



Glasgow City Council

Strathclyde Pension Fund Committee

Report by Director of Strathclyde Pension Fund

Contact: Richard McIndoe Ext: 77383

**Item 5**

24th November 2021

## Review of the Direct Investment Portfolio

### Purpose of Report:

To conclude a review of the Direct Investment Portfolio (DIP).

### Recommendations:

The Committee is asked to **NOTE** the contents of this report and to **APPROVE** the following recommendations:

- no change is proposed to the objectives, structure, overall size parameters, risk and return parameters, or governance structure;
- the individual investment guidelines should be revised as follows
  - Target investment size: **£30m to £100m** (currently £20m to £100m)
  - Minimum investment: **£20m** (currently £10m)
  - Maximum investment: greater of **£250m** or **1%** of Total Fund Value (currently £200m or 1%).
- the existing co-investment programme should be extended in order to maximise its effectiveness, subject to development of a detailed proposal; and
- DIP's profile should be refreshed by
  - re-naming it as the Direct Impact Portfolio
  - redesigning the DIP website page and other materials to highlight the portfolio's achievements and clarify its objectives and
  - re-marketing it with a brief campaign to increase awareness of the portfolio and its objectives, particularly in respect of local investment.

Ward No(s):

Citywide: ✓

Local member(s) advised: Yes  No  consulted: Yes  No

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# 1 Background

## 1.1 Current Review

The SPF business plan for 2021/22 was approved by the Committee in March 2021. Amongst the priorities for the year it includes a review of DIP, including objectives, strategy, structure and capacity. This is consistent with previous practice of reviewing every 3 years after the actuarial valuation and review of overall SPF investment strategy.

## 1.2 Previous Reviews

In December 2009, the Committee agreed to establish a New Opportunities Portfolio (NOP) with a broad remit to invest in assets for which there was an attractive investment case but to which the current structure did not provide access.

The NOP strategy was reviewed in 2012 and in 2015. It was re-branded as the Direct Investment Portfolio (DIP) in 2015.

The most recent review of the DIP strategy and operating arrangements was concluded in December 2018.

## 1.3 Implementation Framework

DIP investment proposals are assessed on their own merits within an agreed implementation framework based on SPF's overall risk-return objectives and specific DIP parameters.

The framework agreed at the 2018 review is summarised below.

<b>Direct Investment Portfolio</b>	
<b>Objectives</b>	Primary objective identical to overall SPF investment objective. Secondary objective of adding value through investments with a positive local, economic or ESG (environmental, social, governance) impact.
<b>Strategy &amp; Structure</b>	In line with SPF risk-return framework but focused on the UK and on Equity, Long Term Enhanced Yield and Short Term Enhanced Yield asset categories.
<b>Risk and Return</b>	Portfolio benchmark return of <b>CPI +3% p.a.</b> Individual risk and return objectives for each investment.
<b>Capacity</b>	Target allocation of <b>5%</b> of total Fund (based on Net Asset Values). Range of <b>2.5%</b> to <b>7.5%</b> of total Fund.
<b>Investment Size</b>	Target: <b>£20m to £100m</b> Minimum: <b>£10m</b> Maximum: greater of <b>£200m</b> or <b>1%</b> of Total Fund Value.
<b>Decision Making</b>	3 stage process with review and satisfactory due diligence by officers, followed by a presentation to the Sounding Board before a proposal is taken to Committee for approval subject to completion of legal documentation.
<b>Monitoring</b>	Includes individual investment reports, participation in advisory boards, and a quarterly DIP monitoring report which is reviewed by the Fund's Investment Advisory Panel.

## 2 Portfolio Summary

The portfolio as at 30<sup>th</sup> September 2021 can be summarised as follows.

	Since Inception	Current Portfolio
	(£m)	(£m)
<b>Total Commitments Agreed</b>	<b>1,831</b>	<b>1,734</b>
Amounts Drawn Down by Managers	<b>1,219</b>	<b>1,143</b>
+ Increase in Value	<b>242</b>	<b>197</b>
- Received Back in Distributions	<b>287</b>	<b>287</b>
- Realisations	<b>121</b>	<b>-</b>
<b>= Total Net Asset Value (NAV)</b>	<b>1,053</b>	<b>1,053</b>

The portfolio comprises **53** separate investments.

A current schedule of DIP investments is included at Appendix A.

## 3 Performance

### 3.1 Portfolio Performance

Portfolio performance to 30<sup>th</sup> September 2021 is as follows.

	Q3 2021 (%)	1 year (%)	3 years (% p.a.)	5 years (% p.a.)	Since Inception (% p.a.)
<b>DIP</b>	<b>2.3</b>	<b>3.6</b>	<b>2.9</b>	<b>5.0</b>	<b>7.2</b>
<b>DIP Benchmark*</b>	<b>1.4</b>	<b>4.5</b>	<b>4.2</b>	<b>2.7</b>	<b>1.7</b>
<b>SPF Total Fund</b>	<b>1.4</b>	<b>17.8</b>	<b>8.8</b>	<b>9.3</b>	<b>11.4</b>

Source: Northern Trust

\* CPI +3% pa from 2019; previously LIBOR

DIP's performance since inception is very good. Shorter-term performance figures are quite modest but are expected to grow over time as is typical for long-term private market investments. SPF Total Fund performance is driven mostly by equity returns. Recent equity returns have been exceptional both for DIP and Total Fund, but equity forms a relatively small part of DIP, so has less of an impact on total DIP return.

### 3.2 Individual Investment Performance

Overall, the portfolio has performed well as have a majority of its individual investments. On a RAG analysis:

- **47** investments are rated **green**
- **3** are **amber**
- **None red.**

**3** are unrated pending completion of legals.

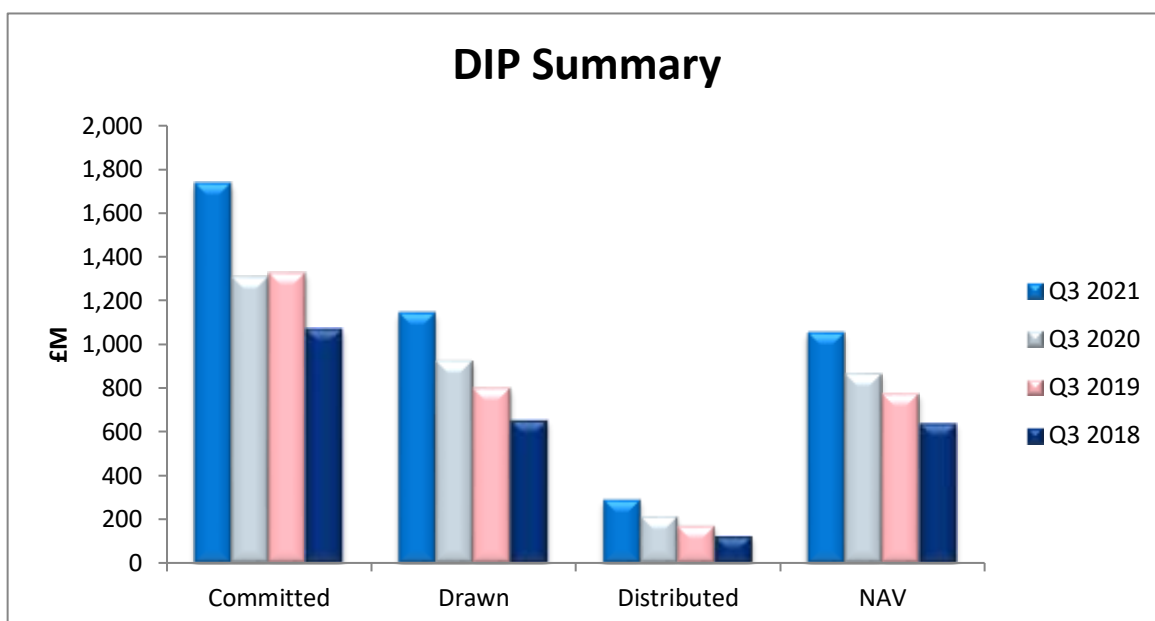
## 4 Progress Since Last Review

The Committee agreed 12 separate recommendations at the conclusion of the 2018 review. They included: investigation of co-investment opportunities and an extension of local property investment; an expanded allocation target and range for DIP overall; increased average lot size for individual investments; a

revised performance benchmark; a new risk assessment template; additional resource; monitoring and reporting of impact; and efforts to encourage DIP managers to become PRI signatories. All have since been implemented.

Total of individual investments has increased from 39 to 53.

The chart below shows how the portfolio financials have developed since 2018.



Given the good progress made by DIP to date, no fundamental change is envisaged as a result of the 2021 review.

## 5 2021 Review

The following aspects of the portfolio have been reviewed:

- Objectives
- Strategy and Structure
- Size
- Risk and Return
- Cost
- Governance
- Profile

Conclusions and recommendations in each of these areas are set out in the sections below.

## 6 Objectives

### 6.1 Primary Objective

The primary objective of the Direct Investment Portfolio is identical to the Fund's overall investment objective. That is to support the funding strategy by adopting an investment strategy and structure which incorporate an appropriate balance between risk and return with the aim of achieving:

- a greater than 2/3 probability of being 100% funded over the target funding period; and
- a less than 10% probability of falling below 70% funded over the next three years.

The DIP risk and return objectives are also broadly similar to those of the Fund overall. Further details are set out in the Risk and Return section at 10 below.

## 6.2 Secondary Objective

The Direct Investment Portfolio has a secondary objective of adding value through investments with a positive local, economic or ESG (environmental, social, governance) impact. Further details are set out in the ESG Impact section at 11 below.

No change to the objectives is currently proposed.

## 7 Strategy and Structure

### 7.1 Strategy

A summary of the current DIP investment strategy is included at Appendix B. Just as the objective for DIP is the same as that of the Fund overall, the risk-return framework is also the same.

No change to the overall strategy is proposed, though some implementation changes are considered below.

### 7.2 Structure

A summary of the current DIP structure is included at Appendix C.

At a very high level, DIP's allocation is dominated by long term enhanced yield investments. Beneath that, there is more than adequate diversification by sector, manager, vintage year and individual asset.

No change to the structure is proposed.

## 8 Size

### 8.1 Background

DIP was established in 2009 with a maximum capacity of £300m. That was subsequently increased to a maximum DIP Net Asset Value (NAV) of 3% of total Fund NAV, and then in 2015 to 5% of Fund NAV. At the 2018 review, it was agreed that DIP should have a target size of **5%** of total Fund value together with a range of **2.5%** to **7.5%** of total Fund value.

### 8.2 Current Position

The table below provides a summary of DIP actual allocation compared to target allocation as at 30<sup>th</sup> September 2021 and 2018.

	<b>2018</b> <b>(£m)</b>	<b>2021</b> <b>(£m)</b>
Total Fund NAV	21,977	27,907
<b>DIP NAV</b>	<b>635</b>	<b>1,053</b>
<b>DIP Target NAV (5%)</b>	<b>1,099</b>	<b>1,395</b>
DIP Target Range	549	697
(2.5% to 7.5%)	1,648	2,093
<b>Undrawn Commitments</b>	<b>420</b>	<b>591</b>

The actual NAV of **£1,053m** is **£342m** below target but comfortably within the target range. The actual NAV plus undrawn commitments would exceed the target but still be within the target range.

### 8.3 Projected Position

As part of the review, portfolio modelling was carried out to provide projections of portfolio growth under a variety of economic scenarios. Some examples of the portfolio modelling carried out are included at Appendix D.

No absolute conclusions can be drawn from the modelling as there are too many variables involved. However, the projections would suggest the following:

- DIP is making good progress towards its target but is unlikely to achieve it based solely on commitments to date if markets continue to rise steadily (though a significant market downturn would take DIP through the target until markets recovered)
- In order to achieve and maintain the target, DIP requires ongoing new commitments. The modelling implies a new commitment pace of 7.5% to 10% of current commitments each year – i.e. c.£125m to £170m p.a.
- DIP is unlikely to breach its current 2.5% to 7.5% range.

Current pace of new commitments is in excess of £200m p.a. If that is maintained, DIP is likely to achieve and exceed its target but remain within target range for the foreseeable future. Therefore, no change is proposed to the current target and target range.

### 8.4 Individual Investments

The size of individual DIP investments has grown broadly in line with the overall size of DIP and the Fund. Early investments were typically in a range of £5m to £10m. Recent investments have more typically been in a range of £20m to £50m or larger. It is anticipated that this trend will continue, and the following revised guidelines are proposed for individual new DIP investments.

- **Target investment size: £30m to £100m** (currently £20m to £100m)
- **Minimum investment: £20m** (currently £10m)
- **Maximum investment: greater of £250m or 1% of Total Fund Value** (currently £200m or 1%).

As previously, each investment will be considered on its own merits and the recommended lot size will be determined by the specific characteristics of the proposal.

## 9 Diversification

### 9.1 Background

Appendix C demonstrates that DIP is well diversified by sector, manager, asset class and vintage year. The 2018 review noted that, whilst it is important that underlying diversification should be maintained, from a practical perspective, it is also important that the portfolio should not become over-diversified as this would tend to increase costs and resource requirements and dilute returns. This is partly addressed through the increasing average lot sizes described above. For similar reasons DIP has also invested in several subsequent funds with individual managers after a first successful investment. This will continue where appropriate. The 2018 review produced 2 new proposals to assist in managing sector diversification as DIP continues to develop – co-investment and an extended programme of local property

investment. Both of these have been successfully developed and implemented. However, a potential extension of the co-investment programme is described below.

## 9.2 Co-Investment Proposal

Co-investment is an additional investment in an individual asset made by a portfolio investor alongside a portfolio investment in that asset. This allows the investor to increase exposure to individual assets held within the portfolio. Typically, co-investments are offered at a fee significantly lower than the portfolio management fee. SPF has successful co-investment programmes within its private equity portfolios and, subsequent to the 2018 review, co-investments of £50m each were agreed alongside new commitments to Dalmore and Equitix funds within DIP. The Equitix commitment has been fully deployed.

A number of the other managers within DIP, particularly the infrastructure managers, offer co-investment opportunities. It is proposed that DIP should explore these further with a view to extending the co-investment programme in order to maximize its effectiveness. This may involve agreeing an amount for allocation to existing DIP managers as and when co-investment opportunities arise. A detailed proposal will be developed for consideration.

## 10 Risk and Return

### 10.1 Return Parameters

The 2018 review set:

- a benchmark return of **CPI +3% p.a.** for DIP as a whole;
- a minimum expected IRR of **5%** for individual investments; and
- indicative return expectations for each of the sectors covered by DIP.

No change is proposed to return expectations.

Further details of expected sector returns are set out in Appendix E.

### 10.2 Risk Register

At the 2018 review a new risk template was introduced and has subsequently been applied to each investment.

Appendix F shows the current summary risk register in respect of the DIP portfolio as a whole. This aggregates the individual risk ratings for each DIP investment. Overall, at 30<sup>th</sup> September 2021 DIP had a low risk rating of 6.4/(25).

## 11 Measuring Impact

Risk and return remain the primary considerations for DIP investments, but local and ESG impacts are an important secondary consideration. These impacts were quantified for the first time in the 2018 review.

The table below summarises headline impacts achieved by DIP to date.

Impact	2018	2021
Environmental Clean Energy Generated	254 GWh p.a.	636 GWh p.a.

Carbon Reduction (tonnes p.a.)	87,000	147,000
Sufficient to Power (homes p.a.)	61,000	219,000
<b>Social</b>		
Jobs Created	2,800	3,900
Jobs Sustained	36,000	55,000
Infrastructure Projects	295	682
<b>Governance</b>		
PRI signatories	11/(24)	31/(33)
<b>Local</b>		
Local/Scottish Investments	Not available.	>£500m

Further details of DIP's positive impacts are included at Appendix G.

## 12 Cost

DIP operates in private rather than listed markets. As a consequence DIP investment management costs are significantly higher than management costs for SPF overall – though in line with other private markets portfolios in the Fund. This is reduced as far as possible by fee negotiation and investment selection. This will continue. The proposed extension of the co-investment programme should achieve lower fees than existing infrastructure investments. The increasing portfolio size and size of individual investments should also achieve some economy, though this may be limited.

## 13 Governance

DIP's governance process is summarized as follows.

<b>DIP Strategy</b>	<ul style="list-style-type: none"> <li>Strategy and guidelines agreed by SPF Committee.</li> </ul>
<b>Investment Sourcing</b>	<ul style="list-style-type: none"> <li>Led by SPFO officers.</li> <li>DIP has an established profile in the UK investment market and this creates a steady pipeline of opportunities for review and analysis.</li> </ul>
<b>Investment Analysis</b>	<ul style="list-style-type: none"> <li>Officers review and filter investment opportunities and carry out initial diligence.</li> <li>Further external diligence as appropriate including by investment and legal consultants (Hymans Robertson and Pinsent Masons).</li> </ul>
<b>Decision-Making</b>	<ul style="list-style-type: none"> <li>Review by Committee Sounding Board.</li> <li>Final investment decision by SPF Committee with assistance from SPF Pension Board.</li> </ul>
<b>Monitoring and Reporting</b>	<ul style="list-style-type: none"> <li>Monitoring of individual investments carried out by officers.</li> <li>Quarterly report on DIP progress reviewed by Investment Advisory Panel.</li> </ul>

	<ul style="list-style-type: none"> <li>▪ Summary report reviewed by committee and included in Annual Report.</li> </ul>
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The governance structure and process are further illustrated in Appendix H.

External consultancy and legal support were reviewed recently, with the appointment of Hymans Robertson and Pinsent Masons respectively in July 2021. Monitoring of portfolio performance will be further supported by the introduction in the next financial year of *privatei*, a private market fund monitoring system hosted by the Fund’s custodian, Northern Trust.

The existing structure and process work well and the review concluded that, given the enhancements described above, no further change was necessary.

However, as the portfolio continues to grow more resource will be required within SPFO to ensure that investment sourcing, analysis, monitoring and reporting can all be carried out with the necessary level of rigour and diligence. Ongoing resource requirements will be kept under review.

#### 14 Profile

DIP has been established for more than 10 years, has built a significant portfolio of current investments, and has been open for business throughout that period - i.e. DIP has accepted and reviewed new proposals, has had a pipeline of investments under review, and has had capacity for new investments at all times. That being the case, DIP has a distinct profile in the institutional investment marketplace both locally and across the UK. DIP has been a founder investor in a number of funds and is regularly a first-close investor in new or follow-on funds. The DIP investment team are confident that they are offered all, or the vast majority of opportunities which fit the agreed criteria – in particular local opportunities. In the course of the review this view has been tested with consultants and other contacts, and is well supported, with no evidence to the contrary.

There is scope, however, to try to refresh the profile of DIP. The following steps are proposed as a means to achieve this:

- **Re-name** - although the DIP name is well recognized, it may not be the best descriptor of how the portfolio has developed in reality – i.e. almost all investments are in funds rather than directly into assets. Direct Impact Portfolio would be an easy and more appropriate alternative; and
- **Redesign** – mainly the DIP website page as first port of call, but could include a flier or other material to highlight the portfolio’s achievements and clarify its objectives. Potentially also a bespoke DIP logo.
- **Re-market** - a short marketing campaign to increase awareness of the portfolio and its objectives, particularly in respect of local investment.

#### 15 Policy and Resource Implications

*Financial:*

None at this time.

*Legal:* None at this time.

*Personnel:* None.

*Procurement:* None.

**Council Strategic Plan:** Strathclyde Pension Fund aligns with the theme of a well governed city. A review of the Direct Investment Portfolio is included as a priority in the SFP 2021/22 Business Plan.

**Equality and Socio-Economic Impacts:**

*Does the proposal support the Council's Equality Outcomes 2017-22* Equalities issues are addressed in the Fund's responsible investment policy.

*What are the potential equality impacts as a result of this report?* No specific impact from this proposal.

*Please highlight if the policy/proposal will help address socio economic disadvantage.* No specific impact from this proposal.

**Climate Impacts:**

*Does the proposal support any Climate Plan actions? Please specify:* Yes. DIP is an important element of Strathclyde Pension Fund's Climate Change strategy, which is being developed in line with Item 34 of the Council's Climate Action Plan.

*What are the potential climate impacts as a result of this proposal?* Continued investment in renewable energy and clean technology.

*Will the proposal contribute to Glasgow's net zero carbon target?* DIP contributes to SPF's net zero carbon target.

**Privacy and Data Protection impacts:** None.

## 16 Recommendations

The Committee is asked **to NOTE** the contents of this report and **to APPROVE** the following recommendations:

- no change is proposed to the objectives, structure, overall size parameters, risk and return parameters, or governance structure;
- the individual investment guidelines should be revised as follows
  - Target investment size: **£30m** to **£100m** (currently £20m to £100m)
  - Minimum investment: **£20m** (currently £10m)
  - Maximum investment: greater of **£250m** or **1%** of Total Fund Value (currently £200m or 1%).
- the existing co-investment programme should be extended in order to maximise its effectiveness, subject to development of a detailed proposal; and
- DIP's profile should be refreshed by
  - re-naming it as the Direct Impact Portfolio
  - redesigning the DIP website page and other materials to highlight the portfolio's achievements and clarify its objectives and
  - re-marketing it with a brief campaign to increase awareness of the portfolio and its objectives.

## Appendices

- A Schedule of DIP Investments
- B Summary of DIP Investment Strategy
- C Summary of DIP Investment Structure
- D Example Portfolio Modelling
- E Indicative Returns
- F Risk Template
- G Measuring Impact
- H DIP Governance Structure

DIP Schedule of Investments as at 30<sup>th</sup> September 2021

Fund	Vintage Year	Sector	Asset Category	SPF Commitment (£m)	Cumulative Drawdowns (£m)	Undrawn Commitment (£m)	Cumulative Distributions (£m)	Net Asset Value (£m)
SEP II	2004	VC	Equity	5	5	0	4	0
SEP III	2006	GC	Equity	5	5	0	18	0
Panoramic Enterprise Capital Fund 1 LP	2010	GC	Equity	3	3	0	9	1
Scottish Loans Fund	2010	CR	STEY	6	6	0	6	1
SEP IV LP	2011	GC	Equity	5	5	0	6	6
Epidarex Fund II	2012	VC	Equity	5	5	0	1	7
Foresight Infra Holdco Ltd (prev PIP Ltd)	2012	INF	LTEY	1	1	0	0	1
Clydebuilt Fund LP	2013	PR	LTEY	75	75	0	14	54
Dalmore PPP Equity PiP Fund	2013	INF	LTEY	50	50	0	23	48
Albion Community Power LP	2014	RE	LTEY	40	36	4	6	38
Alpha Social Long Income Fund	2014	SL	LTEY	15	15	0	3	17
Healthcare Royalties Partners III LP	2014	CR	STEY	19	18	0	11	12
Iona Environmental Infrastructure LP	2014	RE	LTEY	10	10	0	5	9
Resonance British Wind Energy Income Ltd	2014	RE	LTEY	10	10	0	4	8
Green Investment Group Offshore Wind Fund LP	2015	RE	LTEY	80	80	0	39	66
Muzinich UK Private Debt Fund	2015	CR	STEY	20	15	5	9	6
NTR Wind I LP	2015	RE	LTEY	40	35	4	24	26
Panoramic Growth Fund 2 LP	2015	GC	Equity	15	10	5	3	12
Temporis Renewable Energy LP (Onshore Wind)	2015	RE	LTEY	30	30	0	7	32

DIP Schedule of Investments as at 30<sup>th</sup> September 2021

Fund	Vintage Year	Sector	Asset Category	SPF Commitment (£m)	Cumulative Drawdowns (£m)	Undrawn Commitment (£m)	Cumulative Distributions (£m)	Net Asset Value (£m)
Equitix Fund IV LP	2016	INF	LTEY	30	30	0	7	35
PIP Multi-Strategy Infrastructure LP(Foresight)	2016	INF	LTEY	130	120	10	31	96
SEP V LP	2016	GC	Equity	20	18	2	9	23
Dalmore Capital Fund 3 LP	2017	INF	LTEY	50	50	0	6	52
Hermes Infrastructure Fund II	2017	INF	LTEY	50	48	2	5	50
Iona Environmental Infrastructure 3 LP	2017	RE	LTEY	14	12	2	0	13
Maven Regional Buyout Fund	2017	GC	Equity	20	13	7	2	12
Pemberton UK Mid-Market Direct Lending Fund	2017	CR	STEY	40	36	4	6	37
Pentech Fund III	2017	VC	Equity	10	6	4	0	6
Temporis Operational Renewable Energy Strategy LP Fund II	2017	RE	LTEY	30	21	9	2	24
Tosca Debt Capital Fund II LP	2017	CR	STEY	30	21	9	8	20
Beechbrook UK SME Credit II Fund	2018	CR	STEY	30	26	4	5	26
Epidarex Fund III	2018	VC	Equity	15	5	10	0	5
Equitix Fund V LP	2018	INF	LTEY	50	45	5	5	46
Greencoat Solar Fund II LP	2018	RE	LTEY	50	47	3	3	46
Invesco Real Estate Finance Fund II (formerly GAM REFF II)	2018	CR	STEY	20	14	6	5	13
Capital Dynamics Clean Energy Infrastructure VIII	2019	RE	LTEY	40	18	22	1	17
Equitix Fund VI LP	2019	INF	LTEY	50	31	19	0	31
Equitix MA 19 LP (Co-Investment Fund)	2019	INF	LTEY	50	39	11	1	38

DIP Schedule of Investments as at 30<sup>th</sup> September 2021

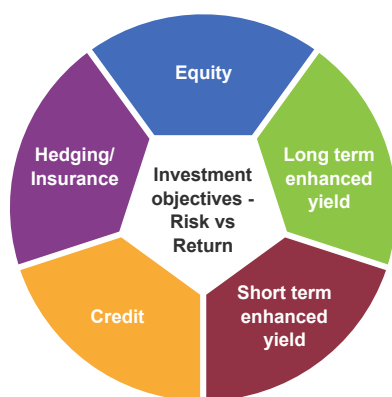
Fund	Vintage Year	Sector	Asset Category	SPF Commitment (£m)	Cumulative Drawdowns (£m)	Undrawn Commitment (£m)	Cumulative Distributions (£m)	Net Asset Value (£m)
Legal & General UK Build to Rent Fund	2019	PR	LTEY	75	75	0	0	74
Places for People Scottish Mid-Market Rental (SMMR) Fund	2019	PR	LTEY	25	16	9	0	6
Clydebuilt Fund II LP	2020	PR	LTEY	100	0	100	0	0
Dalmore Capital Fund 4 LP	2020	INF	LTEY	50	0	50	0	0
Dalmore II 39 LP	2020	INF	LTEY	50	0	50	0	0
Man GPM RI Community Housing Fund	2020	PR	LTEY	30	10	20	1	8
Palatine Private Equity Fund IV	2020	GC	Equity	25	7	18	0	6
Quinbrook Renewables Impact Fund	2020	RE	LTEY	50	6	44	0	6
Clean Growth Fund	2021	VC	Equity	20	3	17	0	3
SEP VI LP	2021	GC	Equity	30	0	30	0	0
Tosca Debt Capital Fund III LP	2021	CR	STEY	30	12	18	0	12
Foresight Regional Investment Fund, Scotland	2021 (Legals)	GC	Equity	30	0	30	0	0
Funding Affordable Homes	2021 (Legals)	PR	LTEY	30	0	30	0	0
Iona Resource and Energy Efficiency (Strathclyde) LP	2021	RE	0	6	0	6	0	0
RiverRock Sustainable Industry Finance Fund LP	2021 (Legals)	CR	STEY	20	0	20	0	0
<b>Total as at 30/09/2021</b>				<b>1,734</b>	<b>1,143</b>	<b>590</b>	<b>287</b>	<b>1,053</b>
<b>Total as at previous quarter 30/06/2021</b>				<b>1,703</b>	<b>1,073</b>	<b>629</b>	<b>266</b>	<b>988</b>

DIP Schedule of Investments as at 30<sup>th</sup> September 2021

Realised Investments								
Fund	Vintage Year	Sector	Asset Category	SPF Commitment (£m)	Cumulative Drawdowns (£m)	Undrawn Commitment (£m)	Cumulative Distributions (£m)	Net Asset Value (£m)
Aberdeen UK Infrastructure Partners LP	2014	INF	LTEY	28	28	0	57	0
Aviva Investors PIP Solar PV LP	2015	RE	LTEY	20	3	0	4	0
City Legacy (Athletes Village)	2013	CR	STEY	35	33	2	39	0
GAM REFF I (formerly Renshaw Bay)	2014	CR	STEY	10	7	3	10	0
Markham Rae	2016	CR	STEY	0	1	0	0	0
SEP Environmental Capital Fund LP	2014	RE	LTEY	4	4	0	11	0
<b>Total as at 30/09/2021</b>				<b>97</b>	<b>76</b>	<b>5</b>	<b>121</b>	<b>0</b>

## Summary of DIP Investment Strategy

In November 2015 the Committee agreed that the portfolio should adopt the risk-return asset framework that had been agreed for development of Strathclyde Pension Fund's (SPF) investment strategy. The framework is illustrated below.



Asset Category	Main Objectives
Equity	To generate return
Hedging / Insurance	To reduce the exposure of the funding level to variations in interest rates and inflation
Credit	To ensure additional yield, provide income and reduce funding volatility
Short term enhanced yield	To provide an income stream above the expected return on investment grade corporate bonds
Long term enhanced yield	To provide a long-term income stream and a degree of inflation protection

In practice, only 3 of the 5 asset categories in the risk-return framework are represented in DIP. 2 categories, Hedging/Insurance and Credit are not represented. This is unlikely to change in the near future.

In addition the following principles are applied to potential DIP investments.

- Risk, size, sector, cash-flow and exit factors each need to be considered on a deal-by-deal basis and in the context of the Fund as a whole.
- Investments should:
  - complement the Fund's existing investment strategy with respect to its risk and return objectives;
  - not overburden the current resources of the Fund;
  - have clear and well developed legal and governance provisions;
  - be structured appropriately. Preference is for multi-asset, multi-investor portfolios in order to mitigate risk.
  - be FCA regulated;
  - be Sterling denominated;
  - be predominately UK;
  - have a stable team with a good business plan and a proven track record in their field;
  - have other, suitable key investors;
- Due diligence will be completed before any formal commitment is made. This will include detailed review of:
  - risk and return characteristics
  - the industry and/or sector

**Summary of DIP Investment Strategy**

- legal documentation
- local and ESG impact and
- fair working practices.
- All managers must be prepared to treat SPF as a professional client (MiFID II)

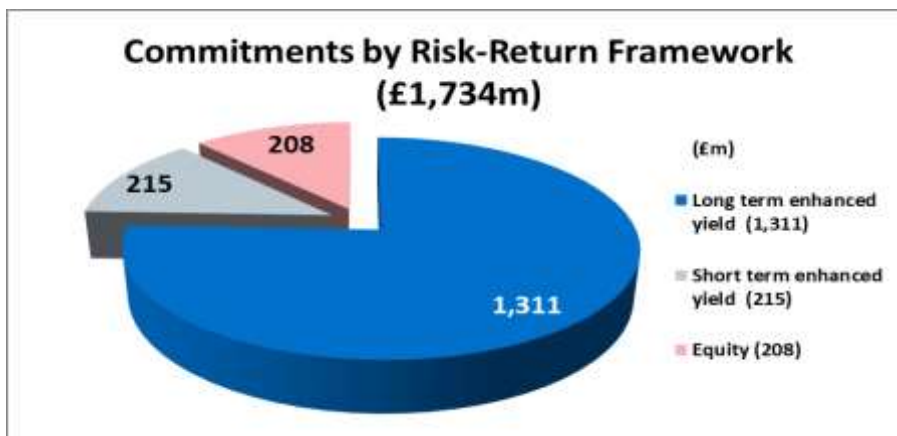
Key characteristics of DIP investments which differentiate them from the main SPF investment structure are summarized as follows.

	<b>Main Structure</b>	<b>Direct Investment Portfolio</b>
<b>Investment Characteristics</b>	<ul style="list-style-type: none"> <li>▪ Liquid, evergreen, strategic.</li> <li>▪ Global.</li> <li>▪ Lot size &gt;1% of Fund.</li> </ul>	<ul style="list-style-type: none"> <li>▪ Illiquid, self-liquidating, opportunistic. Local, economic or ESG (Environmental, Social, Governance) impact.</li> <li>▪ Sterling and UK based.</li> <li>▪ Lot size &lt;1% of Fund.</li> </ul>

## Summary of DIP Investment Structure

### Asset Category Allocation

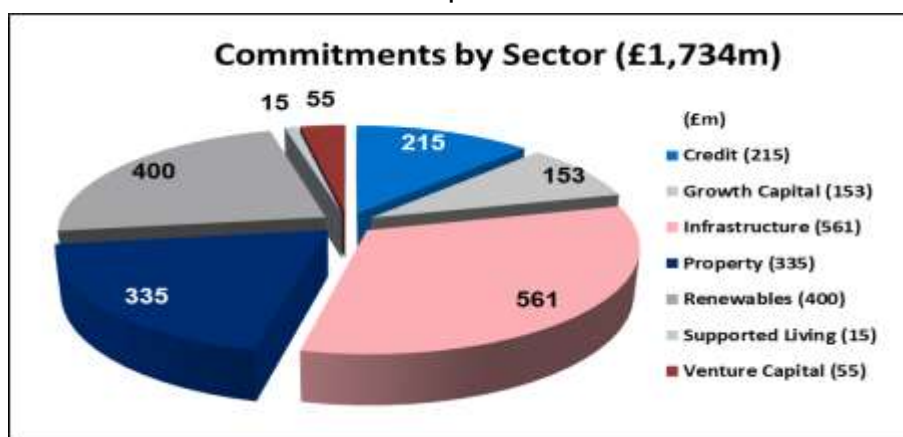
The current structure in relation to the Fund's risk-return framework is illustrated in the chart below which shows total DIP commitments as at 30<sup>th</sup> September 2021.



Long term enhanced yield investments – infrastructure, renewables, and local property – continue to dominate the current DIP allocation profile. The 2018 review considered whether it would be preferable to achieve a more balanced allocation for DIP but concluded that, so long as a balanced strategy was maintained across the Fund as a whole, it was not important for DIP to reflect a similar balance. It is more important that DIP maintains its opportunistic approach, though this will inevitably lead to some bias towards the areas which demonstrate the most opportunities or best investment value over any particular period. LTEY investments typically have a much longer fund life than other categories and this compounds their dominance. For the foreseeable future it is therefore likely that DIP will retain a bias towards long term enhanced yield.

### Sector Allocation

Below the asset category level, DIP is further diversified across individual sectors. Allocation as at 30<sup>th</sup> September 2021 is illustrated in the chart below.

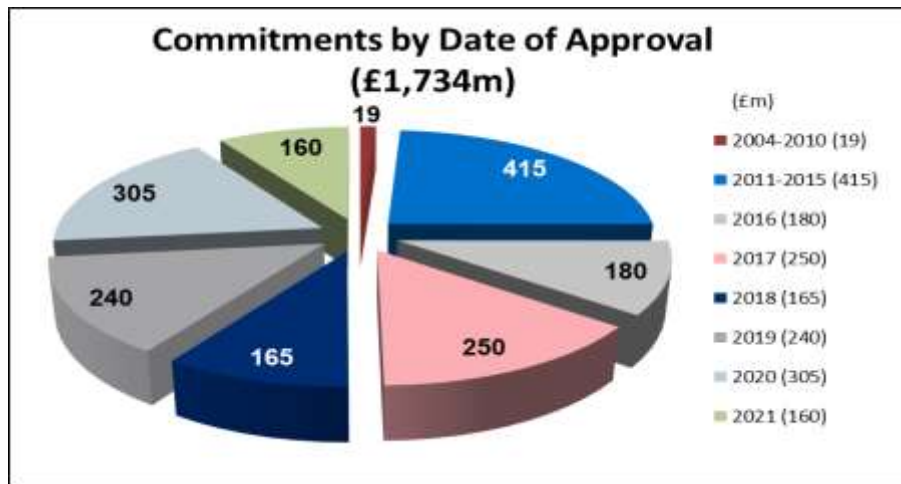


Within each sector there is further diversification by fund manager and individual investment asset, particularly within renewable energy and infrastructure.

## Summary of DIP Investment Structure

### Commitments by Year of Approval

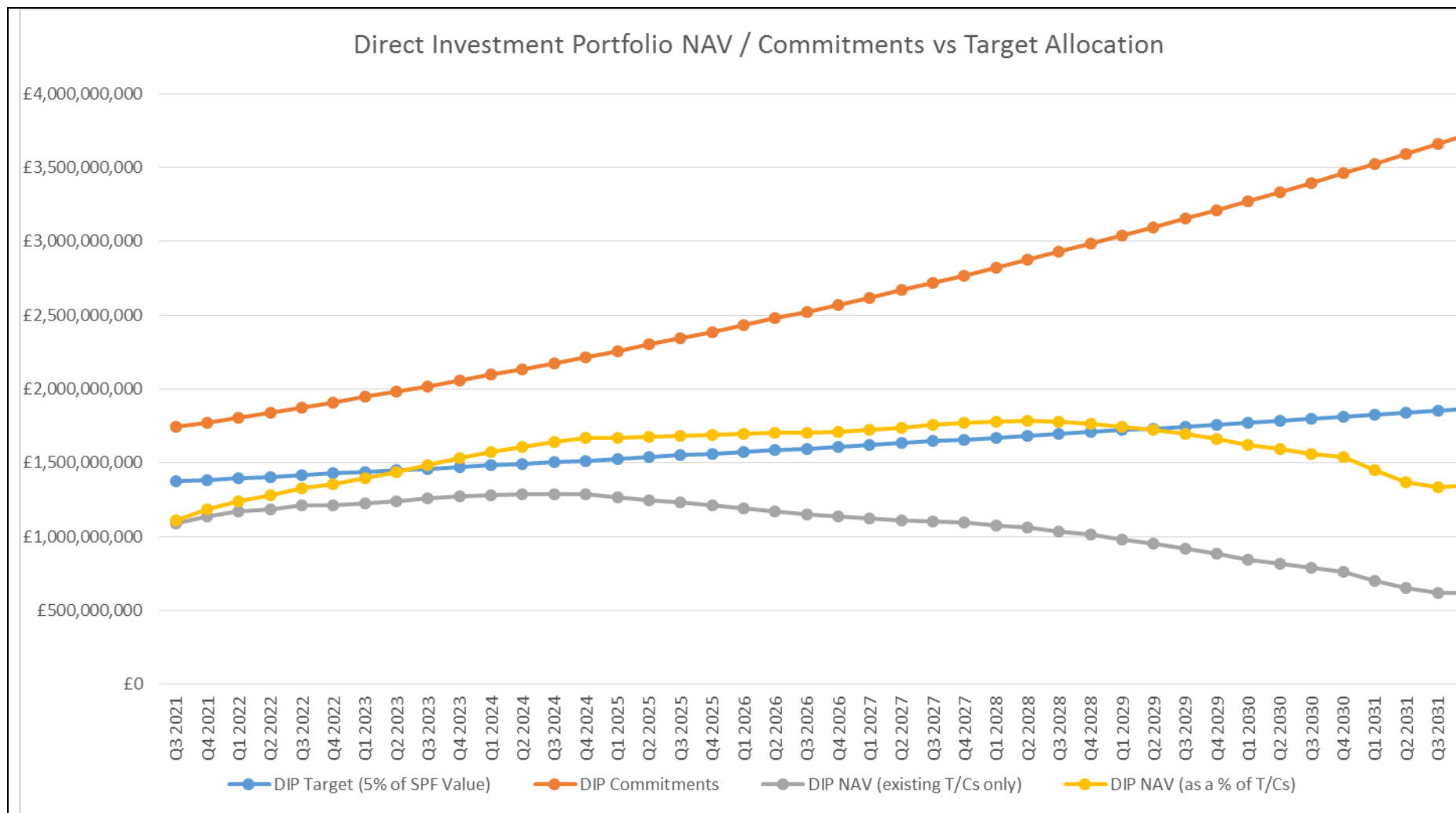
The chart below shows the commitments made by DIP split out by the year of Committee approval as at 30<sup>th</sup> September 2021.



The chart shows a fairly even spread across vintage year. This is generally positive as it provides a further form of diversification which should reduce volatility of cash flow and performance.

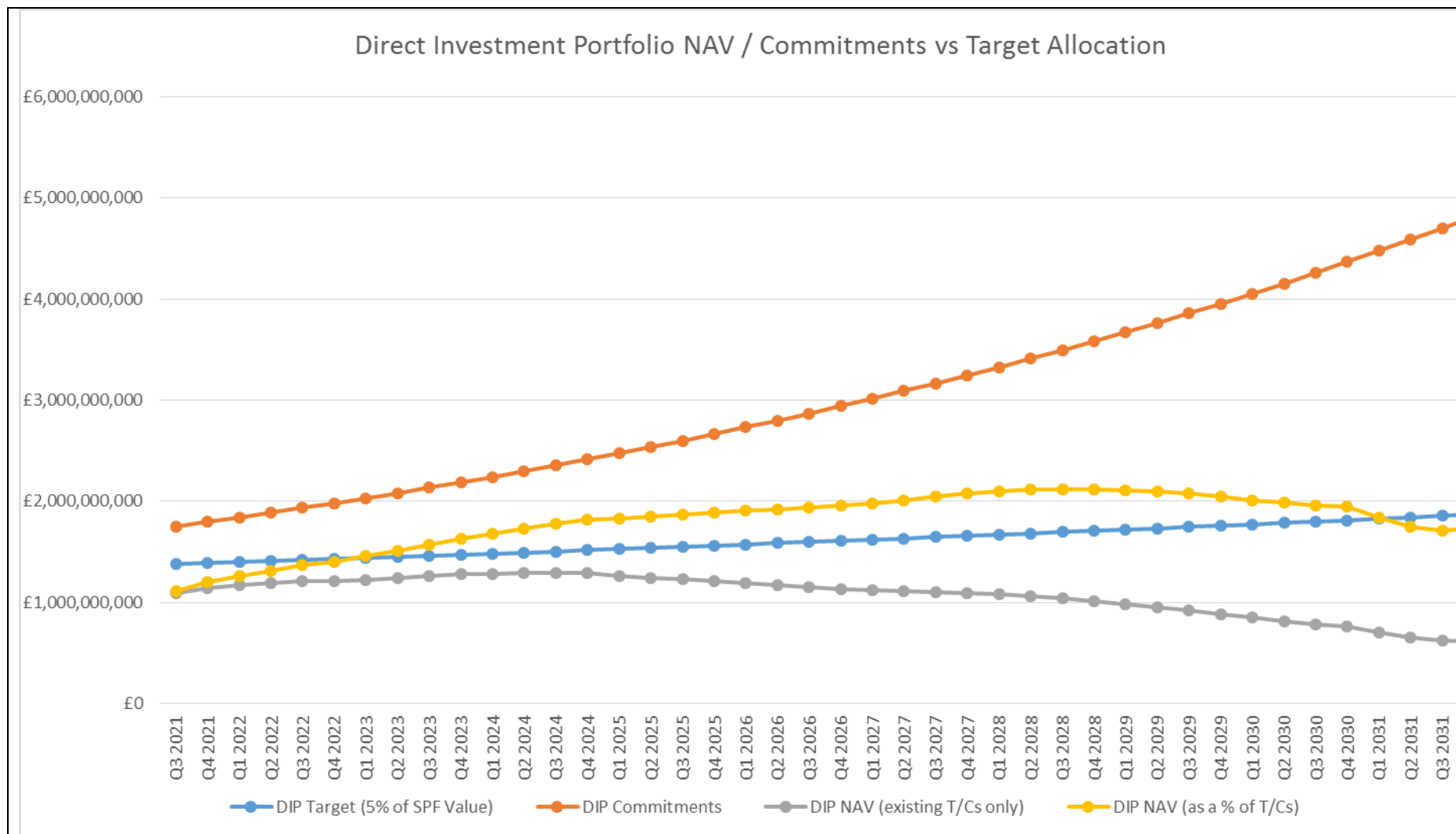
### Example Portfolio Modelling – Commitment Projections

#### Current Projection +7.5% p.a. New Commitments



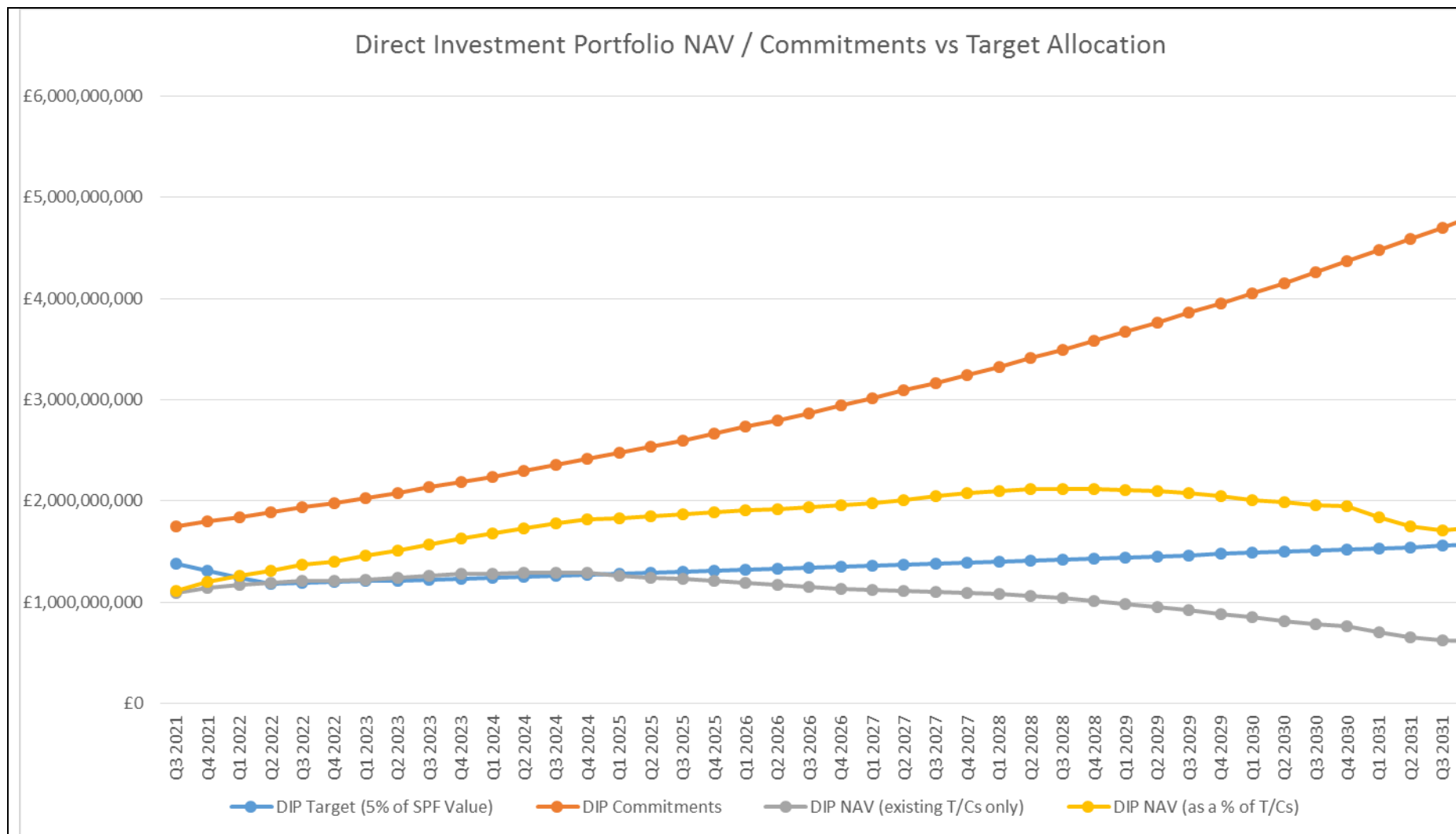
### Example Portfolio Modelling – Commitment Projections

#### Current Projection +10% p.a. New Commitments



### Example Portfolio Modelling – Commitment Projections

Current Projection + market downturn (-20%)



## Indicative Returns

Asset Category	Sector	Indicative Return (Net IRR)	Sub sector returns (Net IRR)
Equity	Private Equity	>12%	<ul style="list-style-type: none"> <li>▪ Buyout &gt;12%</li> <li>▪ Growth capital &gt;15%</li> <li>▪ Venture capital &gt;20%</li> <li>▪ Returns may vary by +/- 5% depending on factors such as target sector, investment stage, average investment size, etc.</li> </ul>
Short Term Enhanced Yield	Private Debt (direct lending)	>6%	<ul style="list-style-type: none"> <li>▪ Corporate (senior secured) &gt;6%</li> <li>▪ Subordinated/mezzanine &gt;10%</li> <li>▪ Funds may invest in more than one type of debt. Target return will reflect expected allocation between different types.</li> </ul>
	Private Debt (real assets)	>6%	<ul style="list-style-type: none"> <li>▪ Real estate debt &gt;8%</li> <li>▪ Infrastructure debt &gt;6%</li> </ul>
Long Term Enhanced Yield	Infrastructure	6-12%	<ul style="list-style-type: none"> <li>▪ Social, transportation, energy, environmental, communications.</li> <li>▪ Returns and yields dependent on leverage, sector, asset type, whether assets are operational or are under construction and whether returns are generated from capital appreciation or from contractual or demand based income stream.</li> </ul>
	Renewable Energy	5-12%	<ul style="list-style-type: none"> <li>▪ On and off shore wind, hydro, solar, bioenergy</li> <li>▪ Returns and yields dependent on leverage, sector, asset type, whether assets are operational or under construction and whether returns are generated from capital appreciation or from contractual or demand based income stream.</li> </ul>
	Housing	4-10%	<ul style="list-style-type: none"> <li>▪ Social, affordable, private rental sector, specialist, broad market</li> <li>▪ Returns and yields dependent on sector, asset type, geography, whether assets are operational or under construction and whether returns are generated from capital appreciation or from contractual or demand based income stream.</li> </ul>

## Risk Template

In March 2019, the Committee approved a revised Risk Policy and Strategy Statement. The statement sets out a common basis for risk management across the Fund's strategies.

As a key part of the risk strategy, a detailed risk register has been established and is maintained for the Strathclyde Pension Fund (SPF). A separate register is maintained for DIP. This is summarised below as at 30<sup>th</sup> September 2021:

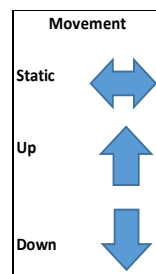
<b>MAJOR/CATASTROPHIC</b>	Significant concerns regarding the ability of the investment to meet its target	15+
<b>MODERATE</b>	Concern regarding either one or a combination of factors.	10-14
<b>MINOR</b>	No concerns at this time.	5-9
<b>INSIGNIFICANT</b>	Risk is easily mitigated by normal day to day process.	1-4











Probability			Impact				
			1	2	3	4	5
			Insignificant	Minor	Moderate	Major	Critical
5	Almost Certain	90%	5	10	15	20	25
4	Likely	70%	4	8	12	16	20
3	Possible	50%	3	6	9	12	15
2	Unlikely	30%	2	4	6	8	10
1	Rare	10%	1	2	3	4	5

←  
significant  
risk zone

## Risk Template

Risk	Ref No
Deployment Risk	DIP01
Operational Risk	DIP02
Counterparty/Default Risk	DIP03
Management/People/Key person Risk	DIP04
Valuation Risk	DIP05
Inflation Risk	DIP06
Legislative/Regulatory Risk	DIP07
Concentration Risk	DIP08
Exit/Liquidity Risk	DIP09
Idiosyncratic Risk	DIP10



RISK Ref No.	RESIDUAL ASSESSMENT					
	Risk Title/Risk Description	Residual Probability	Residual Impact	Residual Risk	Movement	
DIP01	Risk	Deployment	1.6	2.1	3.7	
	Cause	Failure to invest fund				
	Effect	No return on investment				
DIP02	Risk	Operational	2.7	2.9	8.0	
	Cause	Disruption due to poor functioning or damage to physical assets				
	Effect	Delay or inability to meet target				
DIP03	Risk	Counterparty/Default	2.6	3.0	8.1	
	Cause	Failure to meet contractual requirement or payment(s)				
	Effect	Credit Losses				
DIP04	Risk	Key person event	2.5	2.6	6.7	
	Cause	Failure of management team				
	Effect	Pause in investment process				
DIP05	Risk	Valuation	2.5	2.9	7.5	
	Cause	Overpayment for assets at point of investment				
	Effect	Reduction in returns				
DIP06	Risk	Inflation	2.1	2.4	5.5	
	Cause	Macro economic				
	Effect	Increase in asset price volatility				
DIP07	Risk	Legislative/Regulatory	2.2	2.7	6.4	
	Cause	Political or legislative				
	Effect	Adverse effect on assets				
DIP08	Risk	Concentration	2.1	2.6	5.8	
	Cause	Assets not diversified				
	Effect	Counterparty or asset exposure				
DIP09	Risk	Exit/Liquidity	2.3	2.9	6.9	
	Cause	Changes in markets				
	Effect	Inability to realise investment				
DIP10	Risk	Idiosyncratic Risk	2.0	2.5	5.4	
	Cause	Covid 19				
	Effect	Global				
Average		2.3	2.7	6.4		
			Portfolio Rank			

## Measuring Impact

Asset Category	Main ESG Impacts	Local Impacts
<b>Equity</b>	Provision of venture and growth capital to facilitate small company start-ups and expansion. Creates and supports employment. Also supports economic growth and technological development in a range of sectors including biotechnology, medical devices, pharmaceuticals, energy efficiency and IT. Estimate <b>4,274</b> new jobs created by funds in which DIP has invested, and a total of <b>12,131</b> jobs sustained by those funds.	DIP's equity managers have a very strong local presence: SEP, Panoramic and Maven are based in Glasgow; Epidarex and Pentech in Edinburgh both have a strong Scottish focus and significant links to local business networks and universities within their respective sectors (biosciences and IT). All equity managers are investing across the UK or further afield, however.
<b>Short Term Enhanced Yield</b>	Provision of loan capital to a large number of companies, particularly micro, small and medium sized enterprises (SMEs). Supports employment. Provides economic stability. Estimated decrease of <b>393</b> jobs in funds in which DIP has invested (due mainly to the COVID economic downturn), however a total of <b>43,197</b> jobs sustained by those funds.	One of DIP's first investments was the Scottish Loans Fund (SLF) managed by Maven Capital in Glasgow. DIP was a founder investor and agreed 2 separate commitments of £5m. SLF raised £113m in total commitments but only drew down £70m of those funds.  There have been few subsequent local STEY opportunities for DIP and none which have been suitable.
<b>Long Term Enhanced Yield</b>	<b>Infrastructure:</b> construction and maintenance of physical assets; improved built environment; social value. Projects in which DIP has invested have built or are building: <ul style="list-style-type: none"> <li>▪ <b>217</b> schools</li> <li>▪ <b>24</b> hospitals</li> <li>▪ <b>15,042</b> social housing units</li> <li>▪ <b>5,490</b> government and defence personnel housing units</li> <li>▪ <b>8,860</b> units of student accommodation</li> <li>▪ <b>22</b> social care centres / healthcare facilities</li> </ul>	Core infrastructure investments include: <ul style="list-style-type: none"> <li>▪ <b>118</b> assets located in Scotland – total NAV c.<b>£387m</b>.</li> <li>▪ DIP's share of total NAV c.<b>£33m</b>.</li> </ul>

## Measuring Impact

	<p><b>Renewable Energy:</b> construction and/or operation of renewable energy infrastructure assets across a range of technologies including onshore wind, offshore wind, solar, small hydro, community power, and anaerobic digestion.</p> <p>During the past 12 months, renewable energy investments directly attributable to DIP (i.e. its share of fund investments) are expected to:</p> <ul style="list-style-type: none"> <li>▪ Generate <b>636 GWh</b> of renewable energy (sufficient to power <b>219,000</b> homes); and</li> <li>▪ Avoid the emission of <b>147,000</b> tonnes of CO<sub>2</sub>e.</li> </ul>	<p>Renewables investments are distributed across the UK but include:</p> <ul style="list-style-type: none"> <li>▪ <b>42</b> assets located in Scotland – total NAV c.<b>£762m</b>.</li> <li>▪ DIP’s share of total NAV c.<b>£151m</b>.</li> </ul> <p>Many of these also provide additional community benefits in the form of agreed financial contributions.</p>
	<p><b>Property:</b> support for local property market; regeneration from development sites; positive local economic impact.</p>	<p>DIP has committed <b>£25m</b> to the Places for People Scottish mid-market rental fund and <b>£75m</b> to the Legal &amp; General UK build to rent fund. Together these have agreed deals for construction of:</p> <ul style="list-style-type: none"> <li>▪ <b>1,927</b> housing units across <b>12</b> sites in Scotland, of which</li> <li>▪ <b>1,157</b> across <b>6</b> sites are in Strathclyde</li> <li>▪ Total NAV of the Scottish units c.<b>£175m</b></li> <li>▪ DIP’s share of total NAV c.<b>£31m</b>.</li> </ul> <p>LTEY also includes the Clydebuilt portfolio, which DIP created in 2013, Clydebuilt is a local property fund with a focus on development and regeneration, and has invested over £100m in 14 separate properties in the Strathclyde area. Notable projects include: construction of a retail park in Port Glasgow (completed 2019); construction of a retail park in Gorbals, Glasgow (completed 2020); and development of a shopping centre in Shawlands, Glasgow to a mixed use retail and residential “village” (in planning – due to commence work later 2021). In 2020 DIP created Clydebuilt II – a further £100m portfolio.</p>

Measuring Impact

		<p>Other place-based investments have included £30m working capital for construction of the Athletes Village in the East end of Glasgow.</p>
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## DIP Governance Structure

The DIP Governance Structure is illustrated below, together with figures for the number of proposals considered in the 3 years to end September 2021.

