BROMLEY CIVIC CENTRE, STOCKWELL CLOSE, BROMLEY BRI 3UH

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DATE: 14 February 2023

To: Members of the
PENSIONS COMMITTEE

Councillor Keith Onslow (Chairman)
Councillor Kira Gabbert (Vice-Chairman)
Councillors Simon Fawthrop, Julie Ireland, Simon Jeal, Jonathan Laidlaw, Christopher Marlow, Ruth McGregor, Tony Owen and Sam Webber

A meeting of the Pensions Committee will be held at Bromley Civic Centre on
WEDNESDAY 22 FEBRUARY 2023 AT 7.00 PM

Members of the Local Pension Board are also invited to attend this meeting

PLEASE NOTE: This meeting will be held in the Council Chamber at the Civic Centre, Stockwell Close, Bromley, BR1 3UH. Members of the public can attend the meeting – if you wish to attend please contact us, before the day of the meeting if possible, using our web-form:

https://www.bromley.gov.uk/CouncilMeetingNoticeOfAttendanceForm

TASNIM SHAWKAT
Director of Corporate Services & Governance

Copies of the documents referred to below can be obtained from
http://cds.bromley.gov.uk/

A G E N D A

1 APOLOGIES FOR ABSENCE AND NOTIFICATION OF SUBSTITUTE MEMBERS

2 DECLARATIONS OF INTEREST

3 QUESTIONS BY MEMBERS OF THE PUBLIC ATTENDING THE MEETING

In accordance with the Council's Constitution, questions that are not specific to reports on the agenda must have been received in writing 10 working days before the date of the meeting.

Questions specifically relating to reports on the agenda should be received within two working days of the normal publication date of the agenda. Please ensure that questions specifically on reports on the agenda are received by the Democratic Services Team by **5.00pm on Thursday 16 February 2023**.

4 CONFIRMATION OF MINUTES OF THE MEETING HELD ON 1 DECEMBER 2022, EXCLUDING THOSE CONTAINING EXEMPT INFORMATION (Pages 3 - 10)

5 MATTERS OUTSTANDING FROM PREVIOUS MEETINGS

6 PENSION FUND PERFORMANCE Q3 2022/23 (Pages 11 - 48)

7 LOCAL GOVERNMENT ACT 1972 AS AMENDED BY THE LOCAL GOVERNMENT (ACCESS TO INFORMATION) (VARIATION) ORDER 2006 AND FREEDOM OF INFORMATION ACT 2000

The Chairman to move that the Press and public be excluded during consideration of the items of business referred to below as it is likely in view of the nature of the business to be transacted or the nature of the proceedings that if members of the Press and public were present there would be disclosure to them of exempt information.

	Items of Business	Schedule 12A Description
8	**CONFIRMATION OF EXEMPT MINUTES - 1 DECEMBER 2023** (Pages 49 - 50)	Information relating to the financial or business affairs of any particular person (including the authority holding that information)
9	**PENSION FUND TRIENNIAL VALUATION** (Pages 51 - 84)	Information relating to the financial or business affairs of any particular person (including the authority holding that information)
10	**PENSION FUND 2022 DRAFT FUNDING STRATEGY STATEMENT** (Pages 85 - 138)	Information relating to the financial or business affairs of any particular person (including the authority holding that information)
11	**POOLING MATTERS** (Pages 139 - 328)	Information relating to the financial or business affairs of any particular person (including the authority holding that information)

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PENSIONS COMMITTEE

Minutes of the meeting held at 7.00 pm on 1 December 2022

Present:

Councillor Keith Onslow (Chairman)
Councillor Kira Gabbert (Vice-Chairman)
Councillors Simon Fawthrop, Simon Jeal, Jonathan Laidlaw, Christopher Marlow, Ruth McGregor, Tony Owen and Sam Webber

Also Present:

John Arthur, MJ Hudson

16 APOLOGIES FOR ABSENCE AND NOTIFICATION OF SUBSTITUTE MEMBERS

There were no apologies for absence.

17 DECLARATIONS OF INTEREST

Councillor Simon Fawthrop declared that he was a member of the London Borough of Bromley Pension Scheme.

Councillor Tony Owen declared that he received a London Borough of Bromley pension and that his daughter was employed by Coopers School.

18 QUESTIONS BY MEMBERS OF THE PUBLIC ATTENDING THE MEETING

No questions had been received.

19 CONFIRMATION OF MINUTES OF THE MEETINGS HELD ON 8 AND 27 JUNE 2022, EXCLUDING THOSE CONTAINING EXEMPT INFORMATION

RESOLVED: That the minutes of the meetings held on 8 and 27 June 2022 be approved.

20 MATTERS OUTSTANDING FROM PREVIOUS MEETINGS

There were no matters outstanding.

A) Fund Manager Presentation – Baillie Gifford

The Committee received a presentation from Baillie Gifford representatives, Chris Murphy, Client Service Director: Local Government Client Team and

Tim Gooding, Client Service Director: Global Alpha Team, on the London Borough of Bromley Superannuation Fund.

Due to the current economic climate which had been impacted by geopolitical instability and significant increases in inflation and energy costs, performance during the 2022/23 financial year had been significantly below benchmark. This had been particularly marked in relation to stock held in tech companies which had seen exceptionally high growth during the pandemic and were now going through a period of normalisation but were considered a strong long-term investment in having better margins and much lower debt than the index on average. Performance over the long-term remained robust with active management outperformance of the Local Authority's investment with Baillie Gifford valued at £143.1M since 1 December 1999, with the value of the portfolio as at 30 September 2022 totalling £473,046,311. Over the past year, Baillie Gifford had worked to rebalance the portfolio with less stock held in technology-enabled companies and those with significant Chinese exposure, and more to durable franchises. The weight by category was now about 40% 'compounders', 30% 'disruptors' and 30% 'capital cycle' with the downturn in company valuations enabling the purchase of some outstanding investments at depressed prices. Growth investing would remain a key focus in future with innovation and structural change anticipated across a range of industries, such as healthcare and education, as well in emerging markets beyond China. The example of Moderna was used as a company experiencing reduced cashflow in the post-COVID period that was well-placed for long term growth due to technical innovations linked to the development of its COVID-19 vaccine.

In considering the update, the Chairman observed that just over a year ago, Baillie Gifford had presented to the Committee on the over-performance of its investments and that the recent underperformance demonstrated the impact of the difficult economic climate. A Member queried investments in Russia, and the Client Service Director: Global Alpha Team reported that stock held in the VK Group which was domiciled in Russia had recently been sold. A small holding in Russian stocks remained but were currently frozen and would be divested once trading resumed. The fund held no investments in Qatar but was looking to invest more in the growth markets of Latin America and South-East Asia when suitable opportunities arose. In response to a question by a Member, the Client Service Director: Global Alpha Team confirmed that the fund's exposure to Chinese investments had been reduced from approximately 8-9% to 4-5% over the past 12-months in response to concerns around the Chinese Government's view of foreign investment. Another Member queried Elon Musk's ongoing leadership of Tesla following his high-profile acquisition of Twitter, and the Client Service Director: Global Alpha Team advised that as a leading innovator in electric vehicles and energy, Tesla remained a robust investment option and the company benefitted from a strong leadership team that went beyond its co-founder and CEO.

A Member queried Baillie Gifford's corporate policies around free speech and further details would be provided following the meeting. The Chairman

observed that the Baillie Gifford was a strong advocate for environmental and social governance which was built into their investment practice.

The Chairman thanked the representatives of Baillie Gifford for their excellent presentation.

RESOLVED: That:

- **Matters outstanding be noted; and,**

- **The presentation from Baillie Gifford be noted.**

21 2021/22 PENSION FUND ANNUAL REPORT AND DRAFT ACCOUNTS
Report FSD22065

The report presented the draft Pension Fund Annual Report and Accounts 2021/22, which set out details of the administration and performance of the London Borough of Bromley Pension Fund during the 2021/22 financial year for consideration and approval by the Committee. The Pension Fund was required by the Local Government Pension Scheme Regulations 2013 to publish an Annual Report and Statement of Accounts, and this was also subject to external audit.

In considering the draft Pension Fund Annual Report and Accounts 2021/22, the Committee was notified that the terminology 'Pensions Sub-Committee' was used throughout as the period of reporting pre-dated the establishment of the Pensions Committee as a full committee. With regard to the Governance Compliance Statement, a Member queried why there was only partial compliance in some areas designed to make the administration and stewardship of the scheme more transparent and accountable to stakeholders. The Chairman advised that this was primarily due to the size of the scheme, but that membership of the Local Pension Board was divided equally between employer and scheme member representatives who were invited to attend all meetings of the Pensions Committee. In response to a question from a Member regarding terminology, the Chairman explained that a deferred pension was one which was taken later than pensionable age and that scheme members had the option to defer taking their pension if it met their individual needs.

The Chairman moved that the draft Pension Fund Annual Report and Draft Accounts for the 2021/22 financial year be approved as recommended. The motion was seconded by Councillor Christopher Marlow, put to the vote and CARRIED unanimously.

RESOLVED: That the draft Pension Fund Annual Report and Draft Accounts for the 2021/22 financial year be approved.

22 PENSION FUND PERFORMANCE Q2 2022/23
Report FSD22087

The report provided a summary of the investment performance of Bromley's Pension Fund in Quarter 2 of the 2022/23 financial year and included information on general financial and membership trends of the Pension Fund, including early retirements, as well as details of training options for Members and key developments in the Local Government Pension Fund (LGPS) expected during the next 5 years.

The Committee received an update from John Arthur, Senior Advisor: MJ Hudson who confirmed that 2022 had been a difficult year for investors after central banks across the world had raised interest rates to curb rising inflation. Whilst this had been anticipated, inflation levels had been higher than expected due to the geopolitical situation and spiralling wholesale gas prices which had served to destabilise the markets. The Senior Advisor: MJ Hudson advised that in his view, inflation was now peaking and would reduce in the short to medium-term provided there were no more unexpected events impacting the markets. Increased interest rates also offered investment opportunities with the 10-year forecast on UK Gilts now projected at 4.2% for 2022 against 0.0% for 2021. MJ Hudson had undertaken stress testing of cashflow assumptions for more persistently high inflation which provided reassurance that the Bromley Pension Fund was covered to the 2026/27 financial year using investment income currently distributed from the underlying portfolios, and that a further year could be covered should income from Global Equities be distributed to the fund. The performance of Bromley Pension Fund's two equity managers, Baillie Gifford and MFS Global Equity had varied widely over the past year with MFS Global Equity outperforming its benchmark by 6.9% whilst Baillie Gifford's investments had underperformed by -21.3% during the same period. This demonstrated the impact of different philosophies and investment styles in varying market conditions and illustrated how the two equity funds could act in counterpoint to each other.

In considering the update, the Chairman emphasised that active engagement with the challenges presented by the economic climate would be critical moving forward. The Bromley Pension Fund was a resilient scheme between 110-120% funded, even allowing for the reduction in investment values over the past year, and continued to have strong cashflow. The Senior Advisor: MJ Hudson underlined the need to determine the level of risk the Local Authority was prepared to accept in its investment strategy as lower risk investments generally yielded low returns. Furthermore, the Committee may also like to review the proportion of the fund given over to equity investment if there were concerns over the volatile economic climate. A Member stressed the importance of maintaining a simple investment strategy and highlighted that the nature of long-term investment meant that short-term losses often recovered over time. The Chairman observed that this was borne out by independent research which had identified that the relative simplicity of Bromley's fund management practices had supported its long-term stability.

The Committee discussed the Asset Allocation Review which had been commissioned to reassess the Fund's Strategic Asset Allocation from an asset-only perspective and suggest potential alternative portfolios that optimised risk and return based on updated long-term capital market assumptions, expected cashflow requirements and other constraints. The review made two recommendations comprising rebalancing the portfolio to the Strategic Asset Allocation to reduce volatility and to implement a 50% currency hedge on the global equities' portfolio based on the current standing of global currencies. Four potential portfolios to de-risk the fund had also been proposed which comprised 5% allocation to infrastructure; 5% allocation to social/affordable housing; 5% allocation to private debt; and 5% allocation to global credit (hedged), all of which were designed to offer greater diversification and increased yield, albeit with a slightly lower expected return relative to the Strategic Asset Allocation and increased illiquidity.

The Chairman underlined the need to consider the findings of the Asset Allocation Review alongside the actuarial review of the Bromley Pension Fund when this information became available and proposed that rebalancing of the fund's Strategic Asset Allocation be reviewed by the Committee on a regular basis moving forward. Following discussion, this was supported by Members, and it was agreed that the Committee would review rebalancing of the fund's Strategic Asset Allocation on a six-monthly basis. A Member voiced support for action being taken to de-risk the portfolio as it was incumbent on the Committee to take a prudent and responsible approach to investment on behalf of the Bromley Pension Fund members. The Member requested the Senior Advisor: MJ Hudson provide an analysis of how the fund would look if rebalancing had taken place regularly over the past four years and this would be taken forward following the meeting.

With regard to the four potential portfolios to de-risk the fund, Members generally expressed a preference for investing in social housing over infrastructure, although some infrastructure options might be worth exploring, such as renewable energy. A Member suggested that if social housing was considered a viable investment, investment in a future phase of the Meadowship Homes scheme could offer a low-risk long-term investment that would also contribute towards the delivery the Local Authority's housing objectives. Members discussed this possible investment opportunity which would also represent an investment in the Borough and its residents; however, it was recognised that any such scheme was liable to create a conflict of interest and the Committee would need to be mindful of its fiduciary duty and pursue only the best investment options for the fund. Investment in social housing in the Borough which bought rather than built houses also had the potential to impact the local housing market and disadvantage buyers. It was noted that whilst the Government had asked local authorities to plan for investing 5% of local pension funds in social investment across England and Wales, there was no requirement to invest any funds as yet, and a Member underlined the importance of considering other secure fixed income investments to de-risk the portfolio, such as UK gilts. Another Member argued against the recommendation to implement a 50% currency hedge on

the global equities' portfolio in light of the difficulties predicting the dynamic between global currencies over time.

In summation, the Committee agreed not to make any decisions regarding the recommendation to the Asset Allocation Review at this time and to revisit it at the next meeting of the Pensions Committee on 22 February 2023, including the proposal to invest in a future phase of the Meadowship Homes scheme.

RESOLVED: That:

- **The contents of the report and information contained in the related appendices be noted including:**

  a) Appendix 7 which sets out the key developments in LGPS expected during the next 5 years;
  b) Appendix 8 which is the response of the Bromley Pension Fund to the Task Force for Climate Related Financial Disclosures (TCFD) consultation; and,
  c) Appendix 9 which formalises Bromley's Discretionary Policy on the Abatement of Pensions.

- **Members' comments on Appendix 10: Asset Allocation Review document considered in conjunction with Appendix 11: Notes of the MJ Hudson meeting of 2 November 2022 be noted.**

23 LOCAL PENSION BOARD - DRAFT ANNUAL REPORT Report CSD22128

The report presented the Local Pension Board – Draft Annual Report which had been approved by the Local Pension Board at its meeting on 22 November 2022 and would also be provided to Council for noting. The Draft Annual Report comprised a range of information including a summary of the work of the Local Pension Board during the past year and details of areas of concern reported to or identified by the Board as well as any training that had been undertaken by Board Members.

RESOLVED: That the Annual Report of the Local Pension Board be noted.

24 UPDATES FROM THE CHAIRMAN/DIRECTOR OF FINANCE/PENSIONS INVESTMENT ADVISOR

The Committee agreed that the special meeting of Pensions Committee scheduled for 17 January 2023 be cancelled to allow more time for key workstreams to be completed.

RESOLVED: That discussions under the Part 1 (Public) update be noted.

25 LOCAL GOVERNMENT ACT 1972 AS AMENDED BY THE LOCAL GOVERNMENT (ACCESS TO INFORMATION) (VARIATION) ORDER 2006 AND FREEDOM OF INFORMATION ACT 2000

RESOLVED that the Press and public be excluded during consideration of the items of business referred to below as it is likely in view of the nature of the business to be transacted or the nature of the proceedings that if members of the Press and public were present there would be disclosure to them of exempt information.

The following summaries refer to matters involving exempt information

26 CONFIRMATION OF EXEMPT MINUTES - 8 AND 27 JUNE 2022

The Part 2 (Exempt) minutes of the meetings held on 8 and 27 June 2022 were approved.

27 PENSION FUND PERFORMANCE Q2 2022/23 PART 2 (EXEMPT) INFORMATION

The Committee considered Part 2 (Exempt) information on Pension Fund Performance Q2 2022/23.

28 UPDATES FROM THE CHAIRMAN/DIRECTOR OF FINANCE/PENSIONS INVESTMENT ADVISOR (PART 2)

The Chairman and the Director of Finance provided a Part 2 (Exempt) update to the Committee on recent developments relating to pensions.

The Meeting ended at 9.50 pm

Chairman

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Report No.
FSD23020

London Borough of Bromley

PART 1 - PUBLIC

Decision Maker:	**PENSIONS COMMITTEE**
Date:	**22 February 2023**
Decision Type:	Non-Urgent Non-Executive Non-Key
Title:	**PENSION FUND PERFORMANCE Q3 2022/23**
Contact Officer:	Dan Parsons, Senior Accountant Tel: 020 8313 3176 E-mail: dan.parsons@bromley.gov.uk
Chief Officer:	Peter Turner, Director of Finance Tel: 020 8313 4668 Email: peter.turner@bromley.gov.uk
Ward:	Borough Wide

1. Reason for report

1.1 This report provides a summary of the investment performance of Bromley's Pension Fund in the 3nd quarter of 2022/23. The report also contains information on general financial and membership trends of the Pension Fund and summarised information on early retirements.

1.2 The report also includes key developments in the Local Government Pension Fund (LGPS) expected during the next 5 years.

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2. RECOMMENDATIONS

2.1 The Pensions Committee is asked to note the contents of the report and information contained in the related appendices.

2.2 The Pensions Committee is asked to note;

a) Appendix 5 which details;

- **Bromley's Strategic Asset Allocation review by independent adviser MJ Hudson and proposed actions for rebalancing the portfolio;**
- **Advice from MJ Hudson on the opportunity to rebalance and diversify into affordable housing in Bromley via a potential new phase in the Meadowship Homes project; and**
- **Advice from MJ Hudson around currency hedging.**

b) Appendix 6 (see Part 2 – Exempt Agenda) which is the draft Funding Strategy Statement (prior to Consultation); and,

c) Appendix 8 which sets out the key developments in LGPS expected during the next 5 years.

Corporate Policy

1. Policy Status: Existing policy. The Council's Pension Fund is a defined benefit scheme operated under the provisions of the Local Government Pension Scheme (LGPS) Regulations, for the purpose of providing pension benefits for its employees. The investment regulations (The LGPS (Management and Investment of Funds) Regulations 2016) allow local authorities to use all the established categories of investments, e.g. equities, bonds, property etc, and to appoint external investment managers who are required to use a wide variety of investments and to comply with certain specific limits.

2. BBB Priority: Excellent Council .

Financial

1. Cost of proposal: No cost

2. Ongoing costs: Recurring cost . Total administration costs estimated at £5.9m (includes fund manager/actuary/adviser fees, Liberata charge and officer time)

3. Budget head/performance centre: Pension Fund

    3. Total current budget for this head: £49.6m expenditure (pensions, lump sums, etc); £57.6m income (contributions, investment income, etc); £1,245m total fund market value at 31st December 2022

    4.

5. Source of funding: Contributions to Pension Fund

Staff

1. Number of staff (current and additional): 1 FTE

2. If from existing staff resources, number of staff hours: 36 hours per week

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Legal

1. Legal Requirement: Statutory requirement. Local Government Pension Scheme (LGPS) Regulations 2013 (as amended), LGPS (Management and Investment of Funds) Regulations 2016

2. Call-in: Call-in is not applicable.

Customer Impact

1. Estimated number of users/beneficiaries (current and projected): 6,371 current employees; 5,966 pensioners; 6,385 deferred pensioners as at 31st December 2022

Ward Councillor Views

1. Have Ward Councillors been asked for comments? No.

2. Summary of Ward Councillors comments: N/A

3. COMMMENTARY

3.1 Fund Value

3.1.1 The market value of the Fund ended the December quarter at £1,244.8m, up £22.6m as at 30th September. The comparable value as at 31st December 2021 was £1,431.4m. Historic data on the value of the Fund are shown in a table and in graph form in Appendix 1.

3.2 Performance Targets and Investment Strategy

3.2.1 Historically, the Fund's investment strategy was broadly based on a high level 80%/20% split between growth seeking assets (representing the long-term return generating part of the Fund's assets) and protection assets (aimed at providing returns to match the future growth of the Fund's liabilities). Between 1998 and 2012, Baillie Gifford and Fidelity managed balanced mandates along these lines, and, a comprehensive review of the Fund's investment strategy in 2012 confirmed this high-level strategy. It concluded that the growth element would, in future, comprise a 10% allocation to Diversified Growth Funds (DGF) and a 70% allocation to global equities, with a 20% protection element remaining in place for investment in corporate bonds and gilts.

3.2.2 The asset allocation strategy was reviewed again during 2016/17, mainly to address the projected cash flow shortfall in future years, and a revised strategy was agreed on 5th April 2017. The revised strategy introduced allocations to Multi Asset Income Funds (20%) and Property Funds (5%), removed Diversified Growth Funds, and reduced the allocations to Global Equities (to 60%) and Fixed Income (to 15%). In order to implement the revised strategy, it was agreed to sell all of the Diversified Growth Funds and the Blackrock Global Equities assets.

3.2.3 At the meetings on 21st November and 14th December 2017 the Committee appointed Schroders (60%) and Fidelity (40%) to manage the MAI fund mandates and Fidelity to manage a UK pooled property fund mandate. The Fidelity MAI and initial drawdown of the property fund were completed in February 2018 and the Schroders MAI investment completed in May 2018. A further drawdown of the Fidelity property fund was completed in August 2018. The final drawdown of the Fidelity property was completed in December 2018. The sale of the balance of the Blackrock fund was completed in May 2019 and transferred to Fidelity's MAI Fund, as agreed by this Committee at its meeting held on 15th May 2019.

3.2.4 The asset allocation strategy was reviewed again during 2019/20, and a revised strategy has been finalised. The revised strategy has amended the allocations as follows: Equities (58%), Multi Asset Income Funds (20%), Fixed Income (13%), UK Real Estate (4%) and International Property (5%).

3.3 Summary of Fund Performance

3.3.1 Performance data for 2022/23 (short-term)

A detailed report on fund manager performance in the quarter ended 31st December 2022 is provided by the fund's external adviser, MJ Hudson in Appendix 5. The total fund return for the third quarter was -3.36% against the benchmark of -3.56%. Further details of individual fund manager performance against their benchmarks for the quarter, year to date, 1, 3 and 5 years and since inception are provided in Appendix 2.

3.3.2 Medium and long-term performance data

The Fund's medium and long-term returns have remained strong overall, though this year there was variable performance in the first three quarters, and there has been underperformance versus benchmark. In 2021/22 there was a return of 0.7% against a benchmark of 8.69%. There was a return of 34.1% against a benchmark of 23.6% in 2020/21. The returns for 2019/20 and 2018/19 were -2.74% and 8.0% against the benchmark of -1.87% and 8.3% respectively.

Performance rankings were available at the time this report was drafted. The overall Fund ranked 60th against the 62 funds in the PIRC LGPS universe for the year to 31st March 2022, 52nd over 3 years, third over 5 years, second over 10 years and first over 20 and 30 years.

The following table shows the Fund's long-term rankings in all financial years back to 2005/06 and shows the medium to long-term returns for periods ended 31st March. The medium to long-term results have been very good and have underlined the fact that the Fund's performance has been consistently strong over a long period.

Year	Whole Fund Return	Benchmark Return	Local Authority Average*	Whole Fund Ranking*
	%	%	%	
Financial year figures				
2021/22	***0.7***	***8.7***	***8.6***	***60***
2020/21	34.1	23.6	22.8	2
2019/20	-2.74	-1.87	-4.8	22
2018/19	8.0	8.3	6.6	11
2017/18	6.7	3.1	4.5	3
2016/17	26.8	24.6	21.4	1
2015/16	0.1	0.5	0.2	39
2014/15	18.5	16.4	13.2	7
2013/14	7.6	6.2	6.4	29
2012/13	16.8	14.0	13.8	4
3 year ave to 31/3/22	***10.7***	***10.1***	***8.9***	***52***
2015/16	10.6	8.9	8.3	1
2014/15	14.6	13.4	11.2	1
2013/14	8.4	7.5	6.4	6
2012/13	14.2	12.1	11.1	5
2011/12	2.2	2.0	2.6	74
2010/11	9.0	8.0	8.2	22
5 year ave to 31/3/22	***9.4***	***8.4***	***7.5***	***3***
2013/14	11.5	9.8	8.8	2
2012/13	13.6	12.0	10.7	1
2011/12	8.8	7.6	7.1	6
2010/11	10.7	9.2	8.8	11
2009/10	48.7	41.0	35.2	2
2008/09	-18.6	-19.1	-19.9	33
2007/08	1.8	-0.6	-2.8	5
2006/07	2.4	5.2	7.0	100
2005/06	27.9	24.9	24.9	5
10 year ave to 31/3/22	***11.2***	***n/a***	***8.3***	***2***
20 year ave to 31/3/22	***9.0***	***n/a***	***6.9***	***1***
30 year ave to 31/3/22	***9.5***	***n/a***	***8.4***	***1***

*The most recent LA averages and ranking as at 31/03/22 are based on the PIRC LA universe containing 63 of the 89 funds.

3.3.3 In addition to winning the LGPS Investment Performance of the Year in 2017, the LGPS Fund of the Year (assets under £2.5bn) in 2018, Bromley was also in the final shortlist for 2019 and 2020. Bromley also recently won the Pensions, Treasury and Asset Management Award at

CIPFA's Public Finance Awards 2021, recognising the consistent high performance of the Fund.

3.3.4 Performance Measurement Service

As previously reported in April 2016, the Council was informed that WM Company (State Street) would cease providing performance measurement services to clients to whom they do not act as custodian with effect from June 2016. There are currently no providers offering a like for like service, so the Council is using its main custodian, BNY Mellon, to provide performance measurement information and the 2nd quarter summary of manager performance is provided at Appendix 2. PIRC currently provide LA universe comparator data and, at the time of writing, has 62 of the 89 LGPS funds (71%) signed up to the service including the London Borough of Bromley.

3.4 **Early Retirements**

3.4.1 Details of early retirements by employees in the Fund are shown in Appendix 3.

3.5 **Admission agreements for outsourced services**

3.5.1 Bromley MyTime has made its pension deficit repayments in line with the draft repayment plan. The amount outstanding is approximately £0.9m.

3.5.2 The December Year End Accounting exercise has been completed by Mercer and the Triennial valuation exercise and issuing of Employer certificates is underway.

3.5.3 Member Self Service pensions portal and I-Connect (employer) portal are being implemented by Aquilla Heywood. The project is progressing well and the VPN connection between Liberata and Heywood is now established and working. Training has been completed and user acceptance testing is now underway. Estimated date for implementation of MSS is now mid-2023.

3.6 **Fund Manager attendance at meetings**

3.6.1 At the time of this report, meeting dates have not been confirmed by Democratic Services for FY 2022/23. While Members reserve the right to request attendance at any time if any specific issues arise, the timetable for subsequent meetings is as follows although this may be subject to change given future social-distancing requirements:

Meeting Q1 2022/23 (tbc) – Fidelity
Meeting Q2 2022/23 (tbc) – MFS

4. POLICY IMPLICATIONS

4.1 The Council's Pension Fund is a defined benefit scheme operated under the provisions of the Local Government Pension Scheme (LGPS) Regulations, for the purpose of providing pension benefits for its employees. The investment regulations (The LGPS (Management and Investment of Funds) Regulations 2016) allow local authorities to use all the established categories of investments, e.g. equities, bonds, property etc, and to appoint external investment managers who are required to use a wide variety of investments and to comply with certain specific limits.

5. FINANCIAL IMPLICATIONS

5.1 Details of the provisional outturn for the 2021/22 pension fund revenue account are provided in Appendix 4 together with fund membership numbers. A net provisional surplus of £20.3m

including re-invested income of £11m. A net provisional surplus of £9.3m excluding re-invested income occurred during 2021/22 and membership numbers rose by 544 in the year. In the third quarter of 2022/23 total membership numbers increased by 318.

6. LEGAL IMPLICATIONS

6.1 The statutory provisions relating to the administration of the Local Government Pension Scheme are contained in the Local Government Pension Scheme (LGPS) Regulations 2013 (as amended). The investment regulations (The LGPS (Management and Investment of Funds) Regulations 2016) set out the parameters for the investment of Pension Fund monies.

Non-Applicable Sections:	Personnel Implications, Impact on Vulnerable Adults and Children, Procurement Implications
Background Documents: (Access via Contact Officer)	Monthly and quarterly portfolio reports of Baillie Gifford, Fidelity, MFS and Schroders.

APPENDIX 1

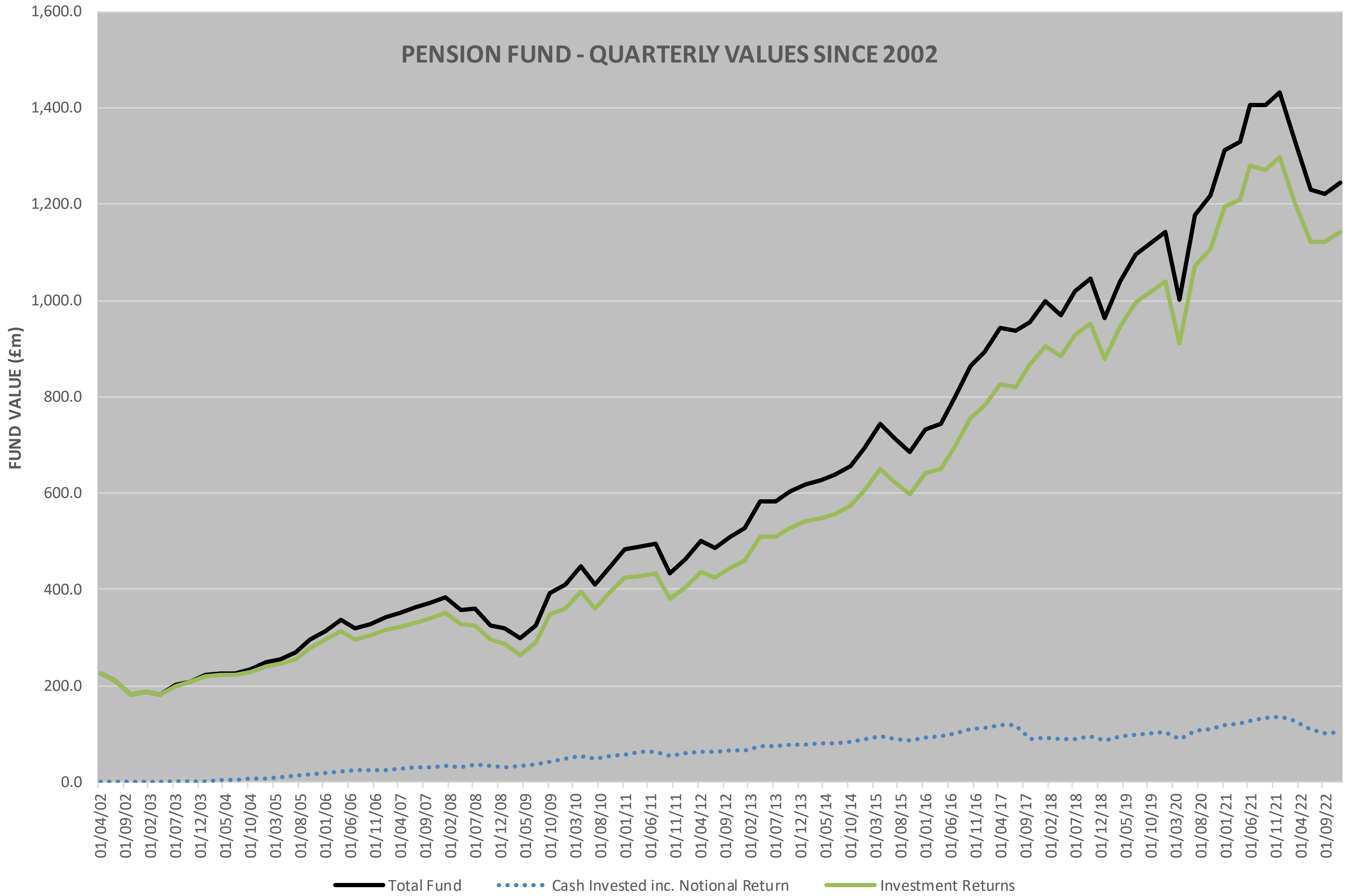
MOVEMENTS IN PENSION FUND MARKET VALUE SINCE 2002

	Baillie Gifford					Fidelity							Blackrock	MFS		Schroders	CAAM	
Date	Balanced Mandate	DGF	Fixed Income	Global Equities	Total	Balanced Mandate	Fixed Income	MAI	Property	Sterling Bond	USD ILF	Total	Global Equities	Global Equities	DGF	MAI	LDI Investment	**GRAND TOTAL**
31/03/2002	113.3				113.3	112.9						112.9						226.2
31/03/2003	90.2				90.2	90.1						90.1						180.3
31/03/2004	113.1				113.1	112.9						112.9						226
31/03/2005	128.5				128.5	126.7						126.7						255.2
31/03/2006	172.2				172.2	164.1						164.1						336.3
31/03/2007	156				156	150.1						150.1					43.5	349.6
31/03/2008	162				162	151.3						151.3					44	357.3
31/03/2009	154.4				154.4	143						143						297.4
31/03/2010	235.4				235.4	210.9						210.9						446.3
31/03/2011	262.6				262.6	227						227						489.6
31/03/2012	269.7				269.7	229.6						229.6						499.3
31/03/2013#	315.3	26.5			341.8	215.4						215.4			26.1			583.3
31/03/2014@	15.1	26.8	45.2	207.8	294.9		58.4					58.4	122.1	123.1	27			625.5
31/03/2015		45.5	51.6	248.2	345.3		66.6					66.6	150.5	150.8	29.7			742.9
31/03/2016		44.8	51.8	247.9	344.5		67.4					67.4	145.5	159.2	28.3			744.9
31/03/2017		49.3	56.8	335.3	441.4		74.3					74.3	193.2	206.4	28.5			943.8
31/03/2018$&			58	380	438		75.6	79.2	15.9			170.7	155.2	206.8				970.7
31/03/2019			59.2	416.5	475.7		78.7	78.8	48.6			206.1	11.4	230.2		115.8		1,039.20
31/03/2020			60.9	411.85	472.7		83.5	80.6	47			211.1		220.3		96.1		1,000.30
30/06/2020			65	529.8	594.8		88.4	87.5	45.6			221.5		254.3		106.8		1,177.40
30/09/2020/			65.4	524.8	590.2		89	128.3	44.7			262		259.2		106.6		1,218.00
31/12/2020\				585.3	585.3		91	133	45.5	67.7		337.2		278.8		111.7		1,313.00
31/03/2021				597.7	597.7		85.7	131.4	46.3	64.8		328.2		293.1		110.9		1,329.90
30/06/2021*				621.2	621.2		87.4	134.8	69.5	66.2		357.9		311.2		114.5		1,404.80
30/09/2021				614.6	614.6		86.5	134	71.6	65.4		357.5		319.5		113.3		1,404.90
31/12/2021				602.3	602.3		87.4	132.1	75.5	65.8	14.1	374.9		340		114.2		1,431.40

MOVEMENTS IN PENSION FUND MARKET VALUE SINCE 2002 CONTINUED

	Baillie Gifford					Fidelity							Blackrock	MFS		Schroders	MS	
Date	Balanced Mandate	DGF	Fixed Income	Global Equities	Total	Balanced Mandate	Fixed Income	MAI	Property	Sterling Bond	USD ILF	Total	Global Equities	Global Equities	DGF	MAI	USD Property	**GRAND TOTAL**
31/03/2022				527.8	527.8		81.2	125.5	77.9	61.2	14.8	360.6		332.9		108.7		1,330.09
30/06/2022				466.7	466.7		73.9	117.1	81.0	56.6	8.6	337.2		318.8		100.7	7.6	1,231.02
30/09/2022				474.4	474.4		65.5	109.8	78.0	50.6	5.3	309.2		329.2		97.6	11.8	1,222.20
31/12/2022				486.0	486.0		67.3	110.2	65.7	53.1	3.9	300.2		348.3		98.0	12.3	1,244.80

£50m Fidelity equities sold in Dec 2012 to fund Standard Life and Baillie Gifford DGF allocations.
@ Assets sold by Fidelity (£170m) and Baillie Gifford (£70m) in Dec 2013 to fund MFS and Blackrock global equities
$ £32m Blackrock global equities sold in July 2017 to pay group transfer value re Bromley College
& Assets sold by Baillie Gifford (£51m), Standard Life (£29m) and Blackrock (£19m) in Feb 2018 to fund Fidelity MAI and Property funds.
£ Assets sold by Blackrock (£120m) in May 2018 to fund Schroder MAI fund.
^ Assets sold by Blackrock (£20m) in August 2018 to fund Fidelity Property fund
* Assets sold by Blackrock (£13.7m) in December 2018 to fund Fidelity Property fund.
" Assets sold by Blackrock (£11.6m) in May 2019 to fund Fidelity MAI
/ Assets sold by Baillie Gifford (£41.2m) in Aug 2020 to fund Fidelity MAI fund
\ Assets sold by Baillie Gifford (£65.5m) in Oct 2020 to fund Fidelity Sterling Corporate Bond fund
*Assets sold by Baillie Gifford (£14.4m) in June 2021 to fund Fidelity Property fund


PENSION FUND - QUARTERLY VALUES SINCE 2002
FUND VALUE (£m)
1,600.0
1,400.0
1,200.0
1,000.0
800.0
600.0
400.0
200.0
0.0
01/04/02
01/09/02
01/02/03
01/07/03
01/12/03
01/05/04
01/10/04
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01/12/18
01/05/19
01/10/19
01/03/20
01/08/20
01/01/21
01/06/21
01/11/21
01/04/22
01/09/22
Total Fund
Cash Invested inc. Notional Return
Investment Returns

PENSION FUND MANAGER PERFORMANCE TO DECEMBER 2022

Portfolio	Month %	3 Months %	YTD %	1 Year %	3 Years %	5 Years %	Since Inception %
Baillie Gifford Global Equity	(4.49)	2.45	(7.91)	(19.30)	5.35	7.71	8.51
Benchmark	(4.85)	1.97	(5.22)	(7.63)	7.91	8.26	7.93
Excess Return	0.37	0.48	(2.69)	(11.68)	(2.56)	(0.56)	0.58
Fidelity Fixed Income	(2.84)	3.81	(15.35)	(21.17)	(5.87)	(2.01)	4.98
Benchmark	(3.04)	3.97	(15.67)	(21.43)	(6.53)	(2.53)	4.19
Excess Return	0.20	(0.16)	0.32	0.26	0.66	0.52	0.79
Fidelity MAI	0.36	2.06	(9.19)	(12.84)	(3.14)		(0.27)
Benchmark	0.33	0.99	2.99	4.00	4.00		4.00
Excess Return	0.03	1.07	(12.17)	(16.84)	(7.14)		(4.27)
Fidelity Property	(4.30)	(15.79)	(14.27)	(10.62)	2.39		2.26
Benchmark	(4.95)	(14.12)	(14.28)	(9.46)	2.20		2.75
Excess Return	0.65	(1.67)	0.01	(1.16)	0.19		(0.49)
MFS Global Equity	(3.60)	5.78	4.64	2.45	9.90	9.67	12.40
Benchmark	(4.89)	1.86	(5.58)	(8.08)	7.40	7.73	10.44
Excess Return	1.30	3.92	10.22	10.52	2.49	1.95	1.96
Schroder MAI	(1.18)	1.38	(7.32)	(11.20)	(2.30)		(0.44)
Benchmark	0.41	1.23	3.73	5.00	5.00		5.00
Excess Return	(1.59)	0.16	(11.04)	(16.20)	(7.30)		(5.44)
Lon Borough Bromley USD	(0.99)	(5.02)	10.03	14.95			9.61
Total Fund	(3.36)	2.08	(5.79)	(12.27)	3.81	5.44	8.53
Benchmark	(3.56)	1.24	(5.64)	(7.61)	4.71	5.52	
Excess Return	0.21	0.85	(0.15)	(4.67)	(0.90)	(0.07)	

N.B. returns may differ to fund manager reports due to different valuation/return calculation methods

EARLY RETIREMENTS

A summary of early retirements and early release of pension on redundancy by employees in Bromley's Pension Fund in the current year and in previous years is shown in the table below. With regard to retirements on ill-health grounds, this allows a comparison to be made between their actual cost and the cost assumed by the actuary in the triennial valuation. If the actual cost of ill-health retirements significantly exceeds the assumed cost, the actuary will be required to consider whether the employer's contribution rate should be reviewed in advance of the next full valuation. In the last valuation of the Fund (as at 31st March 2019) the actuary assumed a figure of 0.9% of pay (approx. £1.4m p.a from 2020/21) compared to £1.2m in the 2016 valuation, £1m in the 2013 valuation and £82k p.a. in the 2010 valuation. In 2015/16 there were nine ill-health retirements with a long-term cost of £1,126k, in 2016/17 there were six with a long-term cost of £235k, in 2017/18 there were five with a long-term cost of £537k, in 2018/19 there were five with a long-term cost of £698k,in 2019/20 there were three with a long-term cost of £173k, and in 2020/21 there were six with a long-term cost of £520k. Provision has been made in the Council's budget for these costs and contributions have been and will be made to reimburse the Pension Fund as result of which the level of costs will have no impact on the employer contribution rate.

The actuary does not make any allowance for other (non-ill-health) early retirements or early release of pension, however, because it is the Council's policy to fund these in full by additional voluntary contributions. In 2018/19 there were eight with a long-term cost of £392k, in 2019/20 there were 14 with a long-term cost of £433k and in 2020/21 there were 14 with a long-term cost of £203k. Provision has been made in the Council's budget for severance costs arising from LBB staff redundancies and contributions have been and will be made to the Pension Fund to offset these costs. The costs of non-LBB early retirements are recovered from the relevant employers.

Long-term cost of early retirements		**Ill-Health**		**Other**	
		No	£000	No	£000
Oct 22– Dec 22	- LBB	1	45	0	0
	- Other	0	0	0	0
	- Total	1	45	0	0
2022/23 total	- LBB	2	260	0	0
	- Other	1	56	1	25
	- Total	3	316	1	25
Actuary's assumption	- 2019 to 2022		1,400 p.a.		N/a
	- 2016 to 2019		1,200 p.a.		N/a
	- 2013 to 2016		1,000 p.a.		N/a
	- 2010 to 2013		82 p.a.		N/a
Previous years	– 2021/22	1	618	0	0
	- 2020/21	10	549	23	270
	– 2019/20	3	173	14	433
	– 2018/19	5	698	8	392
	– 2017/18	5	537	10	245
	– 2016/17	6	235	22	574
	– 2015/16	9	1,126	14	734
	– 2014/15	7	452	19	272
	– 2013/14	6	330	26	548
	– 2012/13	2	235	45	980

APPENDIX 4

PENSION FUND REVENUE ACCOUNT AND MEMBERSHIP

	Outturn 2021/22	Actuals 31 Dec 2022	Projected Outturn 2022/23
	£'000	£'000	£'000
INCOME			
Employee Contributions	8,171	6,024	8,160
Employer Contributions			
- Normal	26,301	19,106	26,260
- Past-deficit	478	359	478
Transfer Values Receivable	4,567	4,959	6,612
Investment Income			
- Re-invested	11,057	8,293	11,050
- Distributed to Fund	14,169	9,806	13,060
Total Income	64,743	48,547	65,620
EXPENDITURE			
Pensions	30,353	22,049	29,398
Lump Sums	4,424	3,222	4,296
Transfer Values Paid	2,541	2,191	2,922
Administration			
- Manager fees	5,186	3,890	5,180
- Other (incl. pooling costs)	1,606	1,200	1,600
Refund of Contributions	271	226	302
Total Expenditure	44,381	32,778	43,768
Surplus/Deficit (-) - including re-invested income (RI)	20,362	15,796	21,852
Surplus/Deficit (-) - excluding RI[1]	9,305	7,476	10,802

MEMBERSHIP	**30/09/2022**	**31/12/2022**
Employees	6,137	6,371
Pensioners	5,911	5,966
Deferred Pensioners	6,356	6,385
	18,404	18,722

Note 1 It should be noted that the draft outturn net surplus of £20.4m in 2021/22 includes investment income of £11m which was re-invested in the funds so, in cashflow terms, there is a £9.3m cash surplus for the year.

MJ HUDSON

London Borough of Bromley

Quarterly Report

Q3 2022

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Performance Summary

The fourth quarter showed some rebound from the poor performance of the first 9 months as, although central banks continued to raise interest rates, markets began to look forward to a period of falling inflation. The table below shows that whilst many asset classes recovered in the fourth quarter, they were still down over 2022 as a whole.

	Index (Local Currency)	Q4 2022	Quarter-on-Quarter	YTD
Equities			**Total Return**	
UK Large-Cap Equities	FTSE 100	7,452	8.7%	4.6%
UK All-Cap Equities	FTSE All-Share	4,075	8.9%	0.2%
US Equities	S&P 500	3,840	7.5%	-18.1%
European Equities	EURO STOXX 50 Price EUR	3,794	14.9%	-8.5%
Japanese Equities	Nikkei 225	26,095	0.7%	-9.0%
EM Equities	MSCI Emerging Markets	956	9.6%	-19.9%
Global Equities	MSCI World	2,603	9.9%	-17.7%
Government Bonds				
UK Gilts	FTSE Actuaries UK Gilts TR All Socks	3,018	1.7%	-23.8%
UK Gilts Over 15 Years	FTSE Actuaries Uk Gilts Over 15 Yr	3,694	-1.8%	-40.1%
UK Index-Linked Gilts	FTSE Actuaries UK Index-Linked Gilts TR All Stocks	4,000	-6.0%	-33.6%
UK Index-Linked Gilts Over 15 Years	FTSE Actuaries UK Index-Linked Gilts TR Over 15 Yr	4,564	-12.8%	-46.9%
Euro Gov Bonds	Bloomberg EU Govt All Bonds TR	208	-2.1%	-18.5%
US Gov Bonds	Bloomberg US Treasuries TR Unhedged	2,188	0.7%	-12.5%
EM Gov Bonds (Local)	J.P. Morgan Government Bond Index Emerging Markets Core Index	124	7.8%	-10.2%
EM Gov Bonds (Hard/USD)	J.P. Morgan Emerging Markets Global Diversified Index	804	8.1%	-17.8%
Bond Indices				
UK Corporate Investment Grade	S&P UK Investment Grade Corporate Bond Index TR	330	6.4%	-18.4%
European Corporate Investment Grade	Bloomberg Pan-European Aggregate Corporate TR Unhedged	213	1.7%	-15.1%
European Corporate High Yield	Bloomberg Pan-European HY TR Unhedged	389	4.7%	-11.1%
US Corporate Investment Grade	Bloomberg US Corporate Investment Grade TR Unhedged	2,968	3.6%	-15.8%
US Corporate High Yield	Bloomberg US Corporate HY TR Unhedged	2,186	4.2%	-11.2%
Commodities				
Brent Crude Oil	Generic 1st Crude Oil, Brent, USD/bbl	86	-2.3%	10.5%
Natural Gas (US)	Generic 1st Natural Gas, USD/MMBtu	4.48	-33.9%	20.0%
Gold	Generic 1st Gold, USD/toz	1,826	9.9%	-0.1%
Copper	Generic 1st Copper, USD/lb	381	11.7%	-14.6%
Currencies				
GBP/EUR	GBPEUR Exchange Rate	1.13	-0.8%	-5.0%
GBP/USD	GBPUSD Exchange Rate	1.21	8.2%	-10.7%
EUR/USD	EURUSD Exchange Rate	1.07	9.2%	-5.8%
USD/JPY	USDJPY Exchange Rate	131.12	-9.4%	13.9%
Dollar Index	Dollar Index Spot	103.52	-7.7%	8.2%
Alternatives				
Infrastructure	S&P Global Infrastructure Index	2,658	11.0%	-0.2%
Private Equity	S&P Listed Private Equity Index	159	11.8%	-28.2%
Hedge Funds	Hedge Fund Research HFRI Fund-Weighted Composite Index	17,520	1.7%	-3.9%
Global Real Estate	FTSE EPRA Nareit Global Index TR GBP	3,590	-0.3%	-14.0%
Volatility			**Change in Volatility**	
VIX	Chicago Board Options Exchange SPX Volatility Index	22	-31.5%	25.8%

Source: Bloomberg
All return figures quoted are total return, calculated with gross dividends/income reinvested.

The Fund rose by 2.1% over the quarter which looks poor given the equity market recovery shown in the table above but the asset class returns quoted above are in local currency. The recovery in Sterling from the Truss/Kwarteng debacle has

been reasonably rapid but has actually been driven more by the weakness of the US Dollar than by Sterling strength. US domiciled stocks account for over 60% of the MSCI Global Equity index.

The quarterly return of 2.1% is above the Fund benchmark return of 1.2%. Over 2022 the Fund fell by -12.3% against a benchmark return of -7.6%. The vast majority of the fall was driven by the underperformance of the Baillie Gifford Global Equity portfolio. Despite the tough market conditions of the last year, the Fund has still returned over 8.5% per annum over the last 35 years. It is this long-term performance which has driven the improved funding ratio.

Following on from the review of managers forecast risk and return expectations for major asset classes and the Strategic Asset Allocation Review conducted by MJ Hudson earlier this year, No major changes to the Strategic Asset Allocation benchmark are proposed. However, given the considerable deviation of the current portfolio from that Strategic Benchmark, I do recommend reducing the Fund's Equity exposure by £70m via a sale from the Baillie Gifford portfolio, reinvesting the money £20m into the US Dollar account supporting the Morgan Stanley International Property portfolio; £20m into the Fidelity Fixed Interest portfolio and £15m into both of the Fund's Multi-Asset Income portfolios. This will increase the diversification within the Fund, use the currently strong equity markets to replenish the cash awaiting drawdown into the International Property portfolio and bring the Fund more into line with the Strategic Benchmark. £20m accounts to approximately 1.6% of the Fund.

Comment

Interest rates continue to rise and will do so for at least another quarter across the US, UK and EU. The questions are:

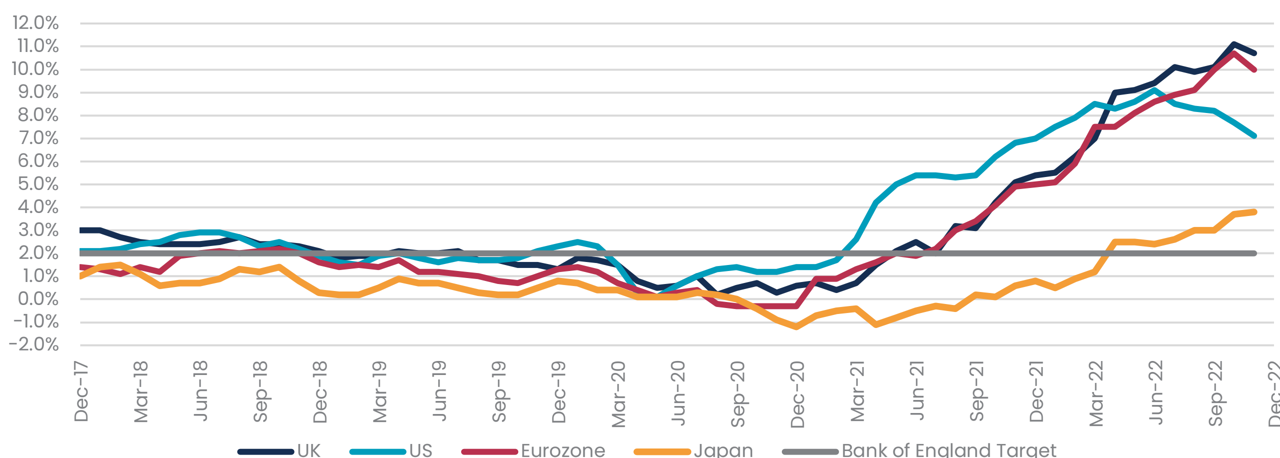
- Has inflation peaked?
- How quickly it will come down?
- Will the rise in interest rates cause a recession?

The answer to these questions will set the tone for markets globally because all asset classes are, to some extent, priced off the expected government bond yield (theoretical risk free rate).

The chart below shows the Consumer Price Inflation (CPI) rate for the major economies. This is a year on year comparison and measures how much prices have changed against this time last year. We are now at the stage where the rapid rise in energy prices following the Russian invasion of Ukraine will fall out of the year on year comparison and be replaced by falling prices for energy as gas and oil prices have fallen back from their peak. This will push inflation lower at quite a pace and has the potential to push inflation below 5% quite quickly in some areas.

As can be seen from this chart, US inflation looks to have peaked and this should be followed by Eurozone and hopefully UK inflation.

Chart 1: CPI – Annual rate of Inflation - Five Years to December 2022



Source: Bloomberg

Notes: UK: UK CPI EU Harmonised YoY NSA (Ticker: UKRPCJYR Index); US: US CPI Urban Consumer YoY NSA (Ticker: CPI YOY Index); Eurozone: Eurostat Eurozone MUICP All Items YoY Flash Estimate (Ticker: ECCPEST Index); Japan: Japan CPI Nationwide YOY (Ticker: JNCPIYOY Index)

In addition to falling energy prices due to a warm winter in the northern hemisphere lowering demand and enabling Europe to replace Russian gas with gas from other sources, the common thread on inflation is that the global supply chain disruptions post Covid are being solved as shown by falling shipping rates. The chart below shows the cost of shipping a standard container from China to the US west coast.

Chart 2: Container shipping rates

This chart is echoed in second hand car prices which are now falling and further evidenced by the recent cut in the list price of Tesla's model Y by 20% amongst other data point,s all indicating that supply chains are becoming efficient again.

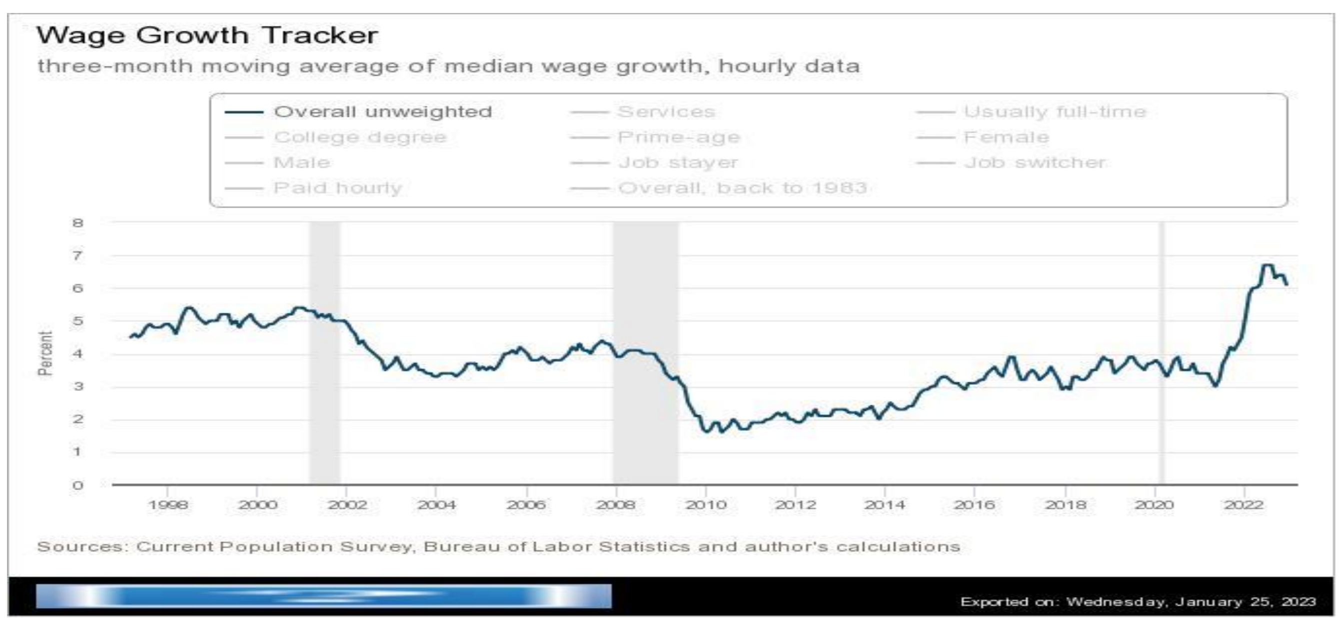
However, in the US, part of the inflationary problem is a very tight labour market which has been pushing up wages. This will only change when the economy slows, reducing the demand for labour and raising unemployment. Arguably, this can only be achieved by causing a recession. Historically, we have not seen an increase in US interest rates of the current magnitude, over a such a short period of time, without it causing a recession.

Even as inflation slows in the US, it is energy and food inflation which is coming down. Wage inflation and service sector inflation will be much harder to squeeze out of the system and I am concerned that the US Federal Reserve (US Fed), which sets US interest rates, may hold interest rates higher for longer than the market now expects.

The chart below shows the US unemployment rate which is still at multi decade lows suggesting little slack in the economy and a continuation of wage inflation.

Chart 3: US Unemployment rate

The level of job vacancies continues to run at a multiple of those looking for work and wage pressures are only slowly rolling over..



Within Europe, energy prices have had a much more direct effect on inflation due to the reliance of the region on Russian gas prior to the invasion of Ukraine. The fact the energy prices are now well below the level hit last year will mean that their effect on inflation will fall out of the calculation very rapidly and we will see falling inflation for the region going forward. Nonetheless, I would expect the European Central Bank to continue to raise interest rates for a while yet. Europe does not have such a tight labour market as the US and hence wage growth is likely to come under control much faster in this region providing the Russian war in Ukraine does not cause further disruptions.

Unfortunately, the problem child is the UK where our energy prices are linked to the European gas price and we have a labour shortage in a number of sectors, in part caused by Brexit. When I wrote about Brexit 5 years ago, my expectation was that there would be a short-term cost as regulations changed but that over the long-term, the UK's innovative and entrepreneurial spirit would eventually shine through, the problem was I was unsure of how long that would take, potentially a couple of years or potentially a generation! Unfortunately, not one of the string of governments we have had post Brexit has really thought through how to reorganise the UK economy and to enact detailed regulation to take advantage of leaving the EU. There appears to be no long-term planning and little intellectual foresight at present. The UK is predicted by the International Monetary Fund (IMF) to have the slowest economic growth of all G7 developed countries for both 2023 and 2024 and be the only G7 country where the economy has failed to recover to pre Covid levels over this period.

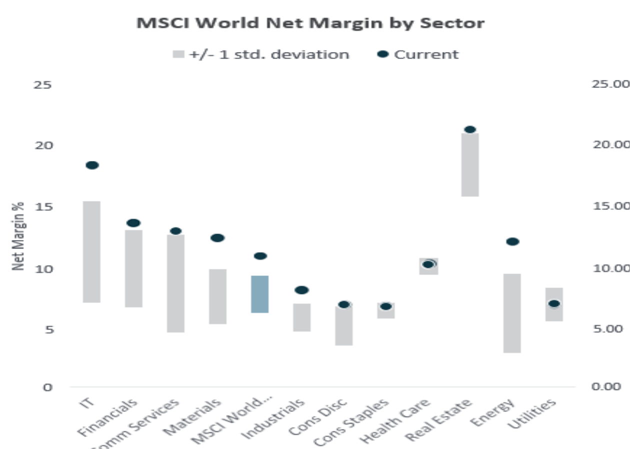
For Investors, there has been a substantial rally in global equity markets from the October lows, with the MSCI global equity index up 17% by end January 2023, investors now seem to be predicting that the US and EU will not enter a recession this year, inflation will fall back below 5% and that central banks will stop rising interest rates soon and start cutting by year end. Whilst this is possible it does not seem the most likely scenario for the future to me. If either the economy weakens into a recession or stays strong forcing central banks to raise interest rates further, then markets may struggle to make further progress for much of this year. The US will remain the lead economy and therefore the actions of the US Fed are likely to set the market tone.

There are three potential economic outcomes for the future to my mind, listed below. I have added my own thoughts on the probability of each outcome.:-

1) A ‘Soft Landing’ with the US Fed hiking rates from the current 4.5% up to 5% over the spring and then pausing during which time US inflation slows allowing the US Fed to cut interest rates into a slowing economy during the second half of this year. In this scenario, Equities would rise further as we would revert to a low interest rate environment (Likelihood 10%).
2) A quick ‘Hard Landing’ as the effect of the recent rises in interest rates finally impacts the consumer, the economy slows rapidly allowing the US Fed to step in and cut rates. In this scenario Equities would fall as corporate earnings expectations take a hit but short-dated bonds would do well as interest rates are cut in the second half of the year. (Likelihood 20%).
3) Persistent underlying inflation and a longer recession. In this scenario, the US Fed raises rates to 5% over the next few months and then pauses as inflation is falling. However, because the fall in inflation is driven by falling energy prices and other more transitory factors rather than falling wage growth, inflation bottoms in the summer but then rises back towards 5% forcing the US Fed to recommence raising interest rates in the Autumn, this would drive both equities and bonds lower. (Likelihood 70%)

I would note that corporate profit margins are at extreme levels at present, as shown in the charts below. It may be that corporates will allow profit margins to reduce in the interest of retaining labour, but the chart suggests there should be little further upside in profit margins from current levels and the potential for earnings downgrades during a recession is high. This would undermine current earnings valuations.

Profit Margins Are Near Peak Levels
Last 20 years



Source: LHS, FactSet. Monthly Data from 31 December 2002 through 30 December 2022. Trailing¹ = Last twelve months RHS, Monthly data from 31 December 2002 through 31 December 2022. Due to data availability Real Estate data is from 30 September 2016 through 31 December 2022. Trailing Net Margin¹ = Previous 12 months.
Index data source: MSCI. MSCI makes no express or implied warranties or representations and shall have no liability whatsoever with respect to any MSCI data contained herein. The MSCI data may not be further redistributed or used as a basis for other indices or any securities or financial products. This report is not approved, reviewed or produced by MSCI.

Declining margins potentially impacting earnings growth in 2023

For use with London Borough of Bromley only

53921

Asset Allocation

The Fund’s tactical asset allocation continues to deviate from the Strategic Asset Allocation (SAA) Benchmark, being overweight equities. The table below shows the changes to the asset allocation over the last year. There was a further small

drawdown into the International Property fund during the last quarter, this was financed from the US Dollar cash holding. The increasing underweight in Bonds is a function of relative performance of these asset classes over the year to date. Despite the fall in global equity markets over 2022, the fall in other asset classes was greater. This has lead to the overweight in global Equities increasing over the last year.

Asset class	Asset Allocation as at 31/12/2021	New benchmark going forward	Position against the benchmark	Asset Allocation as at 31/12/22	Position against the benchmark
Equities	65.8%	57.5%	+8.3%	67.0%	+9.5%
Fixed Interest	10.7%	12.5%	-1.8%	9.7%	-2.8%
Property	5.3%	5%	+0.3%	5.3%	+0.3%
Multi-Asset Income	17.2%	20%	-2.8%	16.7%	-3.3%
Int'l Property +US$	1.0%	5%	-4.0%	1.3%	-3.7%

Figures may not add up due to rounding

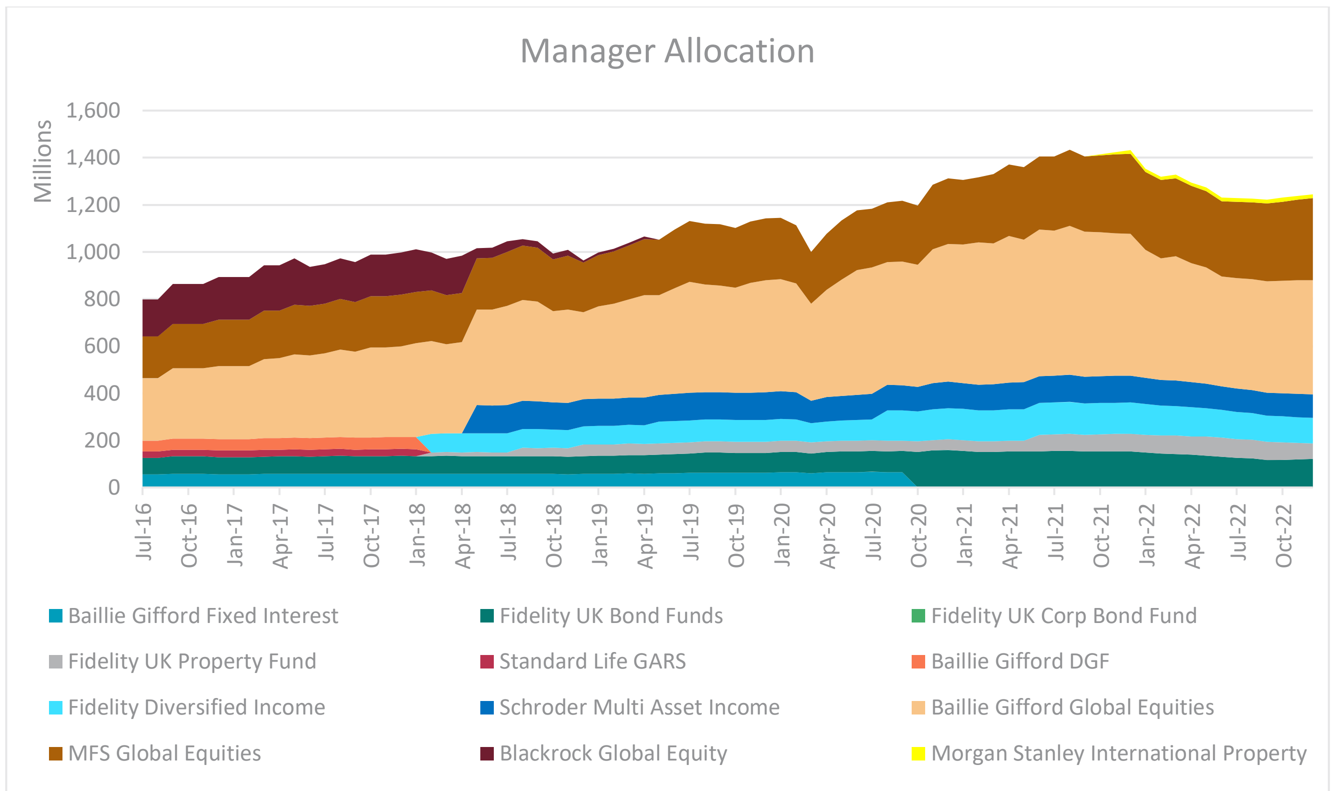
In early Novermber your officers and the Chair held their triennial meeting with the Fund's asset managers to discuss expecations for future investment returns. There was a consensus on a major change in asset valuations driven by the rising Government Bond yields and, whilst a number of managers saw some attraction in various of the alternative asset classes such as Infrastructure, the main improvement in expected returns is in the liquid asset classes of equities and bonds partly because these have been the fastest to reprice lower as interest rates have risen. Because of this, and as discussed at the last Pensions Committee meeting, I do not propose any changes to the Fund's Strategic Asset Allocation benchmark at this time. However, as noted above, the Fund continues to exceed the weighting of the SAA towards global equities by a considerable margin.

Since the last Committee meeting equity markets have risen strongly, and, as described above, I see limited further upisde to justify the current overweight position in global equities against the Fund's Strategic Asset Allocation (SAA).

Recommendation – To reduce the Fund's global equity exposure by approximately 5% (£80m) using the proceeds to replenish the cash account supporting the International Property portfolio (£20m) which will cover the expected drawdowns over the next 12 months. Use the remaining proceeds to replenish the two Multi-Asset Income portfolios to the tune of £20m each and add £20m to theFixed Interest portfolio which is focused on investment grade credit. This will increase the yield and cash distribution of the Fund slightly.

The effect of this adjustment is to bring the Fund's actual asset allocation closer into line with the Fund's SAA targets. The split of the global Equity portfolio between Baillie Gifford and MFS was 58/42 as at year end. If the £60m was divested from the Baillie Gifford portfolio this balance would move to 55/45. Whilst the Baillie Gifford portfolio has underperformed over the last 18 months, in absolute terms it had fallen by only 14% over the last year and this will be less given the continued strength in equity mmarkets since the year end.

The chart below shows the Fund's assets by manager/mandate.



Funding level

Date	Assets	Current Liabilities	Funding Level	Discount rate
31/3/10	£429m	£511m	84%	6.9%
31/3/13	£584m	£712m	92%	4.95%
31/3/16	£748m	£818m	91%	4.2%
31/3/19	£1,039m	£945m	110%	3.65%
Current	£1,244m	£1,083m	115%*	?

*This is an estimate!

The Funding level may deviate from the current assumption used in the table above due to the impact of legislative changes e.g. the McCloud judgement, changes to the actuarial discount rate or changes to inflation expectations. All these issues should be expected to increase the current valuation of future pension liabilities: even so, I would estimate that the Fund currently has in excess of 110% of the value of existing pension liabilities. The actuary assumes that future investment returns will cover the accrual of future pension liabilities. The next actuarial revaluation has commenced using the figures from 31/3/2022. I would expect the main change to be the assumptions used for long-term inflation which will have to rise from the 2.4% used in the 2019 revaluation. This will affect the assumptions used for pension increases and salary increases and is likely to increase the cash outflow from the Fund. I will update this table for the next meeting once the valuation report has been received from the actuary.

Cash Flow

The current actuarial review, using March 2022 figures, will confirm the expected cashflow forecasts into the future. As previously stated, your officers have stress tested the current cashflows for the Fund to take into account the potential for higher pension payments given the currently elevated level of inflation (CPI). I do not expect the figures produced by the actuary to differ wildly from the forecasts created by your officers. The Fund can currently cover any increased cash outflow from a temporary jump in inflation through taking the income from the global Equity, Multi-Asset Credit and UK Commercial Property portfolios.

Executive Summary

- Q4 was a very positive quarter for risk assets generally, with equities and credit rebounding from losses in Q3 as investors have grown more optimistic that inflation may have peaked and central banks will soon have reason to end their rate hikes. Inflation still remains uncomfortably high however, and central bank rhetoric has so far remained hawkish. Long-term bond yields showed little overall movement (with the exception of UK gilts returning to normality), while short-term yields generally rose as monetary policy was tightened further. Additional positive impetus was provided by China's relaxing of its zero-COVID policy, improving the outlook for growth in its economy and by the surprising resilience of European gas supplies, reducing oil/gas prices and easing fears of recession: oil and gas finished the year only 10% and 20% above their end-2021 levels. Equity markets rallied this quarter, especially beleaguered European and Emerging Markets, although global equities are overall unchanged from June 2022 levels, despite volatile price moves in this period. The UK was one of the best-performing equity markets and Sterling recovered some of its earlier losses vs the US Dollar. Value stocks (+14.2%) outperformed growth (+4.6%) by a wide margin this quarter.
- **GDP growth and labour markets:** Despite the on-going recovery from the pandemic, the impact of tight monetary policy and the war in Ukraine are expected to slow growth, particularly in the UK and Europe. Labour markets have, to date, remained strong with unemployment at very low levels historically for the US, UK and Europe (3.5%, 3.7%, and 6.0% respectively from the most recent data).
- The 'new' UK Government under Rishi Sunak has restored order to gilt markets and Sterling by promising fiscally conservative plans. Markets have so far looked favourably on this and returned bond yields to their former positions relative to peer yields although this has not entirely fed through to mortgage rates yet.
- **It is worth highlighting the following themes, impacting investment markets:**
    - **Inflation – the story after the peak.** While CPI inflation appears to have now peaked for the US, UK and Europe, concern remains over how rapidly and to what level inflation will fall. There are indications of inflation becoming more entrenched, but investors appear to be pricing in a more rapid cut in rates than that which central banks are currently forecasting. Euro inflation reached 10.6% in October, a fresh high, however this fell in November to 10.1%. Similarly for the UK, a high of 11.1% was reached in October before falling in November. For the US, the high in CPI appears to have been reached in June at 9.1% and has since declined to 7.1%.
    - **Inflation vs Recession – the next stage for monetary policy.** Monetary policy continued to tighten in most major developed countries, with the Fed, the BoE and the ECB all raising rates several times in Q4. Markets now expect rates to peak at ~4.5% for the UK, ~5% for the US, and a little over 3% for the ECB which indicates hiking cycles are coming towards their end. In addition, the Bank of Japan (BoJ) surprised markets by lifting the yield ceiling for their 10-year bond to 0.5% from 0.25%. The BoJ noted this was to restore proper market function, but as the BoJ owns over half of the bonds in issue, investors have questioned if there is another rationale for the change. Prime Minister Kishida has also announced they will discuss the BoJ's inflation target approach when a new BoJ Governor starts his term in April.
    - **A return to fixed income?** The repricing of debt of all forms, following the rapid rises in interest rates last year, has increased yields on many fixed interest asset classes, potentially increasing long-term returns. Interest rates are now in a more volatile phase, in marked contrast to the repressed volatility of the past decade of QE, so this potential for improved returns is likely to come with increased volatility.
    - **Equity valuations reflect "mild" recession – earnings on watch in 2023.** Following the 18% decline in US equities in 2022, they are now trading at 16.5x forward earnings, below the 10-year average of 17.2x, but up from 15x in

Q3. Over the course of Q4, expectations for 2023 earnings fell by -4.4% with much of the negative impact expected in the first half of 2023 and, some of the leading economic indicators (e.g. ISM survey data) are starting to signal a recession. Investors appear willing to look through any potential decline in earnings, but clearly there remains a risk to earnings as corporate profit margins remain elevated by historical standards and inflating costs may yet impact these.

- **Energy crisis: off the boil, but not gone**. While the immediate threat of blackouts in Europe this winter has probably been avoided and gas storage levels are high, the problem is not over. Furthermore. China's reopening is likely to increase demand pressure on global supplies.

- Global equities rose sharply in Q4, as inflation appears to have now peaked and investors expect that central banks will not need to maintain restrictive monetary policies for as long as they have been guiding. Given the rise in equity markets, the VIX which measures equity volatility and can be read as a "fear" gauge decreased by -31.5%, from 32 to 22, although this level is above the pre-COVID-19 average.
  - In the US, the S&P 500 rose by 7.5% and the NASDAQ fell by -1.0% as markets rallied due to falling inflation data, but investors remain wary of growth and tech stocks. A number of tech companies have announced staff layoffs and cost cutting measures in a response to investor concerns.
  - UK equities rallied in Q4, rising 8.7% as investors welcomed the government leadership change and return to a normal market functioning of gilts following the Truss/Kwarteng debacle and subsequent BoE intervention in the Gilt market. Energy price declines amid warmer temperature and rising inventories of natural gas also helped temper inflation expectations. The BoE raised the base rate to 3.5% in December, however two committee members voted to keep rates unchanged which could signal the start of a shift toward more dovish policy. The BoE also expects Q4 GDP at -0.1%, a 0.2% improvement from its November report.
  - The Euro Stoxx 50 rose by 14.9% in Q4 as investors were cheered by inflation data declining in the quarter, albeit it is still at high levels. Inflation in Europe has been particularly high due to the impact of energy prices following Russia's invasion of Ukraine and their consequent impact on European energy supply.
  - Japanese equities underperformed other equity markets, rising by only 0.7% in Q4. Japanese equities performed well in the quarter until core CPI in December was announced at a 40-year high and the BoJ increased the ceiling of the trading range for the 10-year bond to 0.5% (from 0.25%) which proved a headwind for equities. While inflation remains well below other major economies, investors are wary of a hawkish pivot at upcoming BoJ meetings due to the impending retirement of Governor Kuroda. The Yen reached a high (i.e. a weak Yen) of 150 vs the US Dollar during Q4 but ended the year at 131 following the inflation peak and yield curve adjustment.
  - Emerging market equities performed strongly (+9.6%) with sentiment improving in China following the announcement of COVID-19 restrictions easing. US Dollar weakness also provided a boost.

- Medium and longer term bond yields were largely rangebound in Q4 as investors weighed expected declines in inflation against central banks' desires to ensure inflation is stamped out. Additionally, employment data generally has remained strong which provides the impetus for central banks to hike rates now while labour markets are viewed as strong enough to withstand it. In corporate bonds, high-yield credit outperformed as spreads tightened over the quarter but remain around their long-term average level. Emerging market bonds rose 7.8% in local currency and 8.1% in hard currency.
  - The US 10-year Treasury yield rose marginally in Q4 ending at 3.88% from 3.83%. The 2-year yield rose in Q4, from 4.22% to 4.41%, as the yield curve inverted further. US rates rose initially in the quarter as core inflation data continued to be strong and the US Fed speakers maintained the narrative that hawkish policy needed to be maintained. Later in the quarter rates fell though, as markets took the view that the US Fed will pivot and cut rates in 2023 as inflation falls, spurred by recent falls in monthly CPI data. The US Fed raised short term rates to 4.25-4.5% as at end of Q4..
  - The UK 10-year Gilt yield fell from 4.09% to 3.67% and the 2-year from 4.30% to 3.56%. The declines largely reflected markets returning to normal following the spike in yields in Q3 following the disastrous Truss government 'mini budget' and occurred despite the BoE hiking rates by 125bps. While Gilt rates fell sharply over the quarter, UK Gilts now trade in a similar relative position to peer Government bonds as they did before Q3.
  - European Government Bonds had a total return of -2.1% in Q4. Yield curves flattened or inverted during the quarter, as short end rates rose in response to the ECB raising its policy rate to 2.5% during the quarter and noted

it expects to hike rates further based on its inflation outlook. Long-end rates rose less, as investors view inflation as likely to fall steadily. The German 10-year Bund yield increased from 2.11% to 2.57%, and Italy's went up from 4.51% to 4.70%.

  - US high-yield bonds outperformed investment grade, returning 4.2%, and European high-yield bonds returned 4.7%. Investment-grade bonds returned 6.4% in the UK, 1.7% in Europe and 3.6% in the US.

- Energy prices fluctuated during Q4 as investors mulled over China re-opening, risk of looming recessions in Europe, UK and USA and warmer weather than expected reducing near-term demand for natural gas. Precious metals rose as the US Dollar declined and also received a boost from falling interest rates.
  - US gas prices fell -33.9% over Q4, reversing some of the sharp gains earlier in 2022 as winter weather has been warmer than expected (reducing demand) and inventories have been higher than previously expected.
  - Brent crude oil fell -2.3% in Q4. Prices have been volatile as fears of a fall in demand from a global recession and structural trends toward renewable energy have clashed with supply side dynamics relating to Russia's invasion of Ukraine, OPEC production and the US releasing oil from its Strategic Petroleum Reserve. Brent closed the quarter at US$86 per barrel.

Asset Class/ Manager	**Global Equities/ Baillie Gifford**
Fund AuM	£485m Segregated Fund; 389.0% of the Fund
Benchmark/ Target	MSCI All Countries World Index +2-3% p.a over a rolling 5 years
Adviser opinion	Short-term performance has been poor, acceptable longer term.
Last meeting with manager	John Arthur/John Carnegie by phone

  - Gold and Copper rose 9.9% and 11.7% respectively in Q4, with gold rising as interest rates and the US dollar declined, as well as reports of central banks including China and Turkey increasing their purchases. Copper rose as China, a significant copper importer, announced the start of COVID-19 re-opening. Gold and copper closed Q4 at 1,826 USD/oz and 381 USD/lb, respectively.
- Global listed property had another weak quarter, with the FTSE EPRA Nareit Global Index falling -0.3% in Q4.
  - The Nationwide House Price Index in the UK fell sharply over the quarter, with YoY growth at 2.8% for December. This is markedly down from 9.5% YoY growth in Q3, and 10.7% in Q2. The performance by region showed a smaller variance than prior years as the macro environment of high inflation and high mortgage rates are impacting affordability as real wages struggle to keep up.
  - European commercial property remained under pressure in Q4, with the Green Street Commercial Property Price Index down by -7% this quarter and -12% for the 2022 full year.

In currencies, Sterling strengthened sharply against the US Dollar (+8.2%) but fell against the Euro (-0.8%) over the fourth quarter. The principal driver was the appointment of Rishi Sunak as Prime Minister who is viewed as likely to pursue a more fiscally conservative agenda and the BoE's intervention in gilt markets to stabilise yields. Overall, the US Dollar fell in Q4 (Dollar index -7.7%) reversing much of the Q3 gains. Over the year 2022, the Dollar Index rose +8.2%. Notably, the US Dollar also fell against the Japanese Yen by -9.4% in Q4 as the BoJ shocked markets in December by increasing the top range at which the 10-year bond could yield.

Performance report

The Baillie Gifford Global High Alpha portfolio rose by 2.5% over the quarter against a benchmark rise of 2.0%. The portfolio is now behind the index over the last year by -7.6%. Long-term performance is mixed with the portfolio underperforming over 5 years by -0.6% per annum but outperforming its benchmark by 0.6% per annum since inception in 1999.

This is now the second consecutive quarter when Baillie Gifford has marginally outperformed its benchmark. The overriding effect on the portfolio performance has been rising bond yields which have raised the discount rate used to value future cash flows and dividends and hence lowered the valuation of equities, particularly those where much of the value is in the future because they are fast growing. This corresponds to the area where Baillie Gifford invest ('Growth' as a style). Bond yields peaked in the 3rd quarter of 2022 and so this valuation effect has not been a negative drag on the valuation of 'Growth' style equities over the last 6 months. The underperformance of high growth companies, driven by the rising discount rate has been pretty indiscriminate and whilst Baillie Gifford have made a number of errors over the last few years, I would hope that their skill in analysis and idiosyncratic stock selection will now add value as the major dislocation in bond yields should now be behind us.

Asset Class/ Manager	**Global Equities/MFS**
Fund AuM	£348m Segregated Fund; 28.0% of the Fund
Benchmark/ Target	MSCI World Index (Developed Markets)
Adviser opinion	This portfolio should outperform in a more inflationary environment
Last meeting with manager	Elaine Alston/John Arthur 26/1/23

MFS focuses on companies with a below market valuation but where returns are consistent and competitive positioning within their industry defensible. This makes them more stable in an environment where inflation is rising as they retain more pricing power.

The MFS portfolio rose 5.8% against a rise in the benchmark of 1.9% in the fourth quarter, the portfolio has now outperformed its benchmark by 10.5% over the last year having previously struggled to add value during a period of falling inflation and low interest rates. The portfolio has added 2% per annum over the last 5 years and 2% per annum since inception in 2013.

With inflation continuing to be an issue I would expect the MFS portfolio to continue to perform well as it is concentrated on companies who are better able to pass cost pressures on to their customers due to their strong market position. The portfolio has been very underweight in technology stocks for a long time as they did not feel the valuations justified investment. With the market fall, a number of stocks in this area now fit with their investment philosophy of strong brands with a defensible franchise and they are looking more closely at both Microsoft and Alphabet (owner of Google).

It is the strong and consistent investment philosophy and process of both the Fund's global equity managers which makes it easier to understand in what market environment each equity manager will out or under-perform the benchmark.

I have always asserted that the Fund's two global equity managers were very different in their investment philosophy and process and because of this, the occasions when they outperform and underperform their benchmarks would be fundamentally different making their relative performance against the benchmark negatively correlated. If that is the case then by combining the two portfolios the Fund should achieve long-term outperformance of the benchmark but with a lower volatility than investing in either manager separately.

I have now analysed 5 years of quarterly performance data and the correlation coefficient between the performance, relative to the benchmark, of Baillie Gifford against MFS is -0.5%. This supports my view, stated above.

The Fund now has two similar Fidelity Fixed Interest portfolios. The UK Aggregate Bond Fund has a benchmark which is 50% UK Gilts and 50% UK non-Gilts; the UK Corporate Bond Fund which has a benchmark consisting entirely of UK Investment Grade Corporates and, as such, contains slightly higher credit risk and achieves a slightly higher yield. The manager can invest outside of these benchmarks with a proportion of the portfolio including into overseas investment grade bonds hedged back to Sterling and higher yielding, non-investment grade bonds. These two portfolios are combined for reporting.

Portfolio	2Q22 performance	1 Year performance	Duration	Yield
UK Agg Bond	3.0%	-22.8%	8.6 years	5.6%
UK Corp Bond	5.8%	-18.4%	6.4 years	6.1%

The combined portfolio rose by 3.8% % over the last quarter but has fallen by -21.2% over the last 12 months. The portfolio has continued to add incremental value against the benchmark over longer time periods and has outperformed its combined benchmark by 0.5% p.a. over 5 years and 0.8% p.a. since inception in 1998. This 25-year outperformance is a good indicator of the value added by the manager. It is often easy to add value in rising bond markets when yields fall as the manager can take on extra credit risk, creating a higher yield in the portfolio. It is far harder for a manager to outperform

Asset Class/Manager	**UK Aggregate Bond Fund and UK Corporate Bond Fund/ Fidelity**
Fund AuM	£120m pooled fund; 9.7% of the Fund
Performance target	25% Sterling Gilts; 25% Sterling Non-Gilts; 50% UK Corporate Bonds +0.75 p.a rolling 3 year
Adviser opinion	Manager continues to meet long-term performance targets
Last meeting with manager	Phone call during the quarter: Paul Harris/John Arthur

when bond prices are falling and yields rising as any credit exposure is likely to fall by more than the index. Fidelity have performed roughly in-line with their benchmark during the current bond market retrenchment.

Bond markets remained volatile over the fourth quarter but focused on the expectation of falling inflation. Against this China has reopened post COVID following mass demonstrations against long running and draconian lock-down measures and this will support global growth over the next few quarters.

Markets now appear to be pricing a severe credit default risk in the expectation of a major recession, this does not fit with the mood in global equity markets which seem to be assuming a more gentle slowdown with limited recession risk and with a number of indicators suggesting that inflation has now peaked, the environment should be more supportive for bond yields.

Asset Class/Manager	Mult-Asset Income / Fidelity
Fund AuM	£110m Pooled Fund; 9.0% of the Fund
Performance target	LIBOR +4% including a yield of 4% per annum
Adviser opinion	
Last meeting with manager	Meeting 26/1/23

Asset Class/Manager	Multi-Asset Income / Schroders
Fund AuM	£98m Pooled Fund; 8.0% of the Fund
Performance target	LIBOR +5% including a yield of 4% per annum
Adviser opinion	
Last meeting with manager	By phone during the quarter: John Arthur/ Russel Smith/Remi Olu-Pitan

The Fidelity Multi-Asset Income portfolio rose by 2.1% over the quarter whilst the Schroders portfolio rose by 1.4%. Over 12 months the Fidelity portfolio has returned -12.8% and the Schroders portfolio -11.2%. Over three years the Fidelity portfolio has fallen by -3.1% per annum and the Schroders portfolio by -2.3% per annum. Both these returns are below their benchmark for each period. As previously noted, the benchmarks for these portfolios are of a cash +x style and, as such, will increase by a margin over cash each quarter irrespective of market moves. Whilst both portfolios have underperformed their respective cash benchmarks they do serve an important purpose in that they distribute dividends back to the main Fund which helps cover the cash outflow as pension payments are greater than employer and employee contributions. By removing the need to constantly divest assets from the Fund to cover this cash outflow the Fund is more secure and does not have to sell assets during a period of market stress. This enables the Fund to run a slightly higher risk investment strategy (more equities) which has boosted returns over the long-term.

Returns from these two Multi-Asset Income portfolios have been slightly disappointing and are a close match for the returns delivered by mainstream Multi-Asset portfolios which do not concentrate on delivering income. My expectation was for the income requirement to push the managers to analyse the balance sheet strength of their chosen investments more fully, selecting more financially sound holdings which should have fared better in turbulent markets. In reality, what appears to have happened, is that during the period of ultra-low yields, both managers were forced to take greater investment risk to meet the portfolios' yield requirement. I have spoken with the investment team at Fidelity in some depth and reiterated the expectation that, going forward, the portfolio will be less exposed to general market risk and potentially take more independent, idiosyncratic risk. Both portfolios require a months' notice of dealing and, as such, this should give the managers some comfort for holding some less liquid investment positions which provide a decent yield but are less volatile than the general market.

Asset Class/Manager	UK Commercial Property / Fidelity
Fund AuM	£66m Pooled Fund; 5.3% of the Fund
Performance target	IPD UK All Balanced Property Index
Adviser opinion	
Last meeting with manager	Phone calls during the quarter John Arthur/Paul Harris

The Fidelity UK Property portfolio fell by 15.8% over the quarter as valuations caught up with the rise in bond yields. Over three years the portfolio has risen by 2.4% p.a. outperforming its benchmark by 0.2% per annum. This has mainly been driven by the redevelopment of almost a quarter of the portfolio over the last few years with each redeveloped property returning to the market with a higher rent roll and therefore valuation.

Despite the weaker market environment, tenant demand has remained resilient and, with UK Gilt yields stabilising, liquidity is re-entering the market and giving a greater degree of conviction over pricing.

Asset Class/Manager	International Property / Morgan Stanley
Fund AuM	US$80m(£57.5M) committed / £12.3m drawn. Limited Partnership; 1.0% of the Fund

Performance target	Absolute return
Adviser opinion	
Last meeting with manager	Phone calls during the quarter John Arthur/Gareth Dittmer

The International Property portfolio is now valued at £12.3m following a drawdown this quarter. The Fund currently holds £1m in US Dollar cash and £3.8m in Sterling cash to cover further drawdowns and is cash positive when distributions from other portfolios are taken into account. However, the manager expects to speed up the rate of investment through 2023 as prices are beginning to look more attractive although this may be back end loaded over the year. I would plan for drawdowns of £30m for 2023 and as such there is a requirement for additional cash to cover this (see earlier recommendation on raising cash via a sale of part of the Baillie Gifford Global Alpha portfolio).

Your manager believes that there will be opportunities to acquire assets from, or provide capital solutions to, public companies, funds and owners in need of liquidity as prices reset to reflect higher bond yields giving the potential to provide attractive risk adjusted returns relative to prior years within the portfolio. The existing assts are still performing well with an expected Internal Rate of Return (IRR) of 16% against a forecast of 18% at the time of investment with some assets in Japan (around Tokyo) approaching sale post partial rebuilds.

Meadowship Homes

This comment is based on my understanding of the information I have received.

Whilst I do see some value in the Index-Linked Gilt market for the first time in many years as real yields return to positive territory, I have some concerns with the pricing of the deal as I see it.

The investment would be illiquid and the terms if accepted now would remain for the entirety of the contract term. There would be no secondary market in the Bond.

I see the credit spread as low for a business of this size. At 125bp over the relevant gilt. Senior corporates can borrow around the 50-80bp with smaller companies borrowing at much higher rates.

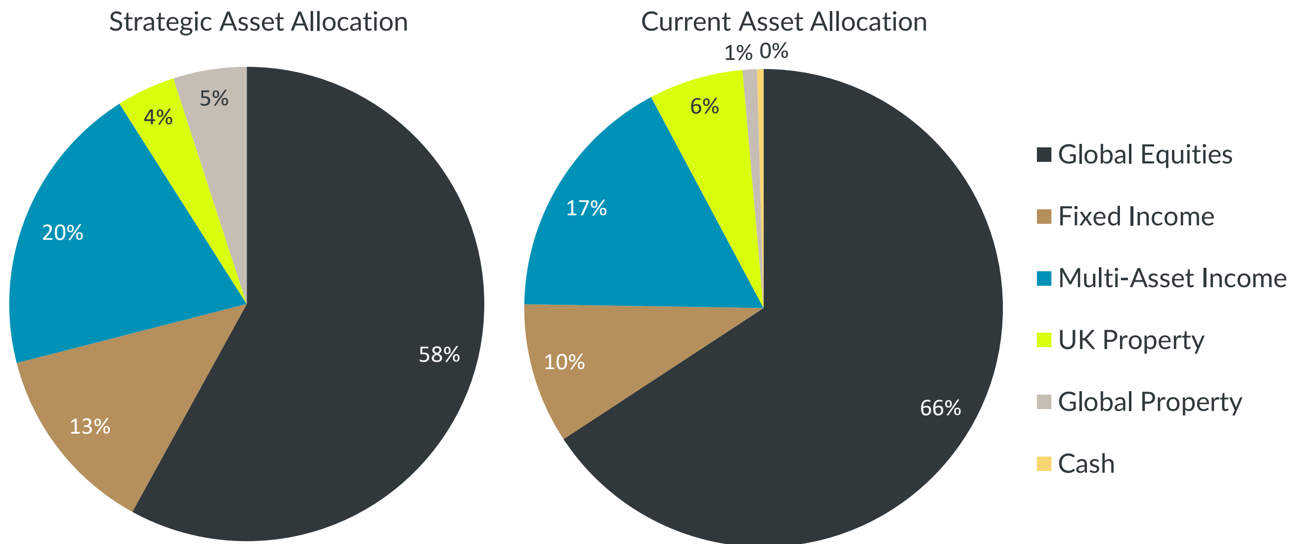
Is there any collateral supporting the bond? If not then the Fund has no protection if there is a fall in rental yield or any other negative impact on the borrower.

The assumed inflation rate is 2.5% for the next 22 years, Whilst this may be in line with current market pricing my own expectation is that we are entering an era of slightly higher inflation over the longer term and I certainly see a transition period of 5-10 years before inflation is stable at a sustainably low level.

Summery – I see the terms as relatively poor value from an investment viewpoint compared to other alternatives available to the Fund at the current time.

Currency Hedging

Figure 1: SAA and Current Asset Allocation (as at 30 September 2022)



The pie charts above set out the Fund's Strategic and current Asset Allocation. Of the asset classes the Fund is invested in, only the Fixed Interest and UK Commercial Property investments are held in Sterling. In addition, about a third of the Fund's investment into Multi-Asset Income will be in Fixed Interest and therefore held in or hedged back to Sterling. In particular, the exposure to global equities is unhedged which means the currency exposure mirrors the country breakdown of the index. (over 60% US Dollar exposure) within the Fund's Strategic Asset Allocation. Against this the liabilities, in terms of current and future pension payments, are all Sterling based. Insight, the investment manager, estimates that the Fund has £820m of unhedged currency risk, a 10% rally in the value of Sterling would therefore reduce the value of the assets of the Fund by £82m, if nothing else changed. Of course, no one factor influencing asset prices acts in isolation and it is fair to argue that, for those companies manufacturing in a country with a weakening currency, the terms of trade improve, giving the business a competitive boost.

Does this matter?

No - because the Fund is an open Defined Benefit Pension Fund and therefore any currency swings will even out over time and over the long-term – 20 years plus, Sterling has tended to weaken consistently over the last 150 years.

Yes – Sterling has been very weak over the last 5 years and currencies have a habit of mean reverting (trending towards the average). The currency looks cheap on purchasing power parity (it cost more to buy the same goods in the US particularly, than the UK, even for a fairly standard product e.g. a Big Mac burger or cheese sandwich).The scale of the benefit to the Fund of the recent weakness of Sterling is large and could be reversed.

As an example of the currency effect on global equity portfolios, the recovery in Sterling against the US Dollar in Q4 2022 reduced performance of a global equity portfolio from a 7% return when hedged back to Sterling to a 2% return when unhedged over that period.

It is important to recognise that the Fund does have currency risk due to the impact of holding non Sterling assets against Sterling based liabilities, therefore, the volatility of future performance would be reduce by hedging back to Sterling a percentage of the global equity portfolio.

Operationally, the effect of including a currency hedge creates cashflow considerations. To hedge a currency a manager would purchase 3 month forward currency contracts locking in the predicted exchange rate for that time. This exchange rate would be the current rate plus or minus any interest rate differential. When these currency contracts expiry and change

in the exchange rate will be settled in cash with the Fund either paying to or receiving from the investment manager the profit or loss on the currency contract. If the Fund hedged 50% (£410m) of the global equity portfolio back into Sterling and Sterling weakened by a further 10% from current exchange rates then the Fund would have to pay the investment manager £41m in cash. This would require selling assets to settle the payment. Obviously if Sterling appreciated then the payment would be from the investment manager to the Fund and the Fund would be £41m better off.

One of the strengths of the Fund at the present time is that it can cover its forecast cashflows into the future. In order to avoid becoming a forced seller of assets as Sterling weakens one solution would be to have the currency manager run a portfolio of £40m short dated bonds (yielding currently around 4%). This then becomes the collateral backing the currency hedge and would only require the fund to replenish this portfolio when Sterling had fallen from current levels. Of course, f Sterling appreciates then money would flow into this portfolio and the buffer covering any future Sterling weakness would increase.

In terms of cost Insight, as an example, would charge 2bp on the value of the hedging portfolio plus a fee to manage any short dated bond portfolio acting as collateral.

I believe approximately 50% of LGPS Funds hedge an element of their global equity portfolios back to Sterling (usually 50%) and 50% do not.

I believe this topic needs further consideration by the Committee but give no recommendation at the current time.

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London Borough of Bromley Pension Fund **Appendix 8**

LGPS Updates

Investment			
Topic	**Description**	**Timescale**	**LBB Status**
1. Responsible Investment / Climate Risk Reporting	The Department for Levelling Up, Housing and Communities (DLUHC) has consulted on proposals that LGPS funds produce their first annual Climate Risk Report by December 2024. Administrating authorities will be expected to manage and report climate risks using four metrics covering absolute emissions, intensity of emissions, data quality and Paris Alignment.	• DLUHC consultation closed in November (120 responses) • Regulations unlikely by 1 April (the proposed start date for reporting) • But data collection still needs to be in place by then	LBB has responded to the DLUHC consultation (as reported to the 1 December 2022 Pensions Committee).
2. Pension Schemes Act 2021 (click here)	The key provisions: enhanced TPR's powers to protect defined benefit (DB) schemes, requiring pension schemes to report on how they manage the financial risks of climate change, tightening the conditions for paying statutory transfer values to protect members from scams and the creation of pensions dashboards.	The new measures will legally require schemes to assess and report on the financial risks of climate change within their portfolios by October 2021 however **the regulations will not apply to the LGPS.** We expect DLUHC to bring forward regulations which will require similar levels of risk assessment and reporting later this year. A second consultation on DB funding is currently underway with a closing date of 24 March 2023: Link to TPR Second Consultation	LBB will keep a watching brief and, through consultation with the Pensions Committee, respond to further developments, guidance and regulations as and when they are published.

3. Investment Policy - pooling	DLUHC is expected to consult on new statutory guidance on LGPS asset pooling. This will set out the requirements on administering authorities and replace previous guidance. SAB opinion: • A variety of models are still being explored • Lack of direction and consistency of interest from Ministers • Greater clarity and transparency are the keys • Focus on desired outcomes and success criteria	• Expected in 2023	LBB will keep a watching brief and, through consultation with the Pensions Committee, respond to further developments, guidance and regulations as and when they are published.
4. The Boycotts, Divestments and Sanctions Bill	It is expected the Bill will cover all public bodies and be wide ranging, covering everything related to expenditure, procurement, investment and treasury management. The Bill is intended to ensure that decisions made by a public body are in accordance with UK and foreign policy. Public institutions, including local councils, would be prevented from creating independent sanctions and boycotts against: • Foreign countries or those linked to them • The sale of goods and services from foreign countries • UK firms which trade with such countries	• We understand that a draft Bill is imminent.	LBB will keep a watching brief and, through consultation with the Pensions Committee, respond to further developments, guidance and regulations as and when they are published.

Governance			
Topic	**Description**	**Timescale**	
1. The Good Governance Project. (click here)	The SAB expects almost all of its recommendations being taken forward: • The LGPS senior officer • Workforce strategy • Monthly data collection mandated • Administration KPIs • Enhanced training requirements • Demonstrating compliance and offering resilience	• Consultation on final regulations expected in 2023	As and when related regulations are published by DLUHC an action plan will be produced.
2. Cost control mechanisms for the LGPS following the 2016 Valuation	The "employer costs cap" was introduced by the Public Service Pensions Act 2013. Its aim is to cap the cost of the scheme to employers. The employer costs cap also includes a "cost floor". The employer costs cap is reviewed at each scheme valuation: every 3 years for the LGPS. If the ceiling or floor are breached, there is a consultation to allow the scheme manager, employers and members to agree the steps needed to bring costs back within target. These steps might include changes to future benefit accrual, or to employee contributions. The Government had considered the cost control mechanism to be closed for the 2016 valuation as it determined that the cost to employers for McCloud remediation should be included in the calculations. Adding the expense of the McCloud remedy has been challenged by judicial review brought by several unions in late January 2023.	Further consultation on changes to the cost control mechanism are expected in 2023.	LBB will keep a watching brief and, through consultation with the Pensions Committee, respond to further developments, guidance and regulations as and when they are published.

Topic	Description	Timescale	
	If the Government were to be defeated on this point then the cost of the scheme would then be considered lower and therefore changes to the scheme would be needed.		
Administration			
Topic	**Description**	**Timescale**	
1. Exit Payment Cap	The Government has stated its intention to bring back the exit cap (also known as the £95K cap). In addition, we understand that it still plans to introduce changes to LGPS and Compensation Regulations at the same time as the exit cap is re-introduced.	No timescale has been provided by Government.	LBB will keep a watching brief and, through consultation with the Pensions Committee, respond to further developments, guidance and regulations as and when they are published.
2. McCloud	The Government has previously outlined the key changes that the Government will make to the LGPS regulations to remove the unlawful age discrimination. The statement confirmed that: • the age requirement for underpin protection will be removed; • the remedy period will end on 31 March 2022; • the underpin calculation will be based on final pay at the underpin date, • even when this is after 31 March 2022; there will be two stages to the underpin calculation: the first on the underpin date – the date of leaving or on the normal pension age in the 2008 Scheme, if earlier. The second stage will be applied when the benefits are paid; and the regulations will be retrospective to 1 April 2014.	• Government response to previous consultation expected February 2023; • Further consultation on draft regulations and statutory guidance expected Spring 2023; • Final regulations expected before summer Parliamentary recess; • Remedy will become law on 1 October 2023; • Any prospective benefit improvement will need to be shown in annual benefit statements from August 2025	Data collection exercise: Under the SAB and LGA guidance, LBB has completed the McCloud data collection exercise (most employers have responded). Resources: Resourcing impact considered and being addressed with Liberate and additional in-house resource Action required (subject to SAB and LGA guidance): - Project management - Data treatments for missing data and overriding current data

Consultation				
	Topic	Description	Timescale	
1.	GMP Equalisation	Following the original Lloyd Banking Group judgement in October 2018 to equalise GMP accrued between 17 May 1990 and 5 April 1997 between male and female members.	The position is currently under further consideration with Treasury.	LBB will keep a watching brief and, through consultation with the Pensions Committee, respond to further developments, guidance and regulations as and when they are published. Note: LBB has completed the GMP reconciliation project (Fund's GMP data vs HMRC). We are now in the process of completing the GMP rectification project.
2.	Goodwin (click here for details)	On 20 July 2020, HMT issued a note confirming that, following a successful case against the Teachers' Pension Scheme (TPS), historical widowers' pensions in the public sector pension schemes discriminated against male members.	Consultation is expected in Spring 2023 on a retrospective award of widowers' pensions backdated to 2005.	LBB will keep a watching brief and, through consultation with the Pensions Committee, respond to further developments, guidance and regulations as and when they are published.
3.	Removing age 75 limit for death grant lump sums	LGPS regulations do not allow for death grant lump sums to be paid if the member is aged 75 or over. The Government now considers this rule to be discriminatory.	Consultation is expected in Spring 2023 on a retrospective award of death grant lump sum to affected beneficiaries backdated to 2011.	LBB will keep a watching brief and, through consultation with the Pensions Committee, respond to further developments, guidance and regulations as and when they are published.
4.	Moving CARE revaluation date from 1 April to 6 April.	The annual allowance (AA) is the maximum amount of pension savings an individual can make in any one tax year, from 6 April to 5 April, that benefit from tax relief. The standard AA limit is currently £40,000. For the 2022 to 2023 tax year, the September 2022 CPI of 10.1% is higher than it has been in recent years. This higher CPI will lead to high revaluation of CARE pensions that active members will accrue in this tax year. However, the CPI increase to the opening value of Pension Scheme pension in the PIA calculation is based on the lower value	Consultation is expected in February 2023 proposing moving the revaluation of pension benefits from 1 April 2023 to 6 April 2023, in effect deferring the inflationary uplift into the next tax year.	

	of CPI in September 2021 of 3.1%. This increases the risk of annual allowance tax charges for active members.		
5. Increase to the minimum pension age	In the Finance Act published on 1st March 2022, the Government has confirmed the increase in Normal Minimum Pension Age or "NMPA" from 55 to 57 with effect from 6 April 2028. The legislation protects members of registered pension schemes who before 4 November 2021 have a right to take their entitlement to benefit under those schemes at or before the existing NMPA.	With effect from 6 April 2028.	LBB will ensure that communications to members reflect this change.
6. Pensions Dashboards Programme (PDP) (click here for details)	Dashboards will enable anyone who has a UK pension not in payment (including LGPS pensions) to be able to view some key details of their pension information. Dashboards will present information from UK-based pension providers including the State Pension. The legislation assumes that all UK pensions will be included. The Pensions Dashboards Regulations 2022 were given approval by Parliament, empowering PDP to set dashboards standards that underpin legislation.	Administering authorities must connect to the dashboards ecosystem within a connection window of 1 September 2024 to 30 September 2024.	In February 2023, LBB signed a contract to June 2025 with its current pensions software provider Heywood Ltd for the purchase of a digital interface to connect to pensions dashboards and conduct any necessary data cleansing to help pensions savers match with LBB data. The contract for Altair (the pensions software) was extended to cover the period to the introduction of the ISP and mitigate risks of data loss or corruption that may arise from swapping pension software at this key time. Officers will concurrently run a full (or framework) tender with interested suppliers who may offer a cost-effective pension system with a potential contract start date from June 2025. The tender process ensures LBB is fully compliant with procurement rules.
7. Task Force on Climate Related Financial Disclosures (TCFD)	TCFD reporting is already mandatory for large private pension schemes, other asset owners and asset managers. The first Local Government Pension Scheme climate risk reports will be completed by December 2024, with which administering authorities will set out their strategies and metrics for managing climate-related risks and	Bromley PF submitted a response to the consultation before the 24 November 2022 deadline, which included the Chairman's comments on pooling and concerns over the additional resources required to comply with more statutory reporting requirements. The	Officers are currently assessing the most cost-effective method of complying with TCFD requirements. Officers initial enquires suggest a cost-effective solution is to ask the Investment Managers to do most of the heavy lifting on TCFD and produce an internal consolidated report and sensitivity analysis. Officers suggest that LGPS reporting requirements are fluid and likely to change.

	opportunities, according to a new government consultation	consultation response was emailed to the Pensions Committee and Board on 17 November. TCFD reporting is likely to be in force by March 2023 with first TCFD reports by December 2024.	**Therefore, Officers will brief on alternatives and seek approval from the Pensions Committee in Q3 2023.**

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Agenda Item 8

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Agenda Item 9

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