Croydon Council

REPORT TO:	**PENSION COMMITTEE** **19 September 2023**
AGENDA ITEM:	
SUBJECT:	**Part A -Progress Report for Quarter Ended 30 June 2023**
LEAD OFFICER:	**Matthew Hallett** **Head of Pensions and Treasury**
CORPORATE PRIORITY/POLICY CONTEXT: **Sound Financial Management**: Reviewing and ensuring that the performance of the Council's Pension Fund (the Fund) investments are in line with their benchmark and in line with the assumptions made by the Actuary.	
FINANCIAL SUMMARY: This report shows that the market value of the Fund investments as at 30 June 2023 was £1,701.7m compared to £1,674.2m at 31 March 2023, an increase of £27.5m and a return of 1.75% over the quarter. The performance figures, independent information and analysis on the fund managers and markets have been provided by the Fund's independent investment advisor Mercer and are included in the part B report.	
FORWARD PLAN KEY DECISION REFERENCE NO.: N/A	

1 RECOMMENDATIONS

1.1 The Committee is asked to note the performance of the Fund for the quarter ended 30 June 2023.

2 EXECUTIVE SUMMARY

2.1 This report provides an update on the Fund's performance for the quarter to 30 June 2023. The report falls into four parts. Section 1 addresses performance against strategic goals. The second section considers the asset allocation strategy and how that is being applied, specifically current and planned investments. The third section deals with risk management and the fourth and final section summarises the recent investment manager site visit.

3 DETAIL

Section 1: Performance

3.1 At the 2022 Triennial Actuarial Valuation funding position for the Fund was 97% using a future investment return assumption (otherwise described as the discount rate) of 4.0% p.a. The Fund would be 100% funded if an assumed investment return of 4.2% p.a. was used and the likelihood of achieving this investment return was deemed to be 73%. In setting the Pension Fund's investment strategy, performance is measured against a benchmark return of CPI + 4% for the whole fund. Achieving this benchmark return will ensure the investments achieve a higher return than as calculated in the valuation and on the basis that other assumptions remain constant, the funding gap will close.

3.2 At the 2019 valuation date the Fund was 88% funded with assets totalling £1,258m. From the 2019 valuation to the 2022 valuation the funding position improved to 97%. The main reason for this improvement was due to investment returns being 23.9% (or £299m) higher than expected. The assets at the valuation date of 31 March 2022 were £1,731m.

3.3 Since the valuation date the assets have returned -0.73% compared to the investment return assumption of 5.0%. In isolation the investment returns have had a negative impact on the funding level. However it should be noted that this would be outweighed by a positive impact due to a decrease in liabilities under current market conditions.

Section 2: Asset Allocation Strategy

3.4 Following the results of the triennial valuation at 31 March 2022, the Fund's investment advisers have carried out an asset allocation review and a revised asset allocation was agreed at the Pension Committee held on 20 June 2023. The Pension Committee also agreed that an allocation to Private Debt maybe added at a later date after further training on this asset class has been undertaken. The revised asset allocation will be incorporated into the Investment Strategy Statement. The revised allocation agreed was as follows:

Asset Class	Previous Strategic Asset Allocation	Actual Allocation 31 March 2023	New Allocation without Private Debt Strategy 1
Developed Equity	**42.0%**	**44.7%**	**42.0%**
Fixed Income	**23.0%**	**15.7%**	**23.0%**
Corporate Bonds	*15.3%*	*11.9%*	*17.0%*
Absolute Return	*7.7%*	*3.8%*	-
Multi-Asset Credit	-	-	*6.0%*
Alternatives	**34.0%**	**36.8%**	**34.0%**
Infrastructure	*10.0%*	*14.8%*	*12.0%*
Private Equity	*8.0%*	*10.0%*	*10.0%*
Private Debt	-	-	-
Property (Core & Residential)	*16.0%*	*12.0%*	*12.0%*
Cash	**1.0%**	**2.8%**	**1%**
Total	**100.0%**	**100.0%**	**100.0%**

3.5 In moving to the revised asset allocation Officers will first look at the London CIV's multi asset credit fund to see if it meets our requirements. The process of moving to the revised asset allocation will take place over the next year.

Monitoring of asset allocation

3.6.1 **Global Equity –** Global equities rose over the quarter, led by the technology sector, amid optimism that US inflation may continue to fall without a significant rise in unemployment. US and Japanese equities performed strongly over the quarter and European equities were positive. UK equities were negative due to the bias towards commodity companies. Sterling rose against the major currencies due to higher for longer interest rate expectations in the UK. This all led to a positive return of 5.55% for the LGIM Developed World (ex-Tobacco) Equity fund which follows that of the major indices. The currency hedged part contributed 7.18% while the unhedged part contributed 3.98% due to the strengthening of Sterling. The LCIV RBC fund again suffered due to its stock selection and returned -0.06% for the quarter. The LCIV RBC fund has performed slightly below its benchmark (11.68% compared to 14.77%) since its inception on 16/04/2020.
Global equities are now at 46.2% compared to the target allocation of 42%.

3.6.2 **Fixed Interest** – During the quarter fixed interest investments suffered due to sticky inflation increasing the expectations of interest rates staying higher for longer. The fixed interest portfolio returned a negative return of -2.1%, with Aberdeen Standard -1.72%, Wellington -6.17% and the LCIV Global Bond 0.09%. The Wellington portfolio suffered in particular because of its overweight to US duration position.

The overall allocation was 15.1% of the portfolio, remaining outside the target allocation of 23% allowing for a 5% tolerance. This is largely due to the poor performance of bonds when compared to the other asset classes. Given the continued uncertainty Officers have continued in not rebalancing the Fund with the view to waiting for the outcome of the strategic asset allocation.

3.6.3 **Infrastructure** – Due to the nature of these assets, performance of Infrastructure investments and indeed Private Equity, discussed in more detail below, is better measured over a period of time, rather than quarter by quarter. All the Fund's Infrastructure investments continue to perform well largely due to their link to inflation. The allocation currently stands at 14.1% compared to the revised target of 12%.

3.6.4 **Private Equity** – Our Private Equity managers continue to perform extremely well and have been the main contributor to positive returns over the last few years. During the last quarter the valuations have come down mainly due to the currency effect. All the private equity assets are valued in currencies other than Sterling, so valuations suffer when Sterling appreciates. The performance of the underlying companies remains strong and so there is currently no cause for concern. Over the quarter the allocation moved from 10.0% to 9.5%. This is slightly below the target allocation of 10%.

3.6.5 **Property** – During the quarter the Schroders property portfolio returned 1.26% and the M&G UK Residential Property Fund returned 1.3%. Despite the positive returns for the quarter the outlook for 2023 for the property sector will remain challenging due to the continued higher interest rate expectations. The Fund's property portfolio is positioned defensively being underweight to retail and office sectors. The allocation to property is 12.0% which is in line with the new target asset allocation of 12.0%.

3.6.6 The table below illustrates the movement in the Fund's valuation during the quarter and the current asset allocation against the target.

London Borough of Croydon Pension Fund
Fund valuation and asset allocation for the quarter ending 30 June 2023

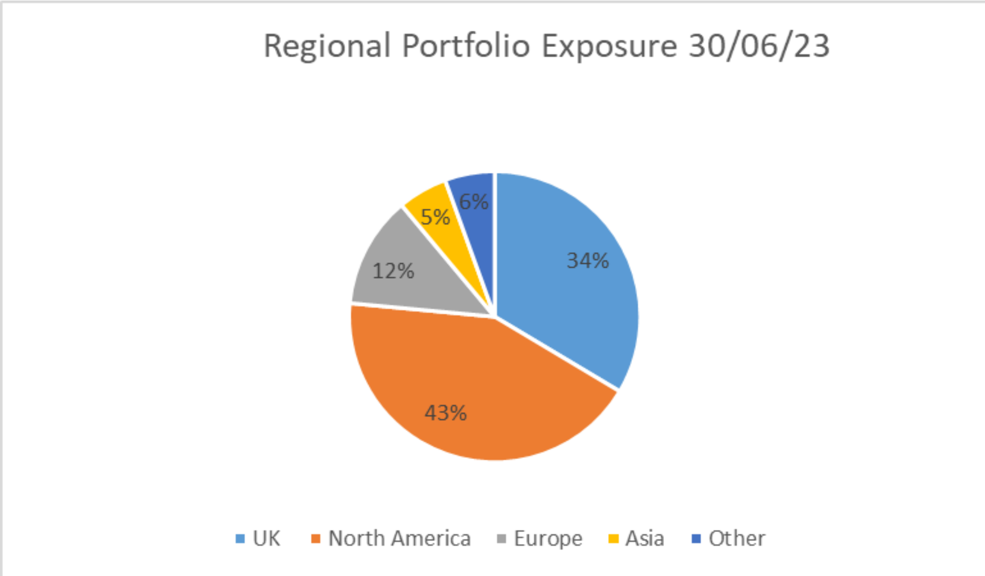
	Valuation at 31/03/23 £'000	Net cashflow £'000	Gain/Loss £'000	Valuation at 30/06/2023 £'000	Asset allocation Fund percentage	Asset allocation target percentage
Equities					46.2%	42%
Legal & General FTSE World (Ex Tobacco)	670,863	-	37,245	708,107		
LCIV RBC	77,964	-	- 49	77,915		
LCIV	150			150		
Fixed Interest					15.1%	23%
Standard Life	123,066	-	- 2,122	120,944		
Wellington	57,336	-	- 3,539	53,798		
LCIV Global Bond	81,804	-	72	81,876		
Infrastructure					14.1%	12%
Access	36,566	1,001	169	37,736		
Temporis	78,622	1,386	120	80,128		
Equitix	78,630	- 5,558	- 302	72,769		
Macquarie GIG Renewable Energy	23,268	- 742	- 1,238	21,288		
I Squared	30,312	- 1,263	- 275	28,774		
Private Equity					9.5%	10%
Knightsbridge	60,676	102	- 1,603	59,176		
Pantheon	70,767	- 1,836	- 1,452	67,479		
Access	14,864	-	441	15,305		
North Sea	20,465	-	- 688	19,777		
Property					12.0%	12%
Schroders	137,845	-	1,741	139,586		
M&G	63,576	- 324	823	64,075		
Cash					3.1%	1%
Legal & General FTSE4Good Cash	955	-	- 9	946		
Cash	46,424	5,477	-	51,901		
Fund Total	1,674,154	- 1,757	29,335	1,701,733	100%	100%

Valuations are based on the bid price as reported by the Fund Managers. The valuations of the Infrastructure and Private Equity funds are the latest available and can be lagged by 3 months.

3.7 Regional Exposure

3.7.1 The Committee asked for an indication of the geographical dispersion of the underlying assets comprising the portfolio. This is set out graphically in the chart below. This information is for illustrative purposes only. It should be noted that there are differences in the period represented as some data is updated far more frequently than others.

Graph 2: Geographic dispersion of funds.



3.7.2 The descriptor Asia includes Japan, Korea and Australia. The descriptor Other includes the continent of Africa and Latin America.

3.8.3 It should be noted that of the 34% invested in the UK 12.0% is allocated to Property and 10.4% to Infrastructure. The majority of the Private Equity and Global Equity investments are in the US and Canada.

3.8 Section 3: Risk Management

3.8.1 The main risk addressed by the Funding Strategy is that returns on investment will fall below the target asset outperformance assumption to ensure that the Pension Fund matches the value of liabilities in the future. Dependent upon that are of course a number of issues.

3.8.2 The global economy will always represent a specific risk and opportunity for the Fund and will effectively be impossible to quantify or evaluate. The Fund takes a long-term view and manages risk by investing in a portfolio of assets which is sufficiently diversified. Having a sufficiently diversified portfolio should ensure the Fund continues to meet its performance objectives over the long term while reducing the impact of short term volatility in caused by uncertainty in global markets.

3.8.3 Mercer, the Fund's investment adviser, have drafted a Fund Monitoring Report, for the 3 months to 30 June 2023. These reports are included in Part B of this Committee agenda.

3.9 Section 4: Investment Manager Visits

3.9.1 No meetings with managers were held over the quarter.

4 CONSULTATION

4.1 Officers have fully consulted with the Pension Fund's advisers in preparing this report.

5 FINANCIAL CONSIDERATIONS

5.1 This report provides an update on the investment of the Council's Pension Fund, including the value of investments to fund future liabilities and the allocations between different asset classes to diversify risk, maximise return and ensure necessary liquidity. The report notes that at the 2022 Triennial Actuarial Valuation, the funding position for the Pension Fund was 97% using a future investment return assumption (otherwise described as the discount rate) of 4.0% p.a.

Approved by: Allister Bannin on behalf of Jane West, Corporate Director of Resources (Section 151 Officer)

6. LEGAL CONSIDERATIONS

6.1 Burges Salmon LLP (a legal advisor appointed to the Pension Fund) comments that there are no direct legal implications arising from the recommendations within this report.

6.2 The Committee must, however, be mindful of their fiduciary duty to make investment decisions including in the best long-term interests of Pension Fund beneficiaries and taxpayers within the investment strategy framework.

7. HUMAN RESOURCES IMPACT

7.1 There are no direct workforce implications arising from the recommendations within this report. If any should arise these will be managed under the Council's policies and procedures.

Approved by: Gillian Bevan**,** Head of HR, Resources and Assistant Chief Executives directorates on behalf of the Chief People Officer Date: 5.9.23

8. EQUALITIES IMPACT

8.1 The Council has a statutory duty to comply with the provisions set out in the Sec 149 Equality Act 2010. The Council must therefore have due regard to:

(a) eliminate discrimination, harassment, victimisation and any other conduct that is prohibited by or under this Act.

(b) advance equality of opportunity between persons who share a relevant protected characteristic and persons who do not share it

(c) foster good relations between persons who share a relevant protected characteristic and persons who do not share it.

8.2 Any risks to the investment fund are likely to impact on the age characteristic in relation to older workers. The council is 67.73% female and 32.27% male so therefore women are more likely to be impacted by any investment risks.

Approved by: Naseer Ahmad **for** Equality Programme Manager, (08/09/2023)

9. ENVIRONMENTAL IMPACT

9.1 There are no environmental impacts arising from this report.

10. CRIME AND DISORDER REDUCTION IMPACT

10.1 There are no crime and disorder impacts arising from this report.

11. FREEDOM OF INFORMATION/DATA PROTECTION CONSIDERATIONS

11.1 This report and Appendices contain confidential information which could be of a sensitive nature, disclosure of which could prejudice the commercial interest of the companies involved and those of the Council's Pension Fund and will be reported in the closed part of the agenda. On application of the public interest test it is considered that the public interest in maintaining the exemption outweighs the public interest in disclosing the information.

Approved by: Allister Bannin on behalf of Jane West, Corporate Director of Resources (Section 151 Officer)

CONTACT OFFICER:

Matthew Hallett, Acting Head of Pensions and Treasury,

BACKGROUND DOCUMENTS:

Included in Part B of the agenda.
Quarterly reports from each fund manager (circulated under separate cover to the Committee Members.) Exempt pursuant to Schedule 12A paragraph 3 of the Local Government Act 1972 as amended.

Appendices:

There are no part A appendices.

Part B appendices:

Exempt pursuant to Schedule 12A paragraph 3: Information relating to the financial or business affairs of any particular person (including the authority holding that information), the following appendices are considered to be precluded from publication:

Appendix A: London Borough of Croydon Returns to 30 June 2023, Mercer

Appendix B: Market Background and Market View Q2 2023, Mercer