Item 5(c)

2nd March 2022

Glasgow City Council

Strathclyde Pension Fund Committee

Report by Richard McIndoe, Director of Strathclyde Pension Fund

Contact: Lorraine Sweeney, Investment Manager, Strathclyde Pension Fund Ext: 77427

DIP Co-investment Programme

Purpose of Report:

To present a proposal for the extension of DIP's existing Co-investment programme.

Recommendations:

The Committee is asked to **APPROVE** the proposed extension of DIP's existing Co-investment programme.

Ward No(s):	Citywide: ✓
Local member(s) advised: Yes ☐ No ☐	consulted: Yes ☐ No ☐

1 Background

At its meeting in November 2021, the committee considered the conclusions of a review of DIP, and agreed that the existing co-investment programme should be extended in order to maximise its effectiveness, subject to development of a detailed proposal.

2.1 Co-investment

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. Subsequent to the previous (2018) review of DIP, co-investments of £50m each were agreed alongside new commitments to Dalmore and Equitix funds. SPF also has successful co-investment programmes within its private equity portfolios.

2.2 Rationale for Extending the Programme

The Equitix commitment previously agreed has now been fully deployed.

A number of the other managers within DIP, particularly the infrastructure managers, offer co-investment opportunities. These typically occur when mangers are presented with compelling opportunities which are too large for their main funds to acquire in their entirety. This may be due either to pre-determined fund concentration limits which are set to ensure that the main funds are sufficiently diversified, or simply that a smaller stake would be more appropriate for the fund concerned. In these cases, SPF will be offered the balance of that particular asset alongside one, or more usually a number, of co-investors. These are investors who wish to deploy additional sums into either larger assets or particular sub-sectors of the infrastructure market.

The proposed extension would allow DIP to:

- deploy incrementally more funds into valuable sectors;
- manage portfolio diversification; and
- take advantage of lower fee structures on co-investments, which will reduce the overall blended cost of DIP's core and co-investment allocations.

2.3 Structure

Individual opportunities often arise at relatively short notice and require a rapid response by potential co-investors. To manage this, it is proposed that DIP should take a portfolio approach by establishing a new investment vehicle which could allocate funds to these opportunities within predetermined parameters but without individual review by committee. This is consistent with the approach taken within SPF's private equity portfolios. A key principle is that funds would only be allocated to managers with whom the committee had already approved a DIP investment.

2.4 Proposal

The proposal is:

- to create an independent co-investment fund (CIF) solely for DIP;
- to agree an initial overall allocation of funds; and
- to agree the parameters/restrictions within which these funds will be allocated and managed.

The proposed parameters are as follows:

- co-investments to be made only in UK assets;
- co-investments to be in assets where there is an existing fund investment;
- co-investments will never be more than the existing fund investment;
- co-investments to be a maximum of £15m in any single asset;
- a summary report of the proposed co-investment transaction to be provided to SPF prior to acquisition;
- SPF to have a right of veto of the proposed transaction;

It is unlikely that the transaction veto would be utilised, as only assets which satisfy the investment criteria of existing fund investment could be considered for co-investment. However, the right of veto, which will be exercised by SPF officers, provides an additional measure of control.

2.5 Size

An initial allocation of £200m is proposed. This is around 10% of the total value of DIP's current commitments and around 20% DIP's current Net Asset Value. It is envisaged that this will be sufficient to fund co-investment opportunities until the next review of DIP in 2024. Any proposed increase to this amount would require further approval by the committee.

2.6 Funds in Scope

A schedule of existing DIP funds which would be in scope for co-investment is included at Appendix A. Any new funds approved by the committee would also be in scope.

2.7 Risks

Given that co-investments will be into assets in existing DIP funds, they will be subject to the same risks and mitigants as those funds. The principal additional risk from the proposal is of investment concentration – i.e. DIP will acquire larger stakes in selected assets. This will be mitigated by the proposed programme parameters, by manager experience of running co-investment programmes, and by DIP's overall broad diversification. The proposal will also help DIP manage the risk of over-diversification.

2.8 Fees

Typically, co-investments are offered at a fee significantly lower than the portfolio management fee.

3 Policy and Resource Implications

Resource Implications:

Financial:	None
Legal:	Any investment will be subject to satisfactory completion of due diligence, including review and execution of appropriate legal documentation.
Personnel:	None.
Procurement:	None.
Council Strategic Plan:	Strathclyde Pension Fund aligns with the theme of a well governed city.

Equality and Socio-Economic Impacts:

Does the proposal support the Council's Equality Outcomes 2021-25? Please specify.	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:	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?	The proposal is likely to lead to increased investment by DIP in renewable energy infrastructure.

Will the proposal contribute to Glasgow's net zero carbon target?	No specific impact from this proposal.
Privacy and Data Protection Impacts:	To be fully provided for in the legal documentation for any proposed investment.

4 Recommendation

The Committee is asked to **APPROVE** the proposed extension of DIP's existing Co-investment programme.

Appendix A

Funds in Scope

Key	Credit	Growth Capital	Infrastructure	Property	Renewable Energy	Supported Living	Venture Capital
	CR	GC	INF	PR	RE	SL	VC

Fund	Asset Category	Sector	Year Approved at Committee	Target Fund Size (£m)	Current Fund Size (£m)	SPF Commitment (£m)	Cumulative Drawdowns (£m)	Undrawn Commitment (£m)	Net Asset Value (£m)
Asset Category: Equity									
Clean Growth Fund	Equity	VC	2021	100	60	20	4	16	3
Epidarex Fund III	Equity	VC	2018	102	102	15	5	10	6
Foresight Regional Investment Fund, Scotland	Equity	GC	2021 (Legals)	60	0	30	0	30	0
Maven Regional Buyout Fund	Equity	GC	2017	125	94	20	13	7	13
Palatine Private Equity Fund IV	Equity	GC	2020	300	200	25	7	18	7
Pentech Fund III	Equity	VC	2017	88	88	10	6	4	9
SEP VI LP	Equity	GC	2021	350	180	30	0	30	0
	Total as at 31/12/2021		**Q4**	**1,125**	**725**	**150**	**35**	**115**	**38**
Asset Category: LTEY									
Capital Dynamics Clean Energy Infrastructure VIII	LTEY	RE	2019	400	300	40	18	22	19
Clydebuilt Fund II LP	LTEY	PR	2020	101	101	100	0	100	0
Dalmore Capital Fund 4 LP	LTEY	INF	2020	1000	137	50	37	13	36
Dalmore II 39 LP	LTEY	INF	2020	50	50	50	15	35	15
Equitix Fund V LP	LTEY	INF	2018	1001	1001	50	45	5	45
Equitix Fund VI LP	LTEY	INF	2019	1500	1110	50	28	22	31
Equitix MA 19 LP (Co-investment Fund)	LTEY	INF	2019	50	50	50	50	0	51
Foresight Infra Holdco Ltd (prev PIP Ltd)	LTEY	INF	2012	4	4	1	1	0	1
Funding Affordable Homes	LTEY	PR	2021 (Legals)	300	-	30	0	30	0

Appendix A

Funds in Scope

Fund	Asset Category	Sector	Year Approved at Committee	Target Fund Size (£m)	Current Fund Size (£m)	SPF Commitment (£m)	Cumulative Drawdowns (£m)	Undrawn Commitment (£m)	Net Asset Value (£m)
Asset Category: LTEY (cont'd)									
Greencoat Solar Fund II LP	LTEY	RE	2018	1500	1152	50	50	0	50
Hermes Infrastructure Fund II	LTEY	INF	2017	500	288	50	48	2	50
Iona Resource and Energy Efficiency (Strathclyde) LP	LTEY	RE	2021	6	6	6	2	4	2
Legal & General UK Build to Rent Fund	LTEY	PR	2019	3000	611	75	75	0	76
Man GPM RI Community Housing Fund	LTEY	PR	2020	400	135	30	21	9	19
PIP Multi-Strategy Infrastructure LP(Foresight)	LTEY	INF	2016	610	574	130	120	10	91
Quinbrook Renewables Impact Fund	LTEY	RE	2020	500	250	50	14	36	15
Temporis Impact Strategy V LP	LTEY	RE	2021	350	-	50	0	50	0
Total as at 31/12/2021			**Q4**	**11,271**	**5,769**	**862**	**525**	**337**	**502**
Asset Category: STEY									
RiverRock Sustainable Industry Finance Fund LP	STEY	CR	2021 (Legals)	150	-	20	0	20	0
Tosca Debt Capital Fund III LP	STEY	CR	2021	250	183	30	12	18	12
Total as at 31/12/2021			**Q4**	**400**	**183**	**50**	**12**	**38**	**12**

DIP Portfolio Total

	Quarter	Target Fund Size (£m)	Current Fund Size (£m)	SPF Commitment (£m)	Cumulative Drawdowns (£m)	Undrawn Commitment (£m)	Net Asset Value (£m)
Total as at 31/12/2021	**Q4**	**12,797**	**6,676**	**1,062**	**573**	**489**	**552**

** E – Explanation for any unavailable performance figures are due to: IRR too early to report, no drawdowns to date or currently in J curve