



Border to Coast Pensions Partnership Ltd

Border to Coast Overseas Developed Equity Fund (“the Fund”)

Report for the Quarter Ended 31 December 2019
(for information)

Report to the Border to Coast Pensions Partnership Ltd Joint Committee
Date of Meeting: 9 March 2020

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Date: 17 February 2020

Purpose of Report

1. This report summarises the performance and activity of the Border to Coast Overseas Developed Equity Fund over Q4 2019.
2. The Committee is recommended to note this report.

Important Information

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Background

3. Border to Coast launched this internally managed Fund on 26th July 2018.
4. The Fund invests primarily in listed equities of companies from overseas developed countries which are included in the index.
5. The Fund has a quality and growth bias with a focus on companies that can withstand economic and market volatility. Quality is defined as companies with an identifiable and sustainable competitive advantage, earnings visibility, balance sheet strength and strong management.
6. The Fund will not generally make active regional allocation decisions so most of the Fund's performance will arise from stock selection.
7. The majority of the Fund's performance is expected to arise from stock selection decisions.

Performance Objective

8. The Fund's objective is to outperform its Benchmark by at least 1% per annum over three year rolling periods. The Benchmark is a composite of the following regional indices:
 - 40% S&P 500 (US)
 - 30% FTSE Developed Europe ex UK
 - 20% FTSE Developed Asia Pacific ex Japan
 - 10 FTSE Japan
9. The Fund aims to provide a benchmark tracking error relative to the Benchmark of between 1% to 3% depending on market conditions. This is considered to be an appropriate risk profile in view of the performance target.

Market Value

10. The Fund's market value at the quarter end was £3bn.

Performance

11. Performance (net of fees) to the quarter end is shown below:

	Since inception 26/07/18 % p.a.	Year %	Quarter %
Overall Fund	7.11	21.77	1.32
Benchmark	6.22	20.02	0.90
Actual Variance ¹	+0.88	+1.75	+0.43
Target Variance ²	+1.00	+1.00	+0.25
Performance Relative to Target ³	-0.12	+0.75	+0.17

¹ Fund performance minus Benchmark performance

² Based on the Fund's Performance Objective

³ Actual Variance minus Target Variance

* Values do not always sum due to rounding

Note

1. Source: Northern Trust
2. Values do not always sum due to rounding
3. Performance is net of ACS charges such as depository and audit fees. Investment management fees have not been included in the performance calculations.
4. Past performance is not an indication of future performance and the value of investments can fall as well as rise.

Comments on Performance

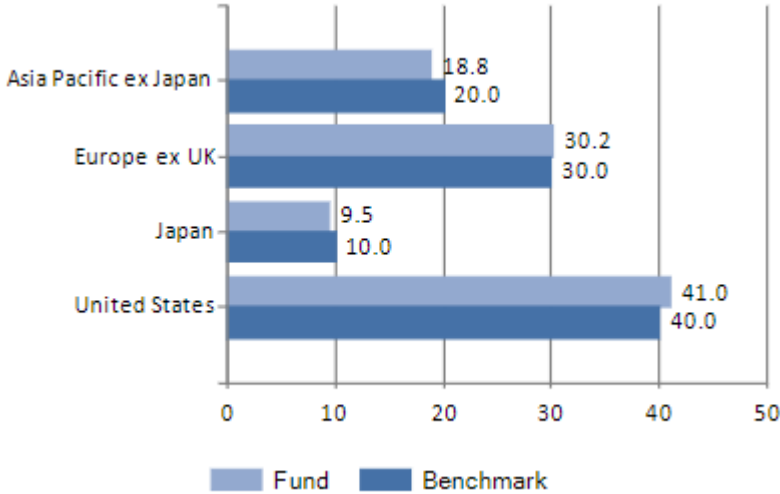
12. Overall Fund performance was above its target over Q4 2019 and is above Benchmark since inception.
13. The performance of the individual regional sleeves of the Fund over Q4 was as follows:
 - US: Fund 1.70% vs Benchmark of 1.29%
 - Japan: Fund 0.91% vs Benchmark of 0.21%
 - Europe ex UK: Fund 0.70% vs Benchmark of 0.81%
 - Asia Pacific ex Japan: Fund 1.68% vs Benchmark of 0.46%
14. Tentative improvement in the trade relations between the US and China had a beneficial impact on export-oriented countries (e.g. Germany, Japan etc.) and sectors (e.g. Industrials, Technology etc.).
15. Some signs of stabilisation and expectations of a recovery in the Technology sector, driven by an unwinding of excess inventory and positive consumer responses to new products – e.g. Galaxy Note 10, iPhone 11.
16. The reversal of the inversion of the US yield curve and reduced expectations of a recession, resulting in an improvement in investor sentiment.
17. A developing global trend of an improvement in the relative performance of value stocks which have under-performed quality stocks significantly over the last decade and are now valued at a substantial discount. The sub-fund is typically over-weight quality stocks and so a continuation of this trend could have a detrimental impact on performance, although there have been a number of false dawns in the past.
18. The top and bottom 5 contributors to performance over the quarter were:

Fund	Portfolio weight (%)	Benchmark weight (%)	Contribution to performance (%)	Commentary
NVIDIA Corporation (o/w)	0.51	0.22	0.06	Benefitted in general improvement in semiconductor stocks
Nokia (u/w)	0.00	0.09	0.04	Cut profit guidance and halted dividend pay outs
UnitedHealth Group (o/w)	0.57	0.42	0.03	Improved political sentiment, plus solid results
CSL (o/w)	0.92	0.66	0.03	Shares out-performed due to solid results
HBM Healthcare (o/w)	0.36	0.00	0.03	Out-performed on the back of successful fundraising
Constellation Brands (o/w)	0.33	0.05	-0.04	Investor disappointment on softening of business disposal plans
Vanguard US Mid Cap ETF (o/w)	2.94	0.00	-0.04	Mid-cap under-performed S&P 500 by 2% over quarter
Home Depot (o/w)	0.66	0.36	-0.04	Concerns that recent weak results may indicate deeper problems
McDonalds Corp (o/w)	0.43	0.22	-0.04	Sudden departure of CEO not well received
Kering (u/w)	0.00	0.21	-0.03	Quarterly results better than expected

Source: Northern Trust & Border to Coast

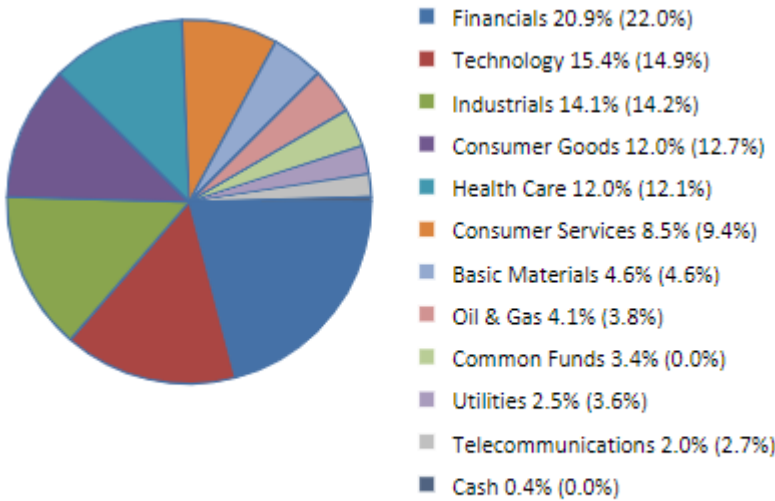
Portfolio Structure

19. The regional breakdown of the Fund and Benchmark, at the quarter end, is set out below:



Source: Northern Trust

20. The sector breakdown of the Fund and Benchmark, at the quarter end, was:



Note: The pie-chart shows the sector allocation of the Fund with the Benchmark sector allocation shown in brackets.

Source: Northern Trust

21. Notes:

- Common Stock Funds (+) – exposure to smaller companies via collective vehicles, in US, Europe and Japan.
- Technology (+) – long-term structural growth drivers including Internet of Things, Artificial Intelligence, Electric/Autonomous vehicles, new generation memory chips.

- Oil and Gas (+) – relatively defensive sector, valuations significantly below the long-term average and strong free cash flow generation, enabling increased shareholder distributions.
- Consumer Services (-) – concerns over consumer spending and continuing structural shift to on-line retail.
- Utilities (-) – pressure from increased capital investment, changes in government policy and increased regulatory risk are having an adverse impact on “traditional” power generation companies.
- Financials (-) – under-weight in Banks due to concerns over profitability, non-performing loans, legacy litigation issues and regulation risk.

22. During the quarter, the largest individual transactions were:

- Vanguard Mid-Cap ETF (+14.1m) – reducing the Fund’s underweighting of smaller US companies.
- Allergan (-£8.3m) – realising gains following takeover approach – proposed merged entity isn’t compelling.

Risk Profile

23. The risk profile of the Fund is monitored on an ex-post (forward looking) and ex-ante (backward looking) basis using data from the fund custodian, Northern Trust, for ex-post, and Bloomberg for ex-ante.

24. Both the ex-post and ex-ante tracking error as of quarter end are below target, standing at 0.63% and 0.56% respectively.

Market Background

25. Global economic growth has continued to soften during the quarter, although leading indicators have shown some signs of stabilisation

26. The recent positive developments in the various trade disputes have reduced uncertainty for export-oriented economies in both developed and emerging regions

27. In the UK, the outcome of the recent election has removed a large part of the uncertainty surrounding Brexit.

28. Global inflation remains low, wage growth appears contained and interest rate expectations fallen.

29. There has been a modest appreciation in global equity markets (MSCI ACWI) with a total return of 1.1% (in sterling terms) during the quarter. Developed markets (+0.7%) underperformed Emerging Markets (+3.5%)

30. Value stocks failed to maintain their previous quarter’s out-performance of quality stocks and momentum stocks continued to under-perform.

31. We are long-term investors - aiming to ignore short-term noise and focus on long term company fundamentals.