



## **LOCAL PENSION COMMITTEE – 25 MAY 2018**

### **REPORT OF THE DIRECTOR OF CORPORATE RESOURCES**

#### **HEDGING OF NON-EQUITY ASSETS**

##### **Purpose**

1. The purpose of this report is to inform the Committee of a decision made by the Director of Corporate Resources under delegated powers, relating to the expansion of the current hedge.

##### **Background**

2. As part of Leicestershire Pension Fund's agreed strategy, it actively manages its exposure to overseas currencies that comes as a by-product of its holdings in overseas equities. This exposure totals about £1.3bn and the neutral position is to hedge 50% of this exposure back to sterling. The Fund employs Kames Capital to actively manage the currency hedge and they have freedom to move away from the default position if they feel that there is a mis-valuation of any currency against sterling; as an example, they are currently 100% hedged against the Australian Dollar and have no hedge against the Japanese Yen.
3. The Fund also has overseas currency exposure in many of its non-equity investments. These can generally be classified as 'managed' (the Fund's targeted return managers, for example, actively consider their exposure to currencies as part-and-parcel of their portfolio construction) and 'unmanaged'.
4. These unmanaged exposures are in areas such as timberland, private equity, and infrastructure. In some cases the managers do no hedging of the underlying investment, so an asset valued in Euros will give the Fund an exposure to that currency. In other cases they hedge all currencies back to the US Dollar as a matter of policy, thereby giving the Fund US Dollar exposure regardless of where the asset actually is.
5. Of the unmanaged currency exposures, the only one that is sufficiently large to justify consideration for hedging is the US Dollar.

##### **Currency Programme Proposal**

6. Scott Jamieson, the Fund's independent investment advisor, is currently of the opinion that the combination of a current account and budget deficit within the US is likely to be detrimental to the performance of the US Dollar against sterling. This view was shared by the Fund's currency managers (Millennium and Kames), LGPS Central and Andy Green of Hymans Robertson.

7. A report produced by Scott on this matter, including comments from Kames and Millennium, is attached as an appendix to this report.
8. Given the consensus of opinion, the Director of Finance wrote to the Chair and Vice-Chair of the Committee to seek their view on the intention to increase the Fund's currency hedging position so that it took into account the Fund's unmanaged US Dollar exposure. Both supported the proposal.
9. It is important to note that changing the hedging position does not alter the Fund's strategy and is purely a tactical move to reflect current concerns. However, given the size of the un-hedged US Dollar exposure (£350 million), it was felt appropriate to consult the Chair and Vice-Chair before taking any action. By way of an example a 1% change in the USD to GBP exchange rate would create a gain or loss of £1.75m (50% of the change in asset value).
10. Kames Capital were instructed to implement the hedge, which was completed on the 9<sup>th</sup> May 2018.
11. The default position for the hedge is 50%, in-line with the existing equity hedge. Kames have freedom to change the position depending upon their opinion of value and risk at any point in time. This will give them the ability to have no hedge in place if they are confident on the Dollar's strength (relative to sterling) or a 100% hedge if they expect a significant weakening of the Dollar.

### **Recommendation**

The Local Pension Committee is asked to note the report.

### **Appendix**

Note: Reflecting on the outlook for the US\$.

### **Equality and Human Rights Implications**

None.

### **Officers to Contact**

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