

FALKIRK COUNCIL

Subject: PRIVATE EQUITY AND ALTERNATIVES UPDATE
 Meeting: PENSIONS COMMITTEE
 Date: 25 SEPTEMBER 2014
 Author: CHIEF FINANCE OFFICER

1. INTRODUCTION

- 1.1 This report updates the Committee on the progress and key events arising from each Manager's investment programme for the three months to 30 June 2014.
- 1.2 The Fund's private equity and alternatives programme is managed as follows:

SL Capital (Standard Life)	-	European Private Equity
Wilshire Associates	-	Global Private Equity
Grosvenor Capital	-	Global Infrastructure
M&G	-	Credit Markets
- 1.3 The Fund's strategic allocation to private equity and alternatives (excluding the allocation to the Baillie Gifford Diversified Growth Fund) is set at 10% of total fund assets. This is split 5% to private equity and 5% to infrastructure.
- 1.4 The attached schedule gives details of the current valuations and commitment levels.

2. SL CAPITAL PARTNERS

- 2.1 SL Capital is a subsidiary of Standard Life Investments, who in turn own 60% of the business. The remaining 40% is owned by 8 partners.
- 2.2 The Fund's overall commitment to SL Capital is **€102m (£82m)**, spread across four European Investment Funds – ESP 2004, ESP 2006, ESP 2008 and ESF 1 – all being fund of fund structures.
- 2.3 The second quarter of 2014 has seen the manager remain reasonably active. The Fund continues to benefit from its maturing investments in the 2004 and 2006 ESP funds, receiving **distributions of €2.1m** during the quarter. The Fund's strategy of investing in a range of vintages means these distributions have been complimented by **€1.4m of calls**, the majority of which relate to the ESP 2008 and ESF 1 funds, which are in the seed/growth stage of their investment lifecycles.
- 2.4 All funds, except ESF 1 outperformed the MSCI Europe Index of 2.2% for the quarter. Highlights included the Saga IPO, helping boost the value of the Acromas fund in ESP 2004 and rises in the value of various co-investments Freescale, HSS Hire and Solina.

- 2.5 In terms of market outlook, the manager remains optimistic about the northern part of the Eurozone, seeing a gradual increase in consumer spending and corporate earnings. Escalating tensions over the Ukraine, however, and the risk of further trade sanctions with Russia are reasons to be wary.
- 2.6 SL Capital have a pipeline of products available for investment, however as the Fund's current allocation to private equity is broadly in line with its strategic allocation, there is no pressing need to make a further commitment at this stage.

3. WILSHIRE ASSOCIATES

- 3.1 During the period from 2004, the Fund has made various commitments to Wilshire Associates covering several geographical areas as follows:

European Funds	-	<u>€10.9m</u>
US Funds	-	\$53.2m
Asian Funds	-	\$ 3.8m
Global (Fund IX)	-	<u>\$15.0m</u>
		<u>\$72.0m</u>
Total Commitment		<u>£52.0m</u>

- 3.2 In their quarterly update, Wilshire remain optimistic about the global macroeconomic backdrop but, echoing SL Capital, have concerns about rising geopolitical tensions.
- 3.3 During the quarter, **€767k was distributed** from the Euro funds while **€16k was called**. As one would expect, given the larger allocation to dollar funds, **\$2m was distributed** and **\$1.8m called**.
- 3.4 Investment activity has commenced in Wilshire Fund IX – the Falkirk Fund's most recent Wilshire commitment - with initial positions being taken in a US Buyout Fund, a European Buyout Fund and an Asia-Pacific Special Situations Fund.

4. GROSVENOR CAPITAL

- 4.1 The Fund's global infrastructure investments are made via an **\$80m commitment** to the Customised Infrastructure Strategies (CIS) Fund managed by the Grosvenor Capital Customised Fund Investment Group (CFIG). The Fund has funded over 75% of its commitments.
- 4.2 The CIS Fund seeks to generate attractive risk-adjusted returns by investing in a diversified range of infrastructure funds, co-investments and secondaries. These focus on brownfield and greenfield assets, encompassing a broad range of infrastructure markets.
- 4.3 Although no distributions were made during the quarter, healthy investment activity was evidenced by CFIG calling in **\$3.1m**. Total value to paid-in capital stands at 1.20. New commitments were made recently to InfraCapital Partners - a fund focusing on the energy, water and transportation utilities in Western Europe – and Project Metropolis, a portfolio of secondary US energy funds.
- 4.4 Grosvenor's investments to date mean that the Falkirk Fund's allocation to Infrastructure stands at 3% against a strategic allocation of 5%. This position should improve with the Falkirk Fund's arrangement to invest in UK infrastructure in conjunction with Lothian Pension Fund.

5. M&G UK COMPANIES FINANCING FUNDS

- 5.1 The M&G UK Companies Financing Funds provide the pension fund with exposure to UK credit markets. The Funds play a valuable economic role in providing debt financing to UK companies facing refinancing obstacles. The aim of the Funds is to create attractive levels of income for investors - LIBOR plus 3%-6% - with a low level of risk.
- 5.2 Falkirk's commitment to the M&G Funds is **£11.8m to Fund I** and **£10m to Fund II**. Fund I has been fully invested and Fund II is in the process of being drawn down.
- 5.3 For Fund 1, the portfolio consists of 8 loans with an average repayment period of 5.3 years and average credit rating of BB+. This includes loans of between £30m and £100m made to companies such as Hogg Robinson, Taylor Wimpey and Provident Financial.
- 5.4 For Fund II, the portfolio so far consists of 6 loans with an average repayment period of 6.3 years. Loans of between £10m and £45m have been made to companies including Caffè Nero and Hall & Woodhouse Ltd.
- 5.5 All loans continue to be paid in accordance with their covenants.

6. CONCLUSION

- 6.1 The investment experience of the Fund's private equity managers is generally optimistic, subject to concerns about rising tensions in Ukraine and the Middle East. The infrastructure and credit market managers continue to source deals at an acceptable pace.
- 6.2 The forthcoming review of the Fund's investment strategy will be an opportunity to consider the merits of private equity given the recent criticism of Fund of Fund structures by the Department of Communities and Local Government.

7. RECOMMENDATION

- 7.1 **The Committee is asked to note the progress of the Private Equity, Infrastructure and Credit Markets Programmes as at 30 June 2014.**

Chief Finance Officer

Date: 12 September 2014

Contact Officer: Alastair McGirr

LIST OF BACKGROUND PAPERS

NIL

Appendix A

Falkirk Council Pension Fund Alternative Markets Update - 30/06/2014

Exchange Rates	
\$	1.6687
€	1.2461

Alternative Assets Summary - Approx Sterling Value

Manager	Fund	Commitment £,000	Unfunded £,000	(a) Cost £,000	(b) Return of Cost £,000	(c) Distrbtn Gains £,000	(d) Market Value £,000	(b + c + d) Total Value £,000	Total Value to Paid in Cap.	Inception Rate of Return
Private Equity										
SL Capital Partners	European Strategic Partners 2004	24,075	2,782	21,293	7,344	5,945	12,875	26,163	1.23	6.0%
SL Capital Partners	European Strategic Partners 2006	24,075	3,220	20,855	5,419	1,696	17,064	24,179	1.16	3.0%
SL Capital Partners	European Strategic Partners 2008	21,668	8,972	12,696	1,091	108	12,900	14,100	1.11	0.4%
SL Capital Partners	European Smaller Funds I	12,038	9,601	2,437	-	-	2,049	2,049	0.84	N/A
SL Capital Partners Total		81,855	24,575	57,281	13,854	7,750	44,887	66,491		
Wilshire Associates	Fund VI - Europe	2,889	222	2,667	1,468	1,000	1,282	3,749	1.41	7.3%
Wilshire Associates	Fund VII - Europe	2,889	273	2,616	549	308	2,149	3,006	1.15	0.5%
Wilshire Associates	Fund VIII - Europe	2,969	706	2,263	566	327	2,032	2,925	1.29	33.2%
Wilshire Associates	Fund VI - US	8,390	492	7,898	2,773	2,593	5,643	11,010	1.39	4.9%
Wilshire Associates	Fund VII - US	6,892	439	6,453	1,797	1,572	5,360	8,730	1.35	4.7%
Wilshire Associates	Fund VIII - US	7,611	873	6,738	1,956	944	6,188	9,088	1.35	8.5%
Wilshire Associates	Fund VII - Asia	1,079	108	971	491	261	584	1,336	1.38	5.1%
Wilshire Associates	Fund VIII - Asia	1,199	706	493	143	35	481	659	1.34	-16.0%
Wilshire Associates	Opportunities Fund II-B	8,989	2,050	6,939	3,649	1,334	4,040	9,023	1.30	9.2%
Wilshire Associates	Fund IX	8,989	8,510	479	0	0	413	413		
Wilshire Associates Total		51,895	14,379	37,517	13,391	8,374	28,174	49,939		
Private Equity Total		133,750	38,953	94,798	27,245	16,124	73,061	116,430		
Infrastructure										
Credit Suisse/Grosvenor	Customised Infrastructure Strategies	47,942	11,662	36,279	3,496	1,919	37,951	43,366	1.20	5.0%
Infrastructure Total		47,942	11,662	36,279	3,496	1,919	37,951	43,366		
Credit Markets										
Prudential/M&G	UK Companies Financing Fund	11,835	0	11,835	4,747	0	8,727	13,474	1.14	4.4%
Prudential/M&G	UK Companies Financing Fund II	10,000	7,081	2,919	0	89	2,917	3,006	1.03	2.5%
Credit Market Total		21,835	7,081	14,754	4,747	89	11,644	16,480		
Total Alternative Fund Value		203,527	57,697	145,831	35,488	18,133	122,656	176,276		