

OXFORDSHIRE LOCAL PENSION BOARD – 9 JULY 2021

INVESTMENT MANAGEMENT COSTS AND PERFORMANCE

Report by the Director Finance

Recommendation

- 1. The Board are invited to discuss the contents of this report and consider what advice, if any, to send to the Pension Fund Committee.**

Introduction

2. This is the fourth in a series of reports considered by this Board in respect of the costs and performance of the investment management portfolios run on behalf of the Pension Fund Committee. The previous reports have all looked at annual performance in the years ending March 2018, 2019 and 2020 respectively.
3. One of the concerns expressed by Officers in drafting these previous reports is that a single year's data on investment performance is too short a period. The majority of fees paid are on a fixed rate basis and vary in line with overall asset values rather than performance. In any one year therefore comparison of fees paid to performance against benchmark will be impacted by the position in the investment cycle with results likely to imply different conclusions for value and growth managers for example. This report therefore looks at fees paid and investment performance over a 3-year period.
4. In previous reports Officers have also stated their concerns that looking simply at fees and investment performance is too narrow a view of the overall performance of our fund managers and fails to take into account the wider objectives of the Committee's investment strategy. In particular, there is a requirement to ensure the overall investment strategy provides for a sufficiently diversified set of investments to mitigate risk. In recent years there is also much greater attention paid to the management of the environmental, social and governance risks within the investment portfolios which may not necessarily be reflected in short-term investment performance. Indeed, many of those companies best placed to manage the transition to a low carbon economy may suffer poorer investment performance in the short term as they fund the transition.

Data for the Period 1 April 2018 to 31 March 2021

5. Annex 1 shows the investment management fees paid against each of the portfolios for the last three financial years, alongside the investment performance for the respective portfolios.
6. A key issue in undertaking any analysis at the present time is immediately obvious from the Annex in that very few of the portfolios have a 3 year history

for the period, due to the transition of assets from the legacy fund managers to Brunel. It is therefore very difficult to draw any firm conclusions.

7. The transition to Brunel has also introduced another distortion to the figures in that we have gained greater transparency over the underlying costs in respect of some of the private market portfolios. As well as providing information on their own fees, Brunel have provided information in respect of the fees paid to the underlying fund managers in the property and private equity portfolios. These underlying fees were previously netted off against the performance figures returned by the legacy managers. The increase in property fees for 2020/21 will therefore be offset by increased out-performance in the investment performance figures for the portfolio.
8. The greater transparency accounts for the majority of the increase in overall level of fees from 30.1bps in 2018/19 to 37.8% in 2020/21. There is also an element explained by the higher fees paid to the legacy private equity managers in 2020/21 which are related directly to performance.
9. Over the 3-year period, the average level of fees is broadly in line with the performance above benchmark achieved by the fund managers. The performance report to the last meeting of the Pension Fund Committee indicates that over a 5 year period, fund managers have added considerable value relative to their fees (total outperformance of 0.8% per annum) although over 10 years, the figure drops to 0.2% per annum.
10. It should be noted that the Committee do not have the option of investing all the Funds assets into passive options of the current asset classes to achieve investment performance in line with the benchmark. Passive options exist for the equity and fixed income portfolios but not for the majority of the private markets. Fee avoidance would therefore involve involving the asset class itself and amending the Investment Strategy.
11. If we look at the asset classes in turn, we can make the following observations:
 - Equities account for about 57% of the total investments but only 33% of the total fees. The average fee cost of the equity portfolios is 23 bps. Due to the transitions to Brunel we do not have any 3 year performance figures, but all Brunel equity portfolios significantly exceeded their benchmarks in the last year, including the Global High Alpha portfolio which outperformed its benchmark by 10.9%, which equates to over £30m. Switching the whole equity investments to passive portfolios could save up to £3m but would potentially forego much greater investment returns.
 - Fixed income accounts for around 17% of the current portfolio and 12% of the total fees, with an average fee of 25bps. The 3 year performance of the portfolio managed by Legal and General shows out performance of 0.9% indicating annual investment out performance net of fees of £3.25m

- Property represents around 6% of the total assets, and accounts for 12% of the total fees. There is not a passive version of the property portfolios, so this would be an asset class we would need to reduce exposure to if we believed we were not getting value for money from the fees paid. The long-term figures for UBS before the property assets were transitioned to Brunel, indicated that investment performance was exceeding fees by around 15 bps per annum, over both 3 and 10 year periods.
- Private Equity involves the highest fee levels in the current portfolio, accounting for over 25% of total fees whilst representing just 8.5% of the total investments. However, this asset class has been one of the strongest performing asset classes within the Fund over a sustained period of time, with 10 year figures showing out-performance against the benchmark by 4.3% well in excess of the average fees paid.
- The Diversified Growth Fund accounts for around 5-6% of the total investments and total fees. Whilst over the most recent 3-year period the portfolio has performed below the benchmark, it has exceeded the benchmark over a 5-year period. The Committee have already determined to review the current allocation to the Diversified Growth Fund as part of their next review of the strategic asset allocation.
- The remaining portfolios (infrastructure, secured income and private debt) do not have a long enough track record to complete any meaningful analysis.

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Fund Manager	Fees as per 2018/19 Accounts	Fees as per 2019/20 Accounts	Fees as per 2020/21 Accounts	3 Year Performance
	£000	£000	£000	
Global Equities - Wellington	1,071	715		
Global High Alpha - Brunel		385	1,174	
Sustainable Equities - Brunel			469	
Emerging Markets - Brunel		166	435	
UK Equities - Brunel	307	850	818	
UK Equities - Baillie Gifford	643			
Passive Equities - LGIM	93			
UK Passive Equities - Brunel (\$)	11	29	41	
Developed World Passive Equities - Brunel (\$)				
Global Equities - UBS	881	863	429	
Total Equities	3,006	3,008	3,366	
Fixed Income - LGIM	1,106	1,197	1,273	0.9
Property - Bridges Fund Management	204	373	203)
Property - Partners Group	409	- 202	-95) -0.3
Property - UBS	252	245	65	
UK Property - Brunel			891	
International Property - Brunel			165	
Total Property	865	416	1,229	
Private Equity - Adams Street	765	805	1,393)
Private Equity - Epiris	144	141	280)
Private Equity - Longwall Ventures	178	178	146)
Private Equity - Partners Group	409	106	436) +6.0
Private Equity - Brunel		798	607	
Total Private Equity	1,496	2,028	2,862	
Infrastructure - Brunel		261	169	
Infrastructure - Partners Group	288	263	549	2.6
Total Infrastructure	288	524	718	

Secured Income - Brunel		52	41		
Diversified Growth Fund - Insight	571	602	597		-1.2
Total	7,332	7,827	10,086		0.3
Total Fees Relative to Average Asset Values (bps)	30.1	32.1	37.8		