

Report to: Pension Committee

Date of meeting: 24 June 2019

By: Chief Finance Officer

Title: Infrastructure update and proposal

Purpose: To inform the Committee of the Fund's infrastructure portfolio proposal.

RECOMMENDATION:

The Committee is recommended to approve that the East Sussex Pension Fund commits £40m to Archmore International Infrastructure Fund III and £20m to Infracapital Greenfield Partners II LP.

1. Background

1.1 The East Sussex Pension Fund (the Fund)'s infrastructure portfolio currently consists of allocations to three funds; the Infracapital Partners III (a mid-market brownfield fund), the UBS International Infrastructure Fund and the Pantheon Global Infrastructure III.

1.2 Following the 2017 strategy review, and the subsequent illiquid markets review, the Committee agreed to increase the Fund's allocation to infrastructure assets from 2% to 4%. This reflected the Committee's investment belief that investors with long-term time horizons are typically less constrained by liquidity requirements and is therefore able to benefit from an illiquidity premium associated from investing in certain assets.

1.3 Hymans believe that the Fund will need to have total infrastructure investments in the region £150-200m by the end of 2022 in order to have 4% of total Fund assets invested in the asset class at that point. The Fund therefore has a £20-70m commitment shortfall. There is therefore a need to commit further capital in order to achieve the target allocation.

2. Infrastructure – ESPF Existing Providers

2.1 UBS are a global infrastructure manager with a very clear and consistent investment philosophy and process. Over the years, UBS has taken steps to prevent any style drift within their infrastructure funds. The investment team has also been relatively stable. UBS run very concentrated infrastructure portfolios; there are only six assets in Fund I (and in their Fund II).

2.2 UBS offering is appropriate as a component of the Fund's overall infrastructure allocation. Hymans recommend committing £40m to Archmore International Infrastructure III Fund, subject to negotiating a discounted fee with UBS, and suggest that the benchmark allocation to UBS infrastructure is maintained at 1% of total Fund assets, which will comprise of both the maturing UBS Fund I and the new Archmore Fund III.

2.3 M&G Infracapital Greenfield Partners II LP will construct core infrastructure assets, as opposed to the brownfield strategy that the Fund currently invests in that buys assets that are already operational. This is a follow-on strategy to Infracapital Greenfield Partners I LP that held a final close in 2017. Infracapital's second greenfield strategy is expected to follow a largely similar investment strategy. Infracapital seeks to create a well-diversified fund, investing in sectors such as transport, energy, and telecoms sectors.

2.4 Infracapital with their Greenfield strategies is seeking to create rather than buying core assets with contractual cash flows to hold over a long period. The strategy should complement the

Fund's existing infrastructure investments and will provide further diversification within the Fund's investment strategy whilst moving more towards an income-based portfolio over the medium to long term. Recommend committing £20m to M&G's fund and suggest that the benchmark allocation to M&G infrastructure is remains at 1% of total Fund assets, which will comprise of both M&G funds. It should be noted that this target is unlikely to be reached based on current commitment levels, but anticipate future fund launches that will help work towards this level over time.

3. Conclusion and reasons for recommendations

3.1 The Committee is recommended to agree that the Fund commits £40m to Archmore International Infrastructure Fund III and £20m to Infracapital Greenfield Partners II LP. These allocations will help the Fund work towards its 4% target infrastructure allocation over the short-term. It is considered that both allocations are complimentary to the Fund's existing infrastructure assets.

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Background Documents
None