

# **Hammersmith & Fulham Pension Fund**

Transition Management Review – Global Equities

MJ Hudson Investment Solutions

---

**SEPTEMBER 2020**

## Table of Contents

Table of Contents .....	2
Contacts .....	2
Executive Summary .....	3
Background.....	3
Transition Event & Analysis .....	4
Risk Management .....	6
Systems and Operations .....	6
Reporting & Communication .....	6
Score Card .....	7

## Contacts

Steve Webster

Director

+44 20 7079 1000

[steve.webster@mjhudson.com](mailto:steve.webster@mjhudson.com)

Ben Gates

Associate

+44 20 7079 1000

[ben.gates@mjhudson.com](mailto:ben.gates@mjhudson.com)

6.1

## Executive Summary

	Legacy	Target
<b>Portfolios</b>	LGIM Low Carbon (33%)	LCIV Global Sustainable Core
<b>Names (£ Size) ex. cash</b>	385 (168m)	39 (164m)
<b>Retained (£ size)</b>	24 (17.5m)	24 (17.5)
<b>Traded (£ size)</b>	385 Sold (150.5m)	15 Bought (146.5m)
<b>Average Daily Volume</b>	0.6%	4.85%

	Estimated	Realised
<b>Implementation Shortfall (bps)</b>	31.5	32.7
<b>Fixed Costs inc. LGIM fees (bps)</b>	13.1	13
<b>Implicit Costs (bps)</b>	18.4	17
<b>Opportunity Cost (bps)</b>	+/-39.9	2.7

*bps = % of portfolio legacy value (inc. cash) £169m*

## Background

London CIV (LCIV) and Hammersmith & Fulham LGPS (H&F) have appointed MJ Hudson to review and oversee the transition of global equities from Legal and General Investment Management (LGIM) to the LCIV Global Sustainable Core Equities Fund (GSC) sub-advised by Morgan Stanley Investment Management (MSIM).

H&F were invested in a passive LGIM MSCI Low Carbon fund, managed as a life fund. H&F instructed LGIM that they wish to transfer a third (£170m) of their holdings to seed the new LCIV GSC fund.

LGIM provided a transition service to H&F, utilising their CSUF (Client Specific Unitised Fund), which effectively acts as a “side pocket” of the LGIM life fund. The LGIM proposed approach to redeem and transition assets using the CSUF had the following pros and cons:

### Pros

- Retained Exposure – Client remains invested throughout the transition event
- Optimal Transaction Tax – No transaction tax when moving assets into the transition fund
- Legacy Asset Expertise – LGIM familiar with trading in legacy assets

### Cons

- Fixed Fee – Equivalent of 4.5bps. Comparatively high as exclusive of brokerage.
- LGIM Choice of Redeemed Assets – LGIM PM choose which assets to redeem (this must be representative of the fund, but can be used by the PM to rebalance the life fund)
- Long Leadtime – Assets can only move, and trade based on LGIM weekly dealing cycle

6.1

On 10<sup>th</sup> August, LGIM moved 409 of 1300 constituent names of LGIM MSCI Low Carbon fund into the CSUF representing a £166m in-specie redemption. As required by LGIM, the redeemed names were broadly representative country and sector weights of the Low Carbon Fund.

On 11<sup>th</sup> August LCIV provided to LGIM the final MSIM target portfolio list for the GSC fund. We note that 23 (£17m) of the 409 names redeemed from the LGIM Low Carbon fund crossed with the target list.

The transition was fully executed on 18<sup>th</sup> of August, benchmarked against the Market on Close (MOC) on 17<sup>th</sup> of August.

Transition trading was settled on 20<sup>th</sup> of August and target assets were moved to the LCIV GSC fund on 24<sup>th</sup> August (for value 21<sup>st</sup> August), which generated a purchase of units, which have now been received by H&F LGPS.



6.1

## Transition Event & Analysis

LGIM completed the transition with an Implementation Shortfall (benchmark 17<sup>th</sup> August) of 32.7bps compared to an estimate of 31.6bps. This result was within the one standard deviation opportunity cost (±39.9) We note that LGIM’s initial July pre-transition analysis had a much higher than expected opportunity cost (50bps) versus our expectation of nearer 30bps. This was subsequently amended down to 40bps for the final August pre-trade.

### TRADE OUTLIERS

We noted from the LGIM’s pre-trade analysis a single purchase name (Reckitt Benckiser), representing 7.5% of the target, is much more illiquid than the rest of the transition portfolio. LGIM said that this purchase is equivalent to trading 15% of one day’s average volume. Unsurprisingly, this name came clear in the post-trade analysis as having the largest detriment to the trading. LGIM completed 75% early in the day but the stock rose over the remainder of the day leading to total IS contribution of 6bps. LGIM traded approximately 30% of the day’s volume.

Additionally, the rally of the S&P 500 and particularly its tech stocks, helped LGIM when it came to selling names like Amazon, Apple, and Tesla. The Alphabet switch of C for A shares was naturally hedging as both prices rose with the gain on selling C counteracting the loss on buying A.

### FOREIGN EXCHANGE

LGIM traded most of the required spot FX, long dated at or close to the WMR benchmark on MOC 17<sup>th</sup> August with some “true-up” trading done on the 18<sup>th</sup> and 19<sup>th</sup> August. We note that all trades were triangulated through the base currency GBP which although not the most efficient (due to paying spread twice in some cases), may be a requirement of the fund’s structure. The most significant true-up was the reversal on USD which was a result of the better-than-expected performance of selling USD shares, as explained above, however this was responsible for the majority of the FX shortfall as a result.

**TABLE 1: FOREIGN EXCHANGE**

Currency	GBP Bought	Sold IS	GBP Sold	Bought IS	Gross GBP	Total IS
AUD	3,795,185	90	1,674	(2)	3,796,859	87
CAD	774,484	16	22,510	(148)	796,994	(132)
CHF	5,575,217	92			5,575,217	92
DKK	1,143,949	9			1,143,949	9
EUR			5,953,932	(860)	5,953,932	(860)
HKD			1,039,639	(66)	1,039,639	(66)
ILS	450,939	19			450,939	19
JPY	11,685,130	161			11,685,130	161
NOK	298,612	5	876	(6)	299,487	(1)
SEK	1,335,237	16	6,298	(24)	1,341,535	(7)
SGD	256,609	9	4,570	(13)	261,179	(4)
USD	159,452	1,883	297,736	3	457,188	1,886
<b>Total</b>	<b>25,474,815</b>	<b>2,298</b>	<b>7,327,235</b>	<b>(1,115)</b>	<b>32,802,050</b>	<b>1,183</b>

**IMPLEMENTATION SHORTFALL ANALYSIS**

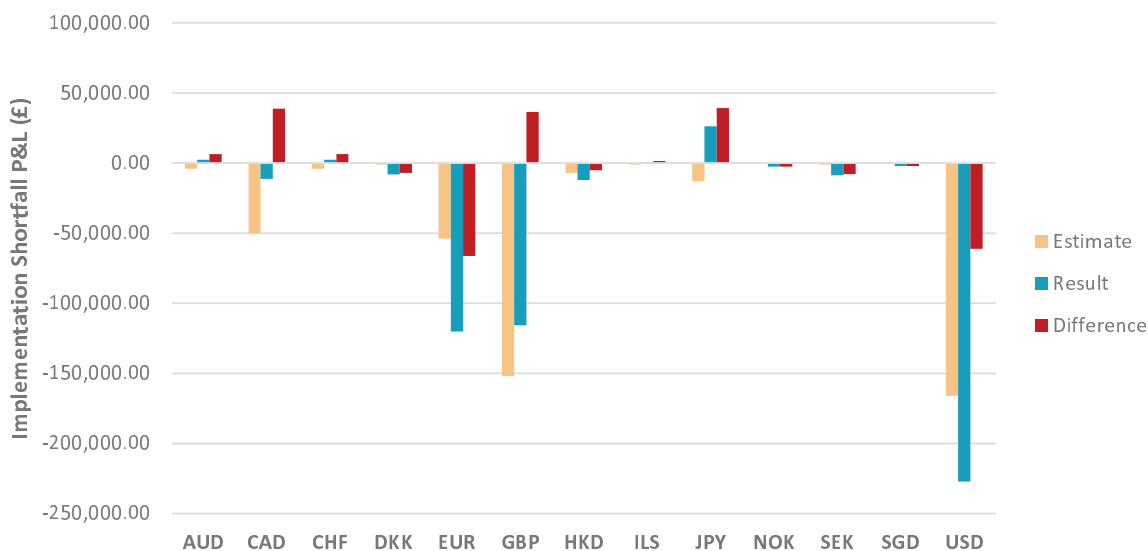
Included below is a summary of the implementation shortfall as calculated by MJ Hudson, compared to the estimate, and result as reported by LGIM. MJH agrees with LGIM's reported result for Implementation Shortfall having verified their trade files and independently verified their calculation. The minor differences in values are due to different benchmark prices sourced on 17<sup>th</sup> August.

**TABLE 2: IMPLMENTATION SHORTFALL COMPARISON**

Asset Type / Cost	Implicit	Commission	Taxes	Total IS
<b>MJH Result</b>				
Equities Sells (£)	(134,920)	15,242	3,516	(116,162)
Equities Buys (£)	468,363	16,573	110,476	595,412
Sub-total (£)	333,443	31,815	113,992	479,251
FX (£)	1,183	-	-	1,183
TM Fee (£)	-	75,000	-	75,000
<b>Grand Total (£)</b>	<b>334,626</b>	<b>106,815</b>	<b>113,992</b>	<b>555,434</b>
<b>Total (bps)</b>	<b>19.8</b>	<b>6.3</b>	<b>6.7</b>	<b>32.9</b>
<b>LGIM Result</b>				
Equities Sells (£)	(135,402)	15,242	3,516	(116,644)
Equities Buys (£)	466,286	16,573	110,476	593,335
Sub-total (£)	330,884	31,815	113,992	476,691
FX (£)	1,183	-	-	1,183
TM Fee (£)	-	75,000	-	75,000
<b>Grand Total (£)</b>	<b>332,067</b>	<b>106,815</b>	<b>113,992</b>	<b>552,875</b>
<b>Total (bps)</b>	<b>19.7</b>	<b>6.3</b>	<b>6.7</b>	<b>32.7</b>
<b>MJH-LGIM Difference</b>	<b>(0.2)</b>	<b>(0.0)</b>	<b>(0.0)</b>	<b>(0.2)</b>
<b>LGIM Estimate</b>				
Equities (£)	308,000	30,000	116,000	454,000
FX (£)	-	-	-	-
TM Fee (£)	-	75,000	-	75,000
<b>Grand total (£)</b>	<b>308,000</b>	<b>105,000</b>	<b>116,000</b>	<b>529,000</b>
<b>Total (bps)</b>	<b>18.4</b>	<b>6.3</b>	<b>6.9</b>	<b>31.6</b>
<b>Result-Estimate Difference</b>	<b>1.2</b>	<b>0.0</b>	<b>(0.2)</b>	<b>1.1</b>

The table below show the estimated and realised performance for each currency (market) transitioned.

**CHART I: ESITIMATE VS RESULT (COUNTRY)**



6.1

## Risk Management

LGIM forecasted a higher level of risk than we were initially comfortable with. LGIM still proposed a 40bps level of risk which believed to be high given the relatively liquid (short period) nature of the transition. To control intra-day exposure risk, LGIM managed the shift from Asia to UK by trading the Asia close with the UK open. Other markets were neutral. Given the transition primary shifts were Japan to UK, there does appear to be some evidence that LGIM did achieve some risk mitigation with lower than expected shortfall occurring in both countries. Slightly more disappointing was LGIM not being able to balance the neutral risk in the US, resulting in an IS £66k worse than estimated.

## Systems and Operations

There were no apparent issues relating to systems or operational failures, though we note that the constraints of the LGIM weekly dealing cycle, meaning that assets can only move between funds and transfer out to LCIV on Fridays, is less than ideal. Additionally, we note that the lead-time for LGIM requiring MSIM’s final wish list a week in advance of trading is long compared to some of LGIM’s competitor.

However we welcome the use of LGIMs CSUF fund to facilitate the transition and recognise that this had provided significant value-add to H&F, specifically the ability to remain invested and the facility not being subject to UK SDRT when moving from the legacy fund to the transition account.

We also believe that LGIM’s transition fees were higher than peers, but understand this is as a result of their fixed fee arrangement for CSUF use.

## Reporting & Communication

LGIM’s reporting was generally of a lower quality than we would normally expect. We highlighted on three occasions errors in their pre-trade report. Specifically, their liquidity analysis in their July report was incorrect and there were omissions in the August report. Importantly, this omission removed the line which represented the most illiquid name (Reckitt Benckiser). We also note that their pre-trade report provided no detailed liquidity analysis (e.g. worst names by ADV). Additionally, LGIM’s approach of representing Implementation Shortfall as

negative numbers differs from the T-charter approach and is possibly confusing to a client comparing this to competing proposals.

LGIM's post trade report lacks shortfall attribution and gives no comparison of estimate verses outcome (Chart 1 in this report generated by MJH).

Lastly, while team communications, expertise and responsiveness was good, LGIM seemed slightly confused about the role of LCIV and their respective sub-advisor.

## Score Card

Categories / Scores	1	2	3	4	5	Change
IS Result			✓			↘
Operational Performance			✓			↘
Communication		✓				↘
Compliance & Controls			✓			↘
Project Management			✓			↘
Trading & Crossing				✓		↘
Risk Management				✓		↘

1. A major failure occurred within with performance category
2. Some of the deliverables within this category were not executed to a satisfactory level
3. Most of the deliverables within this category were achieved as proposed
4. Most of the deliverables within this category were executed to a high standard
5. All of the deliverables within this category out-performed expectations

6.1



1 Fredrick's Place, London, EC2R 8AE, United Kingdom | +44 20 7079 1000 | [london@mjhudson.com](mailto:london@mjhudson.com) | [mjhudson.com](http://mjhudson.com) | [mjhudson-allenbridge.com](http://mjhudson-allenbridge.com)

This document is directed only at the person(s) identified on the front cover of this document on the basis of our investment advisory agreement. No liability is admitted to any other user of this report and if you are not the named recipient you should not seek to rely upon it.

This document is issued by MJ Hudson Allenbridge. MJ Hudson Allenbridge is a trading name of MJ Hudson Allenbridge Holdings Limited (No. 10232597), MJ Hudson Investment Advisers Limited (04533331), MJ Hudson Investment Consulting Limited (07435167), and MJ Hudson Investment Solutions Limited (10796384). All are registered in England and Wales. MJ Hudson Investment Advisers Limited (FRN 539747) and MJ Hudson Investment Consulting Limited (FRN 541971) are Appointed Representatives of MJ Hudson Advisers Limited (FRN 692447) which is Authorised and Regulated by the Financial Conduct Authority. The Registered Office of MJ Hudson Allenbridge Holdings Limited is 1 Fredrick's Place, London, EC2R 8AE.