

ABERDEEN CITY COUNCIL

COMMITTEE	City Growth & Resources
DATE	3 February 2021
EXEMPT	No
CONFIDENTIAL	No
REPORT TITLE	Strategic Infrastructure Partnership with North East Scotland Pension Fund
REPORT NUMBER	RES/21/049
DIRECTOR	Steve Whyte
CHIEF OFFICER	Jonathan Belford
REPORT AUTHOR	Jonathan Belford
TERMS OF REFERENCE	3.2 and 3.3

1. PURPOSE OF REPORT

- 1.1 At its meeting of 7 February 2019, the Committee agreed to instruct the Chief Officer – Finance to explore the opportunities for a strategic partnership between the Council and the North East Scotland Pension Fund (NESPF) for the purposes of supporting local infrastructure investment, and report back on the feasibility. The purpose of the report is to address that instruction.

2. RECOMMENDATION(S)

That the Committee: -

- 2.1 Notes the content of the report and instruct the Chief Officer – City Growth to report back to the Committee on the methodology and approach to bring investor ready proposals to the market, including resource implications and timescales for developing the opportunities described within the various economic and infrastructure strategies.

3. BACKGROUND

- 3.1 In investment terms ‘infrastructure’ is a broad asset class.

The definition of Infrastructure

‘The basic facilities, services and installations needed for the functioning of a community or society, such as transportation and communications systems, water and power lines and public institutions including schools, post offices and prisons’

Infrastructure Sectors;

Transport	– roads, airports and ports.
Utilities	– water, electricity and gas grids
Telecommunications	– fibre and broadcast towers
Social	– hospitals, schools and prisons

Renewable Energy – wind, solar, hydro and biomass

- 3.2 In general the Government is responsible for providing infrastructure services to the community, Government however may discharge its responsibility directly or outsource to the private sector. In addition, the private sector may provide infrastructure services if market conditions are right.
- 3.3 While responsibility rests with Government, infrastructure services can be paid for in different ways, for example from general tax revenues or under ‘user pay’ arrangements.
- 3.4 With ageing infrastructure, increasing demand and new innovations investment in infrastructure throughout the UK is in high demand, with public and private sector joining forces to deliver on expectations across national and local plans.
- 3.5 Locally investment is sought for Aberdeen’s strategic infrastructure priorities identified in the Regional Economic Strategy, City Region Deal and the City Centre Masterplan. Most recently, in May 2020, the Council’s Urgent Business Committee approved the Net Zero City Vision for Aberdeen and a Strategic Infrastructure Plan – Energy Transition to support delivery of the vision, that in turn is attracting external funding.
- 3.6 There are limitations on what the NESPF can invest in. The Pensions Committee was advised in the Strategic Infrastructure Priorities and the Scottish Local Government Pension Scheme report (PC/MAR19/INFRA) that there are some legal restrictions for the NESPF investing directly in Aberdeen City Council capital programme. This followed NESPF having reviewed the option to invest in the Aberdeen City Council Bond, when due diligence and legal advice was clear that the Pension Fund was prevented from participating due to the Pensions Act 1995 Section 40 which restricts employer-related investments.
- 3.7 However, the ambition set out in the Regional Economic Strategy and the Net Zero City Vision for example, and the delivery of infrastructure needed to support a globally competitive city region economy, goes much further than simply a Council being the funder of infrastructure. Both recognise the role of the UK Government and the Scottish Government in responding to market failure and developing a mix of opportunities for a range of stakeholders, either in the public or private sector. This is not without its challenges.

Infrastructure Asset Allocation

- 3.8 The Investment Strategy of the NESPF has a Strategic Asset Allocation in relation to Infrastructure, and at time of writing is underweight in terms of capital deployed, this means there is scope for infrastructure investments to be considered by the Fund. The Pension Fund requires investor ready projects, that have a clear business case and fully prepared offer to the market for any investment to be considered. With this available, investment assessment and due diligence work can be carried out to inform recommendations to the Pensions Committee.
- 3.9 This indicates the NESPF has potential for investment in this asset class.

The challenges of infrastructure investment

- 3.10 Not every infrastructure investment opportunity is going to fit the needs of every investor, there are challenges to be overcome.
- 3.11 Infrastructure's economic characteristics can lead to attractive investment opportunities, such as stable and steady cash flows, being non-cyclical or having low variable costs but not all display the same characteristics.
- 3.12 In response to and recognising the 'public good' argument, providing essential services by infrastructure assets requires government / community involvement and as such;
- Incorporates an explicit or implied cap on returns, resulting in greater emphasis on initial investment assessment, robust valuation and ongoing management.
 - Requires responsible and informed long term investing and effective governance.
- 3.13 Whilst infrastructure investments can display lower volatility they are not immune to economic cycles.
- 3.14 Private investment in infrastructure assets is relatively immature and as such there is no readily available access route for non-specialist investors. Also, the regulatory and/or contractual complexity that tend to accompany such investments also act as a high barrier to entry for non-specialist investors.
- 3.15 Mitigating some of the challenges can be achieved by taking significant care and judgement to match opportunities to risk/return requirements. Selecting an access route that delivers an outcome in line with expectations, delivering on not only return but governance.

A Strategic Partnership with NESPF

- 3.16 At its meeting of 11 December 2020 the Pension Committee considered the matter of a Strategic Partnership and noted that the investment environment was not yet ready for this. For an effective and productive partnership additional work in the City Region area was needed to move investment opportunities forward to being investor ready, and ideally for a pipeline of opportunities to emerge.
- 3.17 The Pension Committee determined that it could not yet enter a strategic partnership and agreed that the Pension Manager maintain a watching brief on the development of investor ready opportunities in the City Region area.
- 3.18 With this in mind and combined with the clear intent included in, for example, the Regional Economic Strategy and Strategic Infrastructure Plan – Energy Transition there are investment opportunities that will need funding. As those proposals become more developed the Council should establish how investor ready opportunities are created brought to the market for investment, including how the NESPF can be an active partner.

3.19 Currently development opportunities, those looking for capital investment are promoted by developers and industry to potential investors. Since 2017/18, wider opportunities, including those being led by the public sector, are being developed and promoted locally and regionally through the collaboration by Invest Aberdeen; working with the Investment Promotion Team at Scottish Cities Alliance, and recently with institutional investor teams in both the UK Government and the Scottish Government. This generally requires evidence and information including:

- Concept – e.g. sector, type of development
- Funding;
- Ownership, consents and approvals;
- Type of investment sought – e.g. financial, ‘special purpose vehicle’, co-investment, expertise;
- Rate of return.

3.20 Bearing this wider approach in response to the Regional Economic Strategy (RES) and City Region Deal projects, and building on the track record the Council has in attracting investment in its commercial projects, it is therefore recommended that the Chief Officer – City Growth reports back to the Committee with more detail on the approach and methodology required to bring investor ready investments to the market, including resource implications and timescales for developing the opportunities described within the various economic and infrastructure strategies. This will reflect that some of these projects are not at this stage ‘investor ready’ in being able to provide the requisite information for investors, but will highlight those that are being focused on in the short term, particularly around energy transition, the city centre, and economic recovery.

4. FINANCIAL IMPLICATIONS

4.1 There are no financial implications arising directly from this report.

5. LEGAL IMPLICATIONS

5.1 Legal advice was sought in relation to the NESPF investing in the Aberdeen City Council bond issue as mentioned in the report. There are no legal implications arising directly from this report.

6. MANAGEMENT OF RISK

6.1 There are no issues arising directly from this report, however the management of risk is a vital component of the governance and due diligence in relation to actual investment decisions.

7. OUTCOMES

COUNCIL DELIVERY PLAN	
Regional and City Strategies	The proposals in this report support the Regional Economic Strategy and Net Zero City Vision by focusing on developing investor ready opportunities for the market. This supports the Innovation, Infrastructure and Internationalisation programme areas directly, and, indirectly for some projects, creating jobs and supporting Inclusive Growth.

8. IMPACT ASSESSMENTS

Assessment	Outcome
Impact Assessment	Full impact assessment not required
Data Protection Impact Assessment	Not required

9. BACKGROUND PAPERS

None

10. APPENDICES

None

11. REPORT AUTHOR CONTACT DETAILS

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