

**FALKIRK COUNCIL**

**Subject: PRIVATE EQUITY AND ALTERNATIVES UPDATE**  
**Meeting: JOINT MEETING OF THE PENSIONS PANEL AND COMMITTEE**  
**Date: 12 MARCH 2015**  
**Author: CHIEF FINANCE OFFICER**

**1. INTRODUCTION**

- 1.1 This report updates the Panel and Committee on the progress and key events arising from each Manager's investment programme for the three months to 31 December 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
  - Hearthstone - Social and Affordable Housing
- 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 schedules give details of the current valuations and commitment levels in both the original currencies and converted to sterling.

**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 spread across four European Investment Funds – ESP 2004, ESP 2006, ESP 2008 and ESF 1 – all being fund of fund structures. The partnerships have been established for 14 years from the final close of each Fund.
- 2.3 In Q4, the 2006 and 2008 Funds comfortably outperformed the MSCI Europe Index of 0.8%, returning 2.6% and 3.0% respectively. The 2004 Fund declined by around 1%, whilst the ESF 1 Fund was largely unchanged. Total value to paid-in capital across the SL funds is around 1.2 and returns around 4%.

- 2.4 During the quarter nearly €7m was returned and €2m called. Returns were spread evenly across the 2004, 2006 and 2008 Funds with calls being made only to the 2008 Fund. There was no activity in the ESF 1 Fund. Highlights included increases in the value of the Sagard II Fund and in various co-investments including Basic Fit and the Harding Group. In the ESF 1 Fund, two new investments were made to Xenon Private Equity VI (a Primary Fund) and Herkules III (a Secondary Fund)..
- 2.5 The Manager considers that consumer spending and business output has weakened across the Eurozone, albeit with variations between northern and southern Europe.

### **3. WILSHIRE ASSOCIATES**

- 3.1 During the period from 2004, the Fund has made various commitments to Wilshire Associates as follows:
- |                |   |                |
|----------------|---|----------------|
| European Funds | - | <u>€10.9m</u>  |
| Dollar Funds   | - | <u>\$72.0m</u> |
- 3.2 In their quarterly update, Wilshire indicate that pricing in US private equity markets is historically high which should benefit exits from their maturing funds. They also highlight their philosophy of looking for quality managers who have a track record of investing in complicated markets and technologies, which, due to their complexity, may have been overlooked by the capital markets.
- 3.3 Q4 was relatively quiet for Wilshire with virtually no capital calls. Returns came mainly from the dollar funds and amounted around \$2m. Around 90% of the Euro denominated funds have been drawn-down, whilst only 75% of the Dollar denominated funds have been drawn-down. This reflects the fact that the most recent commitment of \$15m to Wilshire was to a dollar fund. Total value to paid in capital is between 1.3 and 1.4 for most Wilshire funds and returns in excess of 6 to 7%.
- 3.4 In terms of personnel, the business requires to be monitored in view of the recent departure of Kevin Nee, president of the Wilshire Private Markets business.

### **4. GROSVENOR CAPITAL**

- 4.1 The Fund's global infrastructure investments are made via a commitment of \$80m to the Customised Infrastructure Strategies (CIS) Fund managed by the Grosvenor Capital Customised Fund Investment Group (CFIG).
- 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. Recent purchases include a South Korean infrastructure secondary fund, a co-investment in Acciona Energia, and an investment in Heathrow Airport Holdings Ltd.
- 4.3 During the quarter, nearly \$6m was returned and \$2m called. Of the original commitment of \$80m, \$65m has now been drawn-down. As the mandate only began in 2011, deployment of capital has been relatively fast. Total value to paid-in capital is a healthy 1.4, up from 1.3 last quarter.

- 4.4 As previously outlined, Grosvenor Capital is fund raising for a second global infrastructure fund.

## **5. M&G UK COMPANIES FINANCING FUNDS**

- 5.1 The M&G UK Companies Financing Funds provide the Fund with exposure to UK credit markets. The Funds play a valuable 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 4.8 years and average credit rating of BB+. Within the portfolio, the credit ratings of Barrett and Taylor Wimpey have improved from BBB- to BB+.
- 5.4 For Fund II, the portfolio also consists of 8 loans but with an average repayment period of 6 years. This includes loans to Caffè Nero, Holidaybreak Limited and Workplace Group plc.
- 5.5 All loans continue to be paid in accordance with their covenants.

## **6. HEARTHSTONE SOCIAL AND AFFORDABLE HOUSING**

- 6.1 Details of this mandate have been provided in the General Governance Report.

## **7. CONCLUSION**

- 7.1 The investment outlook of the Fund's private equity managers is neutral in terms of Europe and mildly optimistic in terms of US markets. The danger of overpaying for assets is a common concern of both private equity managers. The infrastructure and credit market managers continue to source deals at a satisfactory rate.
- 7.2 There continues to be a positive flow of distributions across the various private equity funds as their programme matures, although the returns from Wilshire are better than those from SL Capital. In this regard, however, the gradual weakening of the Euro in recent times has not helped the Euro denominated funds. The performance of Grosvenor Capital continues to be very strong.

**8. RECOMMENDATION**

- 8.1 The Panel and Committee are asked to note the progress of the Fund's Alternatives investments as at 31 December 2014 and invited to comment as appropriate.**

**Chief Finance Officer**

**Date: 1 March 2015**

**Contact Officer: Alastair McGirr**

**LIST OF BACKGROUND PAPERS**

NIL

## Appendix A

### Falkirk Council Pension Fund Alternative Markets Update - 31/12/2014

#### Alternative Assets Summary - Original Currency

Manager	Fund	Commitment 000's	Unfunded 000's	(a) Cost 000's	(b) Return of Cost 000's	(c) Distribn Gains 000's	(d) Market Value 000's	(b + c + d) Total Value 000's	Total Value to Paid In Cap.	Inception Rate of Return	Percentage to be drawn down
<b>Private Equity</b>											
SL Capital Partners	European Strategic Partners 2004	€ 30,000	€ 3,467	€ 26,533	€ 11,926	€ 8,679	€ 12,368	€ 32,973	1.24	5.6%	
SL Capital Partners	European Strategic Partners 2006	30,000	3,736	26,264	9,017	3,792	19,371	32,180	1.23	3.5%	
SL Capital Partners	European Strategic Partners 2008	27,000	8,771	18,229	2,779	509	18,537	21,825	1.20	1.5%	
SL Capital Partners	European Smaller Funds I	15,000	10,172	4,828	0	0	4,374	4,374	0.91	N/A	
	<b>SL Capital Partners Total</b>	<b>€ 102,000</b>	<b>€ 26,146</b>	<b>€ 75,854</b>	<b>€ 23,722</b>	<b>€ 12,980</b>	<b>€ 54,650</b>	<b>€ 91,352</b>			25.6%
Wilshire Associates	Fund VI - Europe	€ 3,600	€ 223	€ 3,377	€ 2,106	€ 1,336	€ 1,393	€ 4,835	1.43	7.9%	
Wilshire Associates	Fund VII - Europe	3,600	221	3,379	1,097	507	2,436	4,040	1.20	0.9%	
Wilshire Associates	Fund VIII - Europe	3,700	628	3,072	1,165	547	2,507	4,219	1.37	32.0%	
	<b>Wilshire Associates Europe Total</b>	<b>€ 10,900</b>	<b>€ 1,072</b>	<b>€ 9,828</b>	<b>€ 4,368</b>	<b>€ 2,390</b>	<b>€ 6,336</b>	<b>€ 13,094</b>			9.8%
Wilshire Associates	Fund VI - US	\$14,000	\$751	\$13,249	\$5,403	\$5,190	\$7,966	\$18,559	1.40	6.2%	
Wilshire Associates	Fund VII - US	11,500	698	10,802	3,299	3,198	8,668	15,165	1.40	6.8%	
Wilshire Associates	Fund VIII - US	12,700	1,319	11,381	3,736	2,309	9,978	16,023	1.41	10.6%	
Wilshire Associates	Fund VII - Asia	1,800	166	1,634	864	554	947	2,365	1.45	8.4%	
Wilshire Associates	Fund VIII - Asia	2,000	1,119	881	238	78	931	1,247	1.42	-11.9%	
Wilshire Associates	Opportunities Fund II-B	15,000	2,029	12,971	7,002	2,498	7,473	16,973	1.31	10.4%	
Wilshire Associates	Fund IX	15,000	13,546	1,454	0	0	1,870	1,870			27.3%
	<b>Wilshire Associates US and Asia Total</b>	<b>\$72,000</b>	<b>\$19,628</b>	<b>\$52,372</b>	<b>\$20,542</b>	<b>\$13,827</b>	<b>\$37,833</b>	<b>\$72,202</b>			
<b>Infrastructure</b>											
Grosvenor Capital	Customised Infrastructure Strategies	\$80,000	\$14,907	\$65,093	\$12,683	\$3,506	\$74,671	\$90,860	1.40	9.7%	
	<b>Grosvenor Capital Total</b>	<b>\$80,000</b>	<b>\$14,907</b>	<b>\$65,093</b>	<b>\$12,683</b>	<b>\$3,506</b>	<b>\$74,671</b>	<b>\$90,860</b>			18.6%
<b>Credit Markets</b>											
Prudential/M&G	UK Companies Financing Fund	£11,835	£0	£11,835	£4,943	£0	£8,718	£13,661	1.15	4.7%	
Prudential/M&G	UK Companies Financing Fund II	10,000	6,406	3,594	117	89	3,535	3,741	1.04	4.4%	
	<b>Credit Market Total</b>	<b>£21,835</b>	<b>£6,406</b>	<b>£15,429</b>	<b>£5,060</b>	<b>£89</b>	<b>£12,253</b>	<b>£17,402</b>			29.3%
<b>Social / Affordable Housing</b>											
Hearstone plc	Housing Fund for Scotland	£30,000	£14,750	£15,250	£0	£0	£15,299	£15,299			49.2%
	<b>Social/Affordable Housing Total</b>	<b>£30,000</b>	<b>£14,750</b>	<b>£15,250</b>	<b>£0</b>	<b>£0</b>	<b>£15,299</b>	<b>£15,299</b>			

## Appendix B

### Falkirk Council Pension Fund Alternative Markets Update - 31/12/2014

Exchange Rates	
\$	1.5608
€	1.2841

### Alternative Assets Summary - Sterling

Manager	Commitment £ 000's	Unfunded £ 000's	(a) Cost £ 000's	(b) Return of Cost £ 000's	(c) Distribtn Gains £ 000's	(d) Market Value £ 000's	(b + c + d) Total Value £ 000's	Total Value to Paid in Cap.
SL Capital Partners	79,433	20,361	59,072	18,474	10,108	42,559	71,141	1.20
Wilshire Associates	54,619	13,410	41,208	16,563	10,720	29,174	56,457	1.37
Grosvenor Capital	51,256	9,551	41,705	8,126	2,246	47,841	58,214	1.40
M & G	21,835	6,406	15,429	5,060	89	12,253	17,402	1.13
Hearthstone plc	30,000	14,750	15,250	0	0	15,299	15,299	1.00
	<b>£237,143</b>	<b>£64,478</b>	<b>£172,664</b>	<b>£48,223</b>	<b>£23,163</b>	<b>£147,126</b>	<b>£218,513</b>	
Allocation to Private Equity (based on unfunded commitment plus market value)		6.2%						
Allocation to Private Equity (based on market value only)		4.2%						
Allocation to Infrastructure (based on unfunded commitment plus market value)		3.4%						
Allocation to Infrastructure (based on market value only)		2.8%						