks and shared their experience of managing previous loans. CVC was a very experienced manager with a good track record in managing this type of asset class. Responsible investing was embedded in the investment process.

In discussion, it was highlighted that the managers did not do CVC private equity transactions within their private credit direct lending business and therefore this negated any potential conflict of interest. In terms of environmental, social and corporate governance factors, the managers worked closely with companies in terms of what actions they were taking to offset their carbon emissions. CVC worked closely with companies to provide loans for acquisitions and would continue to support them to help them grow their businesses and continually monitored the companies. It was highlighted that inflationary pressures would impact on companies, but the businesses supported by CVC were very resilient to inflation as their services would always be needed such as businesses in education, health, IT sectors.

The Chair on behalf of the Sub Committee, thanked the CVC representatives for their presentation.

Following consideration, the Sub-Committee **AGREED** that CVC Credit Partners be appointed to manage the Fund's Private Credit mandate (5% of the Fund's portfolio).

The meeting ended at 12.45 pm