

Croydon Council

REPORT TO:	PENSION COMMITTEE 6 December 2022
SUBJECT:	Part A -Progress Report for Quarter Ended 30 September 2022
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 September 2022 was £1,614m compared to £1,633.8m at 30 June 2022, a decrease of £19.8m and a return of -1.22% 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 September 2022.

2 EXECUTIVE SUMMARY

- 2.1 This report provides an update on the Fund's performance for the quarter to 30 September 2022. 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 2019 Triennial Actuarial Valuation the whole of fund funding position was 88% 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 4.8% p.a. was used. 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 Since the valuation date the Fund has made a cumulative return of 29.6% against a return of 14.7% assumed by the valuation. This has had a positive impact on the funding level and the Funding level at 31 March 2022 was estimated to be 97%.

Section 2: Asset Allocation Strategy

- 3.3 The Pension Committee discussed changes to the current asset allocation strategy at the Committee meeting held on 17 March 2020 (Minute A27/20 refers). However, reviewing the current allocation it is apparent that the target allocation cannot yet be applied as it has not been formally adopted because, as per the Minute – "Officers pointed out that they were not able to give investment advice and the Pension Fund's investment adviser had not been given the opportunity to offer appropriate advice to inform the decision." The prudent option is therefore to measure allocation against the prior allocation. This option is supported by the Scheme's investment advisors. Any proposal to amend this asset allocation will require a period of consultation with such persons as it considers appropriate.

3.4 The target portfolio can be broken down as follows:

Asset Class		Target Allocation	Allowable Tolerance
Equities including allocation to emerging markets.		42%	+/- 5%
Fixed interest		23%	+/- 5%
Alternates		34%	+/- 5%
<i>Comprised of:</i>			
Private Equity	8%		
Infrastructure	10%		
Property	16%		
Cash		1%	
Total		100%	

3.5 Monitoring of asset allocation

3.5.1 **Global Equity** – Global equities continued to perform poorly in the last quarter, with high levels of volatility. The two most dominant themes of the previous two quarters continued to be high inflation and the tightening of monetary policy. All the major indices showed a negative return over the quarter.

The Fund's Global equity return for the quarter was -1.03%. The LGIM Developed World (ex-Tobacco) Equity fund returned -1.43% as it follows that of the major indices. The LCIV RBC fund performed positively returning 2.13% for the quarter. Global equities are now at 42.4% compared to the target allocation of 42%.

3.5.2 **Fixed Interest** – Fixed interest investments continued on the downward path posting a negative return of -6.9%, with Aberdeen Standard -5.42%, Wellington -12.98% and the LCIV Global Bond -4.43%. The protection offered by the Aberdeen Absolute Return Fund shielded the loses slightly.

The quarter saw two more aggressive interest-rate hikes by the Federal Reserve and at its September policy meeting showed no signs of slowing down its aggressive stance. This led to further increases in gilt yields which resulted in the negative returns for the fixed interest portfolio. The overall allocation is 15.5% which is 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 elected not to rebalance the Fund with the view to waiting for the outcome of the strategic asset allocation review which will be conducted over the coming months.

3.5.3 **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 renewable investments have performed particularly well recently due to increased inflation expectations and increases in power prices, both of which have a positive impact on the returns. The allocation currently stands at 14.0% compared to a target of 10%.

3.5.4 **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. The performance of private equity investments tends to follow the same direction as global equities. Valuations tend to be lagged so Officers are expecting the positive returns

to tail off although the majority of our private equity investments are priced in foreign currency so the weakness in Sterling has contributed to inflated valuations. Over the quarter the allocation moved from 11.8% to 11.6%. This is above the target allocation of 8%.

3.5.5 **Property** – The Property allocations performance has started to struggle. Although the performance over the last year has been strong. The property allocation now makes at 13.7% of the Fund. The recent negative returns in equities and bonds demonstrate the value of a property portfolio as a diversifier and risk mitigator within the overall Fund’s portfolio.

3.5.6 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 September 2022

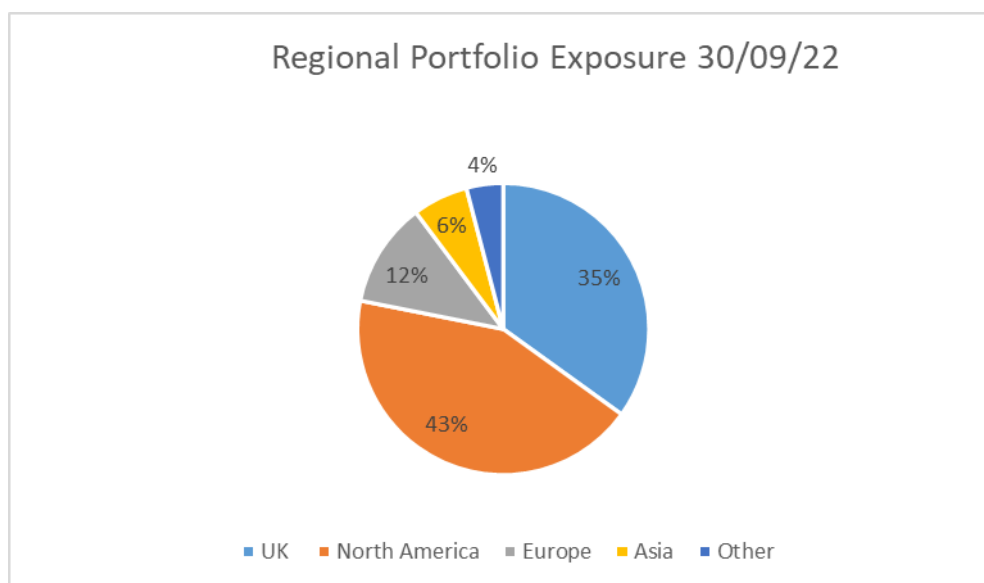
	Valuation at 30/06/2022 £'000	Net cashflow £'000	Gain/Loss £'000	Valuation at 30/09/2022 £'000	Asset allocation Fund percentage	Asset allocation target percentage
Equities					42.4%	42%
Legal & General FTSE World (Ex Tobacco)	614,043	-	8,784	605,259		
LCIV RBC	77,232	-	1,643	78,875		
LCIV	150			150		
Fixed Interest					15.5%	23%
Standard Life	126,094	-	6,838	119,256		
Wellington	62,102	-	8,063	54,039		
LCIV Global Bond	81,110	-	3,597	77,514		
Infrastructure					14.0%	10%
Access	32,788	2,750	2,192	32,230		
Temporis	56,839	-	350	57,189		
Equitix	75,141	574	4,085	78,652		
Macquarie GIG Renewable Energy	24,013	472	-	23,541		
I Squared	29,905	1,443	3,144	34,491		
Private Equity					11.6%	8%
Knightsbridge	75,212	649	314	74,877		
Pantheon	74,993	1,144	3,364	77,213		
Access	25,584	6,265	3,669	15,649		
North Sea	17,518	648	1,305	19,471		
Property					13.7%	16%
Schroders	162,326	-	6,378	155,948		
M&G	64,788	206	1,123	65,705		
Cash					2.7%	1%
Legal & General FTSE4Good Cash	741	-	174	567		
Cash	33,238	10,086	-	43,325		
Fund Total	1,633,817	116	19,982	1,613,951	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.

3.6 Regional Exposure

3.6.1 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.



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

3.6.3 It should be noted that of the 36% invested in the UK 13.7% is allocated to Property and 9.7% to Infrastructure. The majority of the Private Equity and Global Equity investments are in the US and Canada.

3.7 Section 3: Risk Management

3.7.1 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.

3.7.2 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.

3.7.3 Mercer, the Fund's investment adviser, have drafted a Fund Monitoring Report, for the 3 months to 30 September 2022. These reports are included in Part B of this Committee agenda.

3.8 Section 4: Investment Manager Visits

3.8.1 There were no manager meetings held in 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 deals exclusively with the investment of the Council's Pension Fund and compares the return on investment of the Fund against the benchmark return.

Approved by: Alan Layton 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 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 on behalf of the Chief People Officer

8. EQUALITIES IMPACT

8.1 There are no equality implications arising from the report. .

Approved by: Denise McCausland Equality Programme Manager

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.

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 September 2022, Mercer

Appendix B: Market Background and Market View Q3 2022, Mercer