

Croydon Council

REPORT TO:	PENSION COMMITTEE 14 March 2023
SUBJECT:	Part A -Progress Report for Quarter Ended 31 December 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 31 December 2022 was £1,620.9m compared to £1,614m at 30 September 2022, an increase of £6.9m and a return of 0.17% 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 31 December 2022.

2 EXECUTIVE SUMMARY

- 2.1 This report provides an update on the Fund's performance for the quarter to 31 December 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 funding position for the Fund 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 2019 valuation date the Fund has made a cumulative return of 29.6% against a return of 15.9% 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 Fund's investment advisers. Following the results of the triennial valuation at 31 March 2022, the Fund's investment advisers are now conducting an asset allocation review in consultation with the Pension Committee.

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** – The performance of Global equities in general stabilized during the quarter due to a more positive outlook for interest rates and China. This led to a positive return of 4.5% for the LGIM Developed World (ex-Tobacco) Equity fund which follows that of the major indices. The LCIV RBC fund did not benefit from markets rebounding from October lows and returned -0.8% for the quarter. This was mainly due to stock selection within the financial sector and specific consumer and health care stock picks. The LCIV RBC fund has still performed slightly above its benchmark (14.14% compared to 14.06%) since its inception on 16/04/2020.

Global equities are now at 43.8% compared to the target allocation of 42%.

3.5.2 **Fixed Interest** – During the quarter fixed interest investments started to recover with a positive return of 2.7%, with Aberdeen Standard 2.3%, Wellington 3.8% and the LCIV Global Bond 2.4%. Positive returns were experienced during the quarter as bond markets rallied in November amid investor expectations that inflation will be range bound at lower levels than previously anticipated.

The overall allocation increased to 15.9% which is still 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 review which is being 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. During the last quarter the valuations have come down as they tend to follow the direction of global equities, however the performance of the underlying companies remains strong and so there is currently no cause for concern. The majority of the Fund's

private equity investments are priced in foreign currency and so the weakness in Sterling has limited the drop in valuations to some extent. Over the quarter the allocation moved from 11.6% to 11.0%. This is above the target allocation of 8%.

3.5.5 **Property** – During the quarter the Schroders property portfolio returned -12.3% and the M&G UK Residential Property Fund returned -1.62%. The negative capital returns have principally been driven by an outward yield shift caused by increasing interest rates. Although negative, on a relative basis, the performance of the Fund’s property portfolios has been good. The MSCI/AREF UK Quarterly Property Fund Index returned -14.1% for the quarter. The property allocation now makes at 12.4% of the Fund. The outlook for 2023 is that the property sector will remain challenging. The Fund’s property portfolio is positioned defensively being underweight to retail and office sectors.

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 31 December 2022

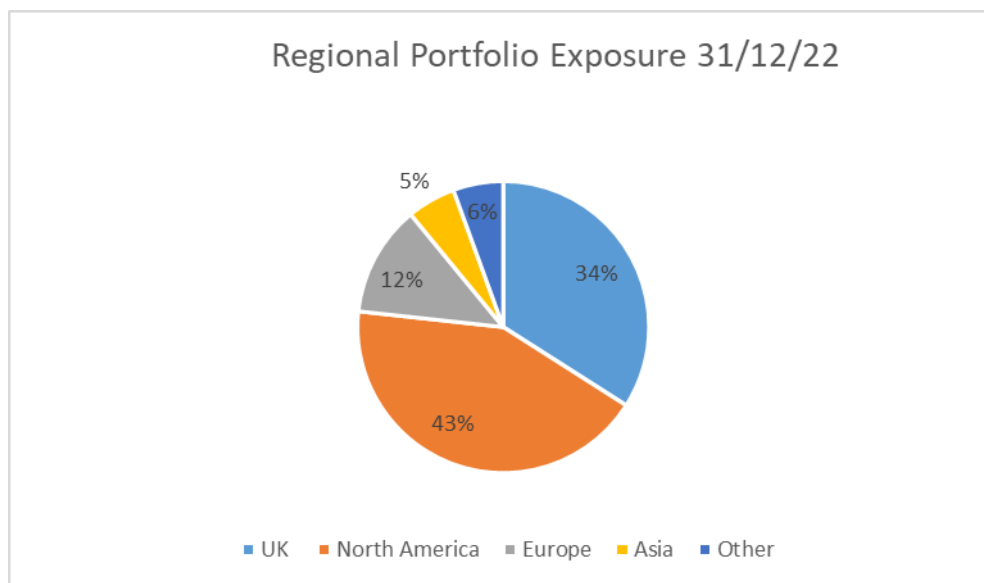
	Valuation at 30/09/2022 £'000	Net cashflow £'000	Gain/Loss £'000	Valuation at 31/12/2022 £'000	Asset allocation Fund percentage	Asset allocation target percentage
Equities					43.8%	42%
Legal & General FTSE World (Ex Tobacco)	605,259	-	26,899	632,159		
LCIV RBC	78,875	-	645	78,230		
LCIV	150			150		
Fixed Interest					15.9%	23%
Standard Life	119,256	-	2,774	122,030		
Wellington	54,039	-	2,058	56,097		
LCIV Global Bond	77,514	-	1,858	79,372		
Infrastructure					14.0%	10%
Access	32,230	1,826	1,579	35,635		
Temporis	57,189	532	393	58,114		
Equitix	78,652	476	102	79,026		
Macquarie GIG Renewable Energy	23,541	-	491	24,212		
I Squared	34,491	3,153	2,087	29,251		
Private Equity					11.0%	8%
Knightsbridge	74,877	-	7,173	67,704		
Pantheon	77,213	1,794	5,140	73,867		
Access	15,649	261	180	15,730		
North Sea	19,471	733	906	21,110		
Property					12.4%	16%
Schroders	155,948	-	18,756	137,192		
M&G	65,705	314	1,025	64,365		
Cash					2.9%	1%
Legal & General FTSE4Good Cash	567	-	169	736		
Cash	43,325	2,557	-	45,882		
Fund Total	1,613,951	4,222	2,691	1,620,864	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 34% invested in the UK 12.4% 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 31 December 2022. These reports are included in Part B of this Committee agenda.

3.8 Section 4: Investment Manager Visits

- 3.8.1 Officers attended the AGM for Access Capital Partners and attended a meeting with North Sea Capital Partners. The performance of the underlying companies within the portfolios managed by these managers remains strong and there were no concerns raised. This was encouraging and we are expecting the performance of these managers to remain strong.

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 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: 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 31 December 2022, Mercer

Appendix B: Market Background and Market View Q4 2022, Mercer