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DATE: 6 December 2023

To: Members of the
**PENSIONS COMMITTEE**

Councillor Keith Onslow (Chairman)
Councillor Kira Gabbert (Vice-Chairman)
Councillors Simon Fawthrop, Simon Jeal, David Jefferys, Christopher Marlow, Ruth McGregor and Sam Webber

A meeting of the Pensions Committee will be held at Bromley Civic Centre, Stockwell Close, Bromley, BR1 3UH on **THURSDAY 14 DECEMBER 2023 AT 7.00 PM**

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

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, members of the public may submit one question each on matters relating to the work of the Committee. Questions must have been received in writing 10 working days before the date of the meeting - by **5.00pm on Thursday 30 November 2023**.

Questions seeking clarification of the details of a report on the agenda may be accepted within two working days of the normal publication date of the agenda – by **5.00pm on Friday 8 December 2023**.

4 **CONFIRMATION OF MINUTES OF THE MEETING HELD ON 11 SEPTEMBER 2023, EXCLUDING THOSE CONTAINING EXEMPT INFORMATION** (Pages 3 - 10)

5 **MATTERS OUTSTANDING FROM PREVIOUS MEETINGS**

6 **PRESENTATION FROM MFS**

7 **PENSION FUND PERFORMANCE Q2 2023/24** (Pages 11 - 66)

8 **UPDATES FROM THE CHAIRMAN/DIRECTOR OF FINANCE/PENSIONS INVESTMENT ADVISOR**

9 **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 |
|---|---|---|
| 10 | **PENSION FUND PERFORMANCE Q2 2023/24 - APPENDIX 8** (Pages 67 - 74) | Information relating to the financial or business affairs of any particular person (including the authority holding that information) |
| 11 | **UPDATES FROM THE CHAIRMAN/DIRECTOR OF FINANCE/PENSIONS INVESTMENT ADVISOR (PART 2)** | 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 11 September 2023

**Present:**

Councillor Keith Onslow (Chairman)
Councillor Kira Gabbert (Vice-Chairman)
Councillors Simon Fawthrop, Simon Jeal, David Jefferys, Christopher Marlow, Ruth McGregor and Sam Webber

**Also Present:**

John Arthur, Apex Group Ltd

## 11 APOLOGIES FOR ABSENCE AND NOTIFICATION OF SUBSTITUTE MEMBERS

There were no apologies for absence.

## 12 DECLARATIONS OF INTEREST

Councillor David Jefferys declared that he had been involved in HM Treasury's Patient Capital Review.

Councillor Simon Fawthrop declared that he was a member of the Local Government Pension Scheme.

## 13 QUESTIONS BY MEMBERS OF THE PUBLIC ATTENDING THE MEETING

No questions had been received.

## 14 CONFIRMATION OF MINUTES OF THE MEETING HELD ON 24 MAY 2023, EXCLUDING THOSE CONTAINING EXEMPT INFORMATION

**RESOLVED: That the minutes of the meeting held on 24 May 2023 be approved.**

## 15 MATTERS OUTSTANDING FROM PREVIOUS MEETINGS

**RESOLVED: That matters outstanding be noted.**

## 16 PRESENTATION FROM BAILLIE GIFFORD

The Committee received a presentation from Baillie Gifford representatives, Tim Gooding, Global Equities Specialist, and Chris Murphy, Client Service Director providing an investment update on the London Borough of Bromley Pension Fund.

In considering the presentation, a Member queried why Baillie Gifford had not met its performance target over the five-year rolling period. The Global

Equities Specialist responded that the difficult financial climate of late-2021 and 2022 period had impacted performance in the short term, but that Baillie Gifford had every confidence in the strength of its investment portfolio in the medium to long-term. The Member asked why Netflix was still categorised as a 'Disrupter' investment and the Global Equities Specialist clarified that this reflected the flexibility of the company's business model including the recent introduction of Netflix Ad-Supported Plans that had attracted new subscribers and the significant potential for growth in markets such as China. Tesla Inc was also categorised as a 'Disrupter' as it had similar resilience within its business model and was well-placed to benefit from its innovation in new areas including grid-level battery storage. With regard to complete sales, the Global Equities Specialist advised that Baillie Gifford worked closely with the companies in which it invested, including promoting environmental social governance with a particular emphasis on strong governance and that complete sales were made for a number of reasons including performance and governance.

In response to a question from a Member about the United States, the Global Equities Specialist confirmed that significant investment opportunities were anticipated as a result of the passing of the Inflation Reduction Act, Infrastructure Investment and Jobs Act and the Chips and Science Act, including in the development and deployment of clean energy technology and the domestic research and manufacturing of semi-conductors. The Member also asked about the threat to intellectual property at a global-level and the Global Equities Specialist stated that whilst this remained a concern, countries that had previous disregarded intellectual property were now making their own advances. Another Member flagged a concern around ethical investment with Elon Musk, CEO of Tesla Motors choosing to limit Ukraine's access to satellite services and the Global Equities Specialist advised that the focus of Bailie Gifford was solely in relation to its investment in Tesla Inc. On a similar note, a Member queried the inclusion of Rio Tinto in the Investment Portfolio as this company had been criticised for its destruction of aboriginal rock shelters as well as for its workplace culture. The Global Equities Specialist confirmed that Baillie Gifford continued to engage closely with Rio Tinto regarding its governance and that the company had accepted all recommendations of the external review of its workplace culture. Environmental concerns would be a key area moving forward and Baillie Gifford would be particularly engaging with Rio Tinto around reducing its carbon emissions.

Another Member observed that the value of the fund as of 30 June 2023 was reported differently within the presentation and other sources and underlined the importance of ensuring clarity in financial reporting to support robust decision-making and scrutiny by the Committee.

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

**RESOLVED: That the presentation from Baillie Gifford be noted.**

## 17 PRESENTATION FROM MORGAN STANLEY

The Committee received a presentation from Morgan Stanley representatives, Gareth Dittmer and Brian Niles, Managing Directors providing an investment update on the London Borough of Bromley Pension Fund.

In considering the presentation, the Chairman queried the modal shift to providing mezzanine debt and preferred equity. The Managing Director provided reassurance that investments made up 85-90% of the Portfolio but that the current economic climate had created an opportunity to secure a good return from lending short-term capital as well as by leasing assets on behalf of investment partners. With regard to other investments, the Managing Director advised that the increase in the proportion of spend invested in Europe had been in relation to specific investments that were likely to see a strong return, including hotel properties. The value of an investment in Garfield (UK) had declined significantly since it was first made in 2021 and the Managing Director explained that this was due to the increasing cost of construction and high inflation rates but that a profit was still anticipated on the overall investment. A Member asked about leverage and the sources of debt finance, and the Managing Director advised that borrowing was undertaken on a deal-by-deal basis using local currency and that a credit facility was also in place to help manage liquidity.

A Member observed that the G10 Portfolio snapshot presented an overall picture of the fund and requested that in future, reports focus on the specific investments of the London Borough of Bromley Pension Fund. Another Member queried the stated Projected Gross Return (Local Currency) for G10 of 16.2% / 1.5x as of 2023 and the Managing Director explained that this equated to the current projected return for all fund investments on a pooled basis being 1.5 times the original investment.

The Chairman thanked the representatives of Morgan Stanley for their excellent presentation.

**RESOLVED: That the presentation from Morgan Stanley be noted.**

## 18 LGPS CONSULTATION RESPONSE
**Report FSD23058**

The report presented the draft response of the Local Authority to the Government consultation on accelerating collective pooling of Pension Fund assets, Levelling Up and Private Equity Investments.

In introducing the proposed consultation response, the Director of Finance advised that the draft had been strengthened to reflect Member feedback. This included changes in relation to proposed reporting requirements which were considered to be excessive in some areas, as well as the lack of reporting obligations for regional pools. The Chairman added that the consultation response had also been amended to include minor changes suggested by the CEO of the London Collective Investment Vehicle (LCIV) who had voiced similar concerns to the Local Authority and other London Boroughs on the proposals for accelerating collective pooling of Pension Fund assets, Levelling Update and Private Equity investments.

A key question within the consultation was whether there should be a deadline for the transfer of funds to regional pools and the Director of Finance requested Members' views, suggesting that any such deadline should be set following tri-annual valuation with a further period allowed for asset allocation which for the Local Authority would be some time after April 2026. The Chairman suggested that no date should be set for transfer as it was likely to become a deadline, and this was agreed by Members. Another Member underlined the importance of feeding back how no decision should be made on mandatory investment until changes to the powers or structures of regional pools had been fully implemented. The Member also raised a concern regarding the response to Question 8 which asked whether funds should be able to invest through their own pool in another pool's investment vehicle, observing that any such arrangement would complicate asset ownership and that it would be more effective for Local Authorities to invest their funds directly in another pool. Another Member noted the proposed requirements for 'levelling up' and queried what would happen to investments made under this requirement should there be a change of Government for whom the 'levelling up' agenda was not a priority.

The Committee went on to discuss the response to Question 11 which asked whether funds should have an ambition to invest 10% of their funds into private equity. It was the strongly held view of Members that the lack of transparency of private equity as an asset class combined with a lack of existing in-house and fund manager expertise in this highly-complex area would make any such ambition an inappropriate and risky investment. This was particularly the case as the Local Government Pension Scheme was not a public fund but was a privately-owned fund that the Committee had a fiduciary duty to manage on behalf of Scheme Members. A Member asked that a statement to this effect be included in the consultation response and this was supported by the Committee. Another Member suggested that a paragraph that formed part of the response to Question 11 on investments outside the UK be removed as it contradicted an earlier statement and this was also supported by Members.

The Chairman advised that the draft Local Government Pension Scheme consultation response would be updated in line with the suggestions made with a view to submitting the consultation response by the end of September 2023.

**RESOLVED: That the draft Local Government Pension Scheme consultation response be approved for submission.**

**19 PENSION FUND PERFORMANCE Q1 2023/24**
**Report FSD23060**

The report provided a summary of the investment performance of Bromley's Pension fund in Quarter 1 of the 2023/24 financial year and included information on general financial and membership trends of the Pension Fund as well as details of key developments in the Local Government Pension Fund (LGPS) expected during the next five years.

In introducing the report, the Chairman noted that the Bromley Pension Fund's tactical asset allocation continued to deviate from the Strategic Asset Allocation Benchmark in being overweight in equities and it was proposed to undertake further rebalancing in the form of transferring 5% or £65M from the Baillie Gifford Global Equity Portfolio that was currently managed through the LCIV into a Short-Dated UK Corporate Bond fund managed by Fidelity. This proposal was supported by Members, although a Member underlined that should the transfer be agreed, the effect of this in rebalancing the Strategic Asset Allocation would mean there was no need to revise the Strategic Benchmark which was a subsequent recommendation of the report. It was also recommended to work with Fidelity on the costs and benefits of moving the Fund's fixed interest investments to a single segregated portfolio and should this be supported by Members, an update on this work would be provided to the Committee at its next meeting on 6 December 2023. It was also planned to revisit the Strategic Asset Allocation benchmark at the next meeting of the Committee and a Member suggested that consideration be given to disinvest from multi-asset income funds at that time as the increase in interest rates in recent months had made equity and bond funds a more attractive investment option.

With regard to other matters, the Chairman was pleased to note that progress had been made in implementing the Member Self-Service Pensions Portal and I-Connect (Employer) Portal and that the Member Self-Service Pensions Portal was scheduled to go live to deferred and active Pension Fund Members in October 2023. The Chairman also flagged that a Government consultation was anticipated on the potential removal of the age limit of 75 years for death grant lump sums as such a rule was now considered discriminatory and further updates would be provided to the Committee when available.

Councillor Simon Fawthrop moved that the proposal to switch 5% or £65m from the Baillie Gifford Global Equity Portfolio currently managed through the LCIV into a Short-Dated UK Corporate Bond fund managed by Fidelity be approved alongside the other report recommendations, excluding the recommendation seeking a revision of the Strategic Benchmark. The motion was seconded by Councillor Simon Jeal, put to the vote and CARRIED unanimously.

**RESOLVED: That:**

- **The contents of the report and appendices be noted.**

- **The recommendations in Appendix 5 be agreed as shown below:**

  i) **To switch 5% or £65m from the Baillie Gifford Global Equity portfolio currently managed through the LCIV into a Short-Dated UK Corporate Bond fund managed by Fidelity;**

ii) **Agree to follow up with Fidelity the costs and benefits of moving the Fund's fixed interest investments to a single segregated portfolio; and,**

iii) **Agree the cash management arrangement as highlighted in the Apex report.**

- **Appendix 6 which set out the key developments in the Local Government Pension Fund expected during the next five years be noted.**

**20 PENSION FUND ANNUAL REPORT 2022/23 WITH DRAFT ACCOUNTS**
**Report FSD23061**

The report presented the draft Pension Fund Annual Report and Accounts 2022/23, which set out details of the administration and performance of the London Borough of Bromley Pension Fund during the 2022/23 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.

Councillor Simon Fawthrop moved that the draft Pension Fund Annual Report and Draft Accounts for the 2022/23 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 2022/23 financial year be approved.**

**21 LOCAL PENSION BOARD ANNUAL REPORT**
**Report CSD23089**

The report presented the Local Pension Board Annual Report which had been approved by the Local Pension Board at its meeting on 27 July 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 undertaken by Board Members.

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

**22 LOCAL PENSION BOARD: APPOINTMENT OF BOARD MEMBERS**
**Report CSD23097**

The report sought approval to appoint two Scheme Member representatives to the Local Pension Board as Board Members.

**RESOLVED: That Lesley Rickards and Gill Slater be formally appointed as Scheme Member representatives to the Local Pension Board for four-year terms of office commencing 11 September 2023.**

## 23 UPDATES FROM THE CHAIRMAN/DIRECTOR OF FINANCE/PENSIONS INVESTMENT ADVISOR

The Chairman and the Director of Finance provided a Part 1 (Public) update to the Committee on recent developments relating to pensions.

The Charman advised that the annual Pension seminar would take place on 2 December 2023 and all Members would be invited to attend.

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

## 24 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**

## 25 CONFIRMATION OF EXEMPT MINUTES - 24 MAY 2023

The Part 2 (Exempt) minutes of the meeting held on 24 May 2023 were approved.

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

No Part 2 (Exempt) update was given.

The Meeting ended at 10.03 am

Chairman

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Report No.
FSD23081

# London Borough of Bromley

**PART 1 - PUBLIC**

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| | |
|---|---|
| **Decision Maker:** | **PENSIONS COMMITTEE** |
| **Date:** | **14 December 2023** |
| **Decision Type:** | Non-Urgent Non-Executive Non-Key |
| **Title:** | **PENSION FUND PERFORMANCE Q2 2023/24** |
| **Contact Officer:** | Dan Parsons, Senior Accountant<br>Tel: 020 8313 3176 E-mail: dan.parsons@bromley.gov.uk |
| **Chief Officer:** | Peter Turner, Director of Finance Tel: 020 8313 4668<br>Email: peter.turner@bromley.gov.uk |
| **Ward:** | Borough Wide |

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1. Reason for report

1.1 This report provides a summary of the investment performance of Bromley's Pension Fund in the 2nd quarter of 2023/24. 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, quarterly performance reporting;**

**b) Appendix 6, which sets out the key developments in LGPS expected during the next 5 years.**

**c) Appendix 7, which sets out the Climate Change Scenario report prepared in March 2023 by the Actuary as part of the triennial valuation.**

**2.3 The Pensions Committee is furthermore asked to approve Appendix 8 (see Part 2 Exempt agenda), which is the extension of the WTax contract for withheld tax services for a further two 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 .

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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); £1,269m total fund market value at 31st March 2023

    4.

5. Source of funding: Contributions to Pension Fund

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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.

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Customer Impact

1. Estimated number of users/beneficiaries (current and projected): 6,509 current employees; 6,019 pensioners; 6,443 deferred pensioners as at 31st March 2023

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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 September quarter at £1,268.0m, down £14.7m as at 30th June. The comparable value as at 31st September 2022 was £1,222.2m. 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%).

3.2.5 In February 2023, the portfolio was rebalanced. The Committee agreed to sell £70m of the Baillie Gifford Global Equity Fund to purchase £20m of the Fidelity Fixed Interest Fund, £15m each of the Fidelity and Schroders Multi-Asset Income Funds and put £20m into the US Dollar account awaiting drawdown into the Morgan Stanley International Property Fund.

3.2.6 The Committee voted to pool the remaining Baillie Gifford Global Equity Fund with the London Collective Investment Vehicle. An in-specie transfer finalised on 22nd May 2023 and a new quarterly report on performance (Q2) is available from London CIV and has been included in the agenda pack.

3.2.7 In September 2023, the Committee agreed to sell a further £65m of Baillie Gifford and transfer to a new Fidelity Short Term Bond Fund. This occurred in October 2023. The Committee agreed to further review Asset Allocation at the December 2023 meeting.

3.3 **Summary of Fund Performance**

3.3.1 Performance data for 2023/24 (short-term)

A detailed report on fund manager performance in the quarter ended 30th September 2023 is provided by the fund's external adviser, Apex in Appendix 5. The total fund return for the second quarter was -0.92% against the benchmark of 0.67%. 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 second quarter, and there has been a slight underperformance versus benchmark. In 2022/23 there was a return of -3.72% against a benchmark of -2.59%. In 2021/22 there was a return of 0.7% against a benchmark of 8.7%. 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 -2.7% and 8.0% against the benchmark of -1.8% and 8.3% respectively.

Performance rankings were available at the time this report was drafted. The overall Fund ranked 63rd against the 63 funds in the PIRC LGPS universe for the year to 31st March 2023, 50th over 3 years, 20th over 5 years, second over 10 years and 20 years and first over 30 years.

The following table shows the Fund's long-term rankings in all financial years back to 2012/13 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 | | | | |
| ***2022/23*** | ***-3.72*** | ***-2.59*** | ***-1.6*** | ***63*** |
| 2021/22 | 0.7 | 8.7 | 8.6 | 60 |
| 2020/21 | 34.1 | 23.6 | 22.8 | 2 |
| 2019/20 | -2.7 | -1.8 | -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 31/3/23*** | ***9.1*** | ***9.4*** | ***9.5*** | ***50*** |
| ***5 year ave to 31/3/23*** | ***6.4*** | ***6.8*** | ***5.9*** | ***20*** |
| ***10 year ave to 31/3/23*** | ***8.9*** | ***n/a*** | ***7.3*** | ***2*** |
| ***20 year ave to 31/3/23*** | ***10.0*** | ***n/a*** | ***8.4*** | ***2*** |
| ***30 year ave to 31/3/23*** | ***8.5*** | ***n/a*** | ***7.7*** | ***1*** |

*The most recent LA averages and ranking as at 31/03/23 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 <u>Performance Measurement Service</u>

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 63 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 £0.67m.

3.5.2 The August Year End Accounting exercise for Schools and Academy Employers is underway.

3.5.3 Member Self Service pensions portal went live for deferred and active members in October 2023 and £6K under budget. The I-Connect (employer) portal is being implemented by Aquilla Heywood.

3.6 **Fund Manager attendance at meetings**

3.6.1 Meeting dates have been set to February 2024. 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.

Meeting 21 Feb 2024 – Schroders

## 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 outturn for the 2022/23 pension fund revenue account are provided in Appendix 4 together with fund membership numbers. A net provisional surplus of £24.4m including re-invested income of £11m. A net provisional surplus of £13.4m excluding re-invested income occurred during 2022/23 and membership numbers rose by 459 in the year. In the second quarter of 2023/24 total membership numbers decreased by 158.

5.2 The Director Finance approved the use of a Pension Fund specific Money Market Fund (MMF), for excess Pension Fund cash to be allocated into, to maximise the interest accrued on any cash balances. Officers set up a MMF with Royal London Asset Management (RLAM) and have transferred £15m into this facility.

## 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 Fidelity, London CIV, MFS, Morgan Stanley and Schroders. |

**APPENDIX 1**

# MOVEMENTS IN PENSION FUND MARKET VALUE SINCE 2002

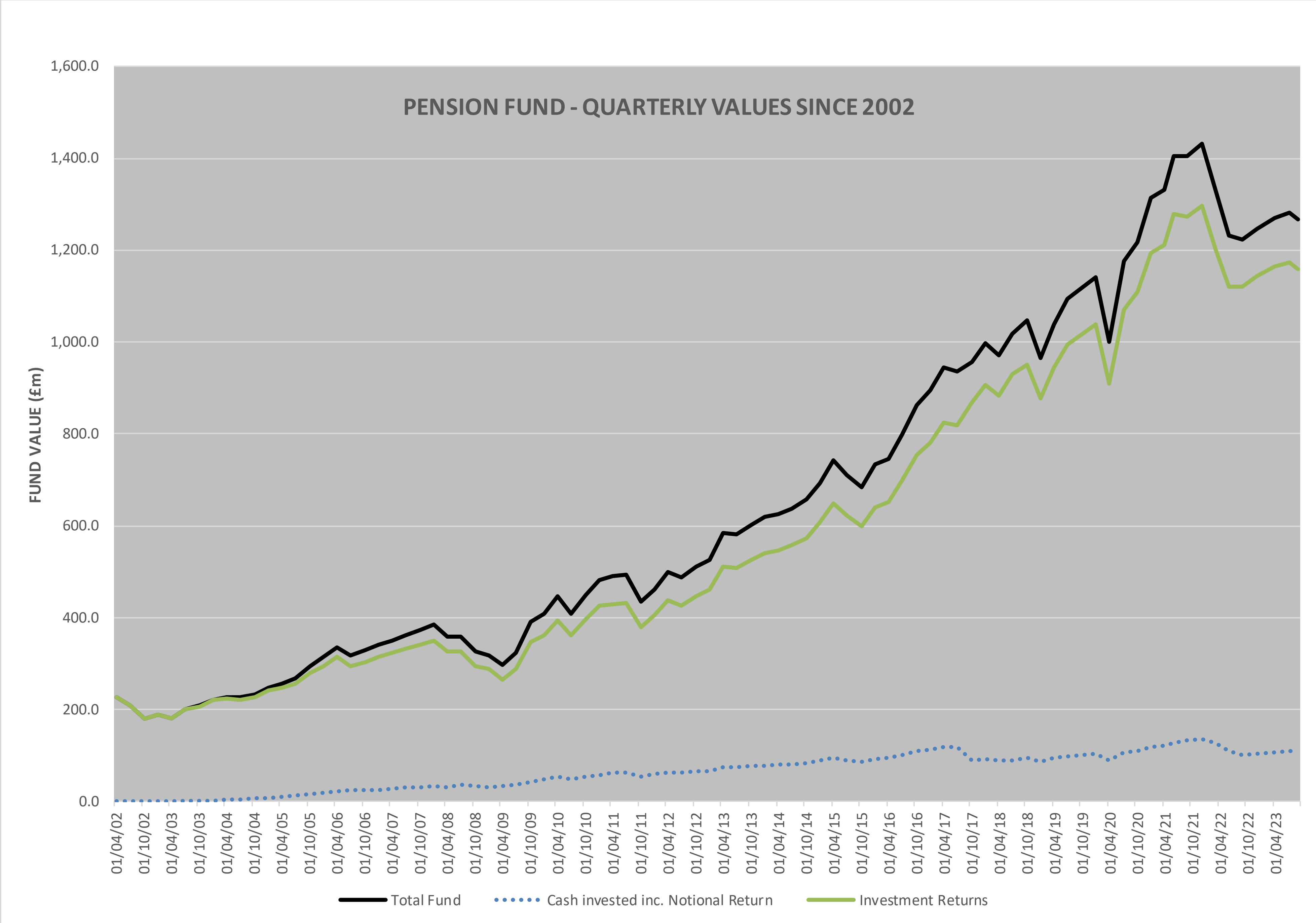
| | Baillie Gifford | | | | | Fidelity | | | | | | | Blackrock | MFS | | Schroders | CAAM | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Date | Balanced Mandate | DGF | Fixed Income | Global Equities | Total | Balanced Mandate | Fixed Income | MAI | Property | Sterling 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 | | | | | | MFS | Schroders | MS | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Date | Global Equities (LCIV) | Total | Fixed Income | MAI | Property | Sterling Bond | USD ILF | Total | Global Equities | 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 |
| 31/03/2023[x] | 438.3 | 438.3 | 78.6 | 124.4 | 65.1 | 63.5 | 20.5 | 352.1 | 350.2 | 114.8 | 14.2 | 1,269.60 |
| 30/06/2023[y] | 454.7 | 454.7 | 74.6 | 120.7 | 63.9 | 61.8 | 20.2 | 341.2 | 359.4 | 113.3 | 14.1 | 1,282.70 |
| 30/09/2023[z] | 435.6 | 435.6 | 74.1 | 118.8 | 63.1 | 61.9 | 13.7 | 331.6 | 364.0 | 113.9 | 22.9 | 1,268.00 |
| | | | | | | | | | | | | |
| | | | | | | | | | | | | |
| | | | | | | | | | | | | |
| | | | | | | | | | | | | |

N.B. Custodian valuations may differ to fund manager reports due to different valuation/return calculation methods and / or timing differences.

# £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
[x] Assets sold by Baillie Gifford (£70.0m) in Feb 2023 to rebalance the portfolio, and fund £20m of the Fidelity Fixed Interest Fund, £15m each of the Fidelity and Schroders Multi-Asset Income Funds and £20m into the US Dollar account awaiting drawdown into the Morgan Stanley International Property Fund.
[y] Assets transferred in-specie from Baillie Gifford (£444m) in May 2023 to Baillie Gifford LCIV Global Alpha Growth Fund.
[z] Assets sold by Baillie Gifford (£65.0m) in Oct 2023 to rebalance the portfolio, and fund £65m into the Fidelity Short Dated Bond 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
01/10/02
01/04/03
01/10/03
01/04/04
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01/04/19
01/10/19
01/04/20
01/10/20
01/04/21
01/10/21
01/04/22
01/10/22
01/04/23
Total Fund
Cash invested inc. Notional Return
Investment Returns

## PENSION FUND MANAGER PERFORMANCE TO SEPTEMBER 2023

| Portfolio | Month % | 3 Months % | YTD % | 1 Year % | 3 Years % | 5 Years % | Since Inception % |
|---|---|---|---|---|---|---|---|
| Baillie Gifford Global Equity | 0.33 | 0.49 | 3.56 | 11.45 | 2.10 | 7.44 | 8.61 |
| Benchmark | (0.44) | 0.73 | 4.18 | 11.04 | 9.47 | 8.41 | 8.06 |
| Excess Return | 0.77 | (0.24) | (0.62) | 0.41 | (7.37) | (0.97) | 0.56 |
| Baillie Gifford LCIV GAG | (2.45) | (4.25) | | | | | |
| Benchmark | (0.44) | 0.73 | | | | | |
| Excess Return | (2.02) | (4.98) | | | | | |
| Fidelity Fixed Income | (0.06) | (0.15) | (4.28) | 0.87 | (8.92) | (2.25) | 4.71 |
| Benchmark | (0.39) | 0.74 | (4.00) | 2.19 | (8.99) | (2.56) | 4.00 |
| Excess Return | 0.33 | (0.90) | (0.29) | (1.32) | 0.07 | 0.31 | 0.72 |
| Fidelity MAI | (0.35) | (0.08) | (1.92) | 0.17 | (2.57) | (0.85) | (0.57) |
| Benchmark | 0.33 | 0.99 | 1.98 | 4.00 | 4.00 | 4.00 | 4.00 |
| Excess Return | (0.67) | (1.07) | (3.90) | (3.83) | (6.57) | (4.85) | (4.57) |
| Fidelity Property | 0.10 | (1.20) | (3.02) | (18.07) | 2.75 | 1.80 | 1.45 |
| Benchmark | (0.14) | (0.42) | (0.04) | (14.34) | 3.18 | 1.76 | 2.33 |
| Excess Return | 0.24 | (0.78) | (2.98) | (3.73) | (0.43) | 0.04 | (0.88) |
| MFS Global Equity | 0.00 | 1.29 | 3.95 | 10.60 | 11.91 | 9.55 | 11.91 |
| Benchmark | (0.48) | 0.62 | 3.90 | 10.48 | 8.96 | 7.88 | 10.52 |
| Excess Return | 0.47 | 0.67 | 0.05 | 0.11 | 2.95 | 1.67 | 1.39 |
| Schroder MAI | 0.21 | 1.38 | 0.88 | 4.96 | 0.78 | 0.21 | 0.27 |
| Benchmark | 0.41 | 1.23 | 2.47 | 5.00 | 5.00 | 5.00 | 5.00 |
| Excess Return | (0.20) | 0.16 | (1.59) | (0.04) | (4.22) | (4.79) | (4.73) |
| Lon Borough Bromley USD | 4.00 | 6.59 | 5.39 | (6.68) | | | 4.77 |
| **Total Fund** | (0.75) | (0.92) | 0.28 | 4.63 | 2.14 | 4.87 | 8.42 |
| **Benchmark** | (0.28) | 0.67 | 2.16 | 6.78 | 5.14 | 5.58 | |
| **Excess Return** | (0.47) | (1.59) | (1.88) | (2.15) | (3.00) | (0.71) | |

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 |
| Jul 23 – Sept 23 - LBB | 0 | 0 | 0 | 0 |
| - Other | 0 | 0 | 0 | 0 |
| - Total | 0 | 0 | 0 | 0 |
| 2023/24 total - LBB | 0 | 0 | 0 | 0 |
| - Other | 0 | 0 | 0 | 0 |
| - Total | 0 | 0 | 0 | 0 |
| 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 – 2022/23 | 3 | 316 | 1 | 25 |
| – 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 |

## PENSION FUND REVENUE ACCOUNT AND MEMBERSHIP

| | Outturn 2022/23 | Provisional as at 30 Sep 2023 | Estimate 2023/24 |
|---|---|---|---|
| | **£'000** | **£'000** | **£'000** |
| **INCOME** | | | |
| Employee Contributions | 8,165 | 8,167 | 8,170 |
| Employer Contributions | | | |
| - Normal | 26,264 | 26,280 | 26,270 |
| - Past-deficit | 478 | 478 | 478 |
| Transfer Values Receivable | 7,891 | 5,213 | 5,213 |
| Investment Income | | | |
| - Re-invested | 11,195 | 11,130 | 11,130 |
| - Distributed to Fund | 15,409 | 13,620 | 13,620 |
| Total Income | 69,402 | 64,888 | 64,881 |
| **EXPENDITURE** | | | |
| Pensions | 29,447 | 29,900 | 29,900 |
| Lump Sums | 4,831 | 4,395 | 4,395 |
| Transfer Values Paid | 3,953 | 2,700 | 2,700 |
| Administration | | | |
| - Manager fees | 5,002 | 5,000 | 5,000 |
| - Other (incl. pooling costs) | 1,606 | 1,600 | 1,600 |
| Refund of Contributions | 142 | 250 | 250 |
| Total Expenditure | 44,981 | 43,845 | 43,845 |
| Surplus/Deficit (-) - including re-invested income (RI) | 24,421 | 21,043 | 21,036 |
| Surplus/Deficit (-) - excluding RI[1] | 13,226 | 9,913 | 9,906 |
| **MEMBERSHIP** | **30/06/2023** | | **30/09/2023** |
| Employees | 6,462 | | 6,208 |
| Pensioners | 6,035 | | 6,064 |
| Deferred Pensioners | 6,524 | | 6,591 |
| | 19,021 | | 18,863 |

Note 1 It should be noted that the draft outturn net surplus of £24.4m in 2022/23 includes investment income of £11m which was re-invested in the funds so, in cashflow terms, there is a £13.4m cash surplus for the year.

# London Borough of Bromley

Quarterly Investment Report

Q2 2023

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# Key Indicators at a Glance

| Index (Local Currency) | | Q2 2023 | Q2 | YTD |
|---|---|---|---|---|
| **Equities** | | | **Total Return** | |
| UK Large-Cap Equities | FTSE 100 | 7,608 | 2.07% | 3.82% |
| UK All-Cap Equities | FTSE All-Share | 4,127 | 1.78% | 2.91% |
| US Equities | S&P 500 | 4,288 | -3.27% | 13.51% |
| European Equities | EURO STOXX 50 Price EUR | 4,175 | -4.83% | 11.51% |
| Japanese Equities | Nikkei 225 | 31,858 | -3.36% | 26.16% |
| EM Equities | MSCI Emerging Markets | 953 | -2.85% | 2.09% |
| Global Equities | MSCI World | 2,853 | -3.36% | 11.36% |
| **Government Bonds** | | | | |
| UK Gilts | FTSE Actuaries UK Gilts TR All Stocks | 2,895 | -0.63% | -4.09% |
| UK Gilts Over 15 Years | FTSE Actuaries Uk Gilts Over 15 Yr | 3,283 | -5.69% | -11.13% |
| UK Index-Linked Gilts | FTSE Actuaries UK Index-Linked Gilts TR All Stocks | 3,714 | -4.69% | -7.16% |
| UK Index-Linked Gilts Over 15 Years | FTSE Actuaries UK Index-Linked Gilts TR Over 15 Yr | 3,839 | -10.67% | -15.87% |
| Euro Gov Bonds | Bloomberg EU Govt All Bonds TR | 208 | -2.54% | -0.08% |
| US Gov Bonds | Bloomberg US Treasuries TR Unhedged | 2,155 | -3.06% | -1.52% |
| EM Gov Bonds (Local) | J.P. Morgan Government Bond Index Emerging Markets Core In | 128 | -3.65% | 3.72% |
| EM Gov Bonds (Hard/USD) | J.P. Morgan Emerging Markets Global Diversified Index | 818 | -2.23% | 1.76% |
| **Bond Indices** | | | | |
| UK Corporate Investment Grade | S&P UK Investment Grade Corporate Bond Index TR | 334 | -1.01% | 1.39% |
| European Corporate Investment Grade | Bloomberg Pan-European Aggregate Corporate TR Unhedged | 219 | 0.70% | 2.69% |
| European Corporate High Yield | Bloomberg Pan-European HY TR Unhedged | 415 | 3.76% | 6.76% |
| US Corporate Investment Grade | Bloomberg US Corporate Investment Grade TR Unhedged | 2,969 | -3.37% | 0.02% |
| US Corporate High Yield | Bloomberg US Corporate HY TR Unhedged | 2,314 | 2.21% | 5.86% |
| **Commodities** | | | | |
| Brent Crude Oil | Generic 1st Crude Oil, Brent, USD/bbl | 95 | 19.48% | 10.94% |
| Natural Gas (US) | Generic 1st Natural Gas, USD/MMBtu | 2.93 | 32.18% | -34.55% |
| Gold | Generic 1st Gold, USD/toz | 1,848 | -6.14% | 1.20% |
| Copper | Generic 1st Copper, USD/lb | 374 | -8.72% | -1.92% |
| **Currencies** | | | | |
| GBP/EUR | GBPEUR Exchange Rate | 1.15 | 1.44% | 2.15% |
| GBP/USD | GBPUSD Exchange Rate | 1.22 | -1.12% | 0.96% |
| EUR/USD | EURUSD Exchange Rate | 1.06 | -2.45% | -1.23% |
| USD/JPY | USDJPY Exchange Rate | 149 | 12.43% | 13.92% |
| Dollar Index | Dollar Index Spot | 106 | 3.58% | 2.56% |
| USD/CNY | USDCNY Exchange Rate | 7.30 | 6.17% | 5.79% |
| **Alternatives** | | | | |
| Infrastructure | S&P Global Infrastructure Index | 2,476 | -7.27% | -4.04% |
| Private Equity | S&P Listed Private Equity Index | 181 | 4.75% | 18.84% |
| Hedge Funds | Hedge Fund Research HFRI Fund-Weighted Composite Index | 18,215 | 1.43% | 4.27% |
| Global Real Estate | FTSE EPRA Nareit Global Index TR GBP | 3,383 | -3.86% | -5.76% |
| **Volatility** | | | **Change in Volatility** | |
| VIX | Chicago Board Options Exchange SPX Volatility Index | 18 | -6.31% | -19.15% |

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

# Performance

The Fund fell by -0.92% in the third quarter of 2023 to a value of £1,268m. As can be seen from the table on the previous page, bonds were noticeably weak during the quarter and the major overseas equity markets also fell in local currency terms. In addition, infrastructure assets fell as the rise in bond yields finally impacted valuations. I would also note the rise in the price of oil and gas over the quarter as this will impact future inflation and was, in part, behind the rise in bond yields (fall in prices). Much of the underperformance against the benchmark was driven by the poor performance of the LCIV Global High Alpha Equity portfolio managed by Baillie Gifford which returned -4.25% over the quarter against a 0.7% rise in the MSCI global equity benchmark.

Over the longer term the Fund is lagging its benchmark over 3-years (by -3.0%) and 5-years (by -0.7%) but with returns of 8.4% per annum over the last 36 years, being above the Fund's actuarial discount rate assumption for future investment returns which will have helped improve the funding ratio.

# Asset Allocation changes since quarter end

At the last Pension Committee meeting on 11th September, it was agreed to divest 5% (£65m) of the Fund's total AuM from the Baillie Gifford Global High Alpha Equity portfolio managed via the LCIV and reinvest into UK Short Dated Corporate Bonds via a fund managed by Fidelity. This transaction took place at the beginning of November. Discussions have also continued with Fidelity regarding moving the existing two bond funds Bromley invest in into a segregated account and this work is ongoing. I was also asked at that Committee meeting to provide an update on the Multi-Asset Income Funds and specifically on the portfolio managed by Fidelity and comment on its recent poor performance, an update is included at the end of this report.

# Comment

The decision at the last Pensions Committee meeting to shift money out of global equities and into UK short duration corporate bonds was driven by the high yields currently available at the short end of the UK bond market (which exceed the investment return required in the Funds actuarial valuation) and by a belief that interest rates in the UK are nearing a peak and, therefore, investing in this area would be low risk (the bonds could be held to maturity with no interest rate risk). The decision was not to invest into longer dated UK bonds at the current time because these were not offering the same yield but also did not seem to have priced in a higher for longer interest rate environment and that, therefore, there was still scope for longer dated bond yields to rise (prices to fall).

In the last quarterly report I noted that there was '*scope for short-term interest rates to be nearing a peak in the US and UK and soon Europe whilst long-term bond yields may still exhibit some volatility as markets come to realise that inflation is not beaten yet; that interest rates will stay higher for longer; that high government debt levels will lead to higher interest charges with greater government bond issuance and that Quantitative Tightening removes a major buyer from the bond markets as central banks let their existing holdings of bonds bought during Quantitative Easing mature and fall off their balance sheet.*'

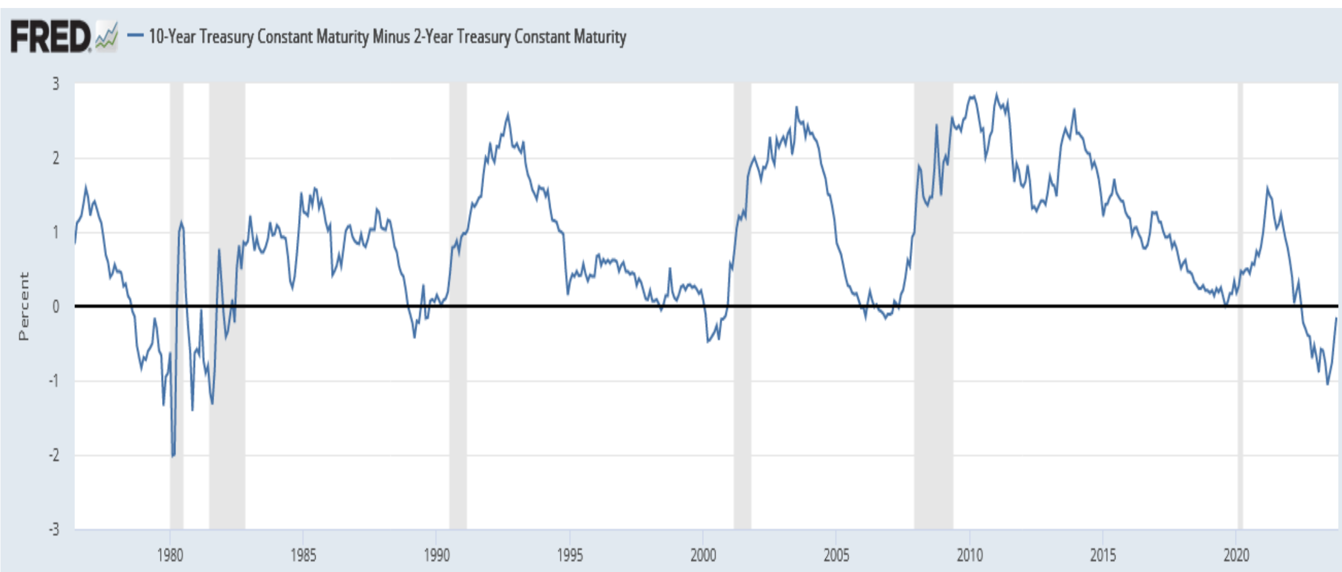
I am not sure which of the factors noted above was the main driver of the rise in longer duration bond yields during the third quarter, but, particularly, in the US, it is the continuing strength of the US consumer and hence the US economy which is concerning markets and this led to a change in the shape of the yield curve undermining market sentiment for risk assets by the end of the quarter.

The situation at the end of the second quarter of 2023 was that both the UK and US had inverted yield curves where short duration bonds were yielding noticeably more than longer duration bonds. This has traditionally been seen as the harbinger of a recession. An inverted yield curve is the market's way of saying that short-term interest rates are peaking because they have risen to an extent that is likely to cause a recession and thereby lead to lower interest rates in the future.

There are two ways a negative yield curve can unwind, either short-term interest rates fall as the economy enters a recession, forcing wages and inflation down and central banks to eventually react to the lower growth profile by cutting interest rates (termed a 'bull flattening' for bond investors) or, for long-term interest rates to rise as markets realise that the economy is not slowing enough to reduce inflation back to target and that rates will therefore either need to rise further or stay higher for longer (a 'bear flattening' for bond investors). Q3 2023 was very much the latter for the US market as the economy has stayed strong despite the sharp rise in interest rates seen over the last 18 months.

The chart below shows the US Treasury 10-year yield minus the 2-year yield. When the line is below zero, 2-year yields are higher than 10-year yields and bond markets are, thereby, predicting a US recession. The shaded areas are actual recessions in the US. As can be seen in the chart, a negative yield curve is a good indicator of a coming recession and this only starts to revert and move into positive territory when markets are confident the US economy is about to enter a recession and that interest rate cuts are firmly on the horizon. During the three most recent occasions when this has occurred (1991, 2001 and 2008) the yield curve normalised (long duration bond yields higher than short ones) through a fall in interest rates expectations pushing the 2-year bond yields down (bond prices up). As can be seen at the right hand side of the chart, during Q3 2023, it looks like this line is again reverting to normality with long-term yields moving towards short-term yields but this time it has been driven by a rise in long-term yields. This is not the market predicting an imminent recession and thereby cuts in interest rates, but is driven by the view that inflation is not completely under control in the US and that either interest rates are likely to rise further or stay elevated for longer or both. The market's view during Q3 2023 is that a US recession is not on the horizon …yet.

**Chart 1: US yield curve**




Source: Federal Reserve Bank of St Louis

This further rise in long-term bond yields, whilst understandable given the strength of the US economy (and the US consumer in particular) acts as a further piece of monetary tightening as it raises the cost of longer term borrowing and does, therefore, increase the likelihood of a recession in 2024.

The US economy has been far stronger than predicted with annualised economic growth hitting 4.9% in Q3 2023, up from 2.1% in Q2, far above expectations at the start of the year. This has been driven mainly by the consumer although there are now signs of some productivity growth. The US consumer is showing remarkable resilience and like Rasputin seems impossible to kill off at present. Nonetheless, recent data does now show the US consumer with a negative savings rate (spending more than they earn) and this cannot continue indefinitely. I think what we are seeing is the effect of using averages for economic data when we increasingly have a bipolar situation with the well off commanding higher pay and supported by resilient equity markets so continuing to spend but the less well off, with less stable employment, struggling to make ends meet, however, this element is lost within the data averages.

There now look to be three possible outcomes to the economic situation.

1) The US economy now begins to slow as the interest rate rises seen so far take effect. In this scenario the US Federal Reserve (US Fed) holds rates high throughout 2024 only cutting once they are confident inflation will return to the 2% level and stay there.

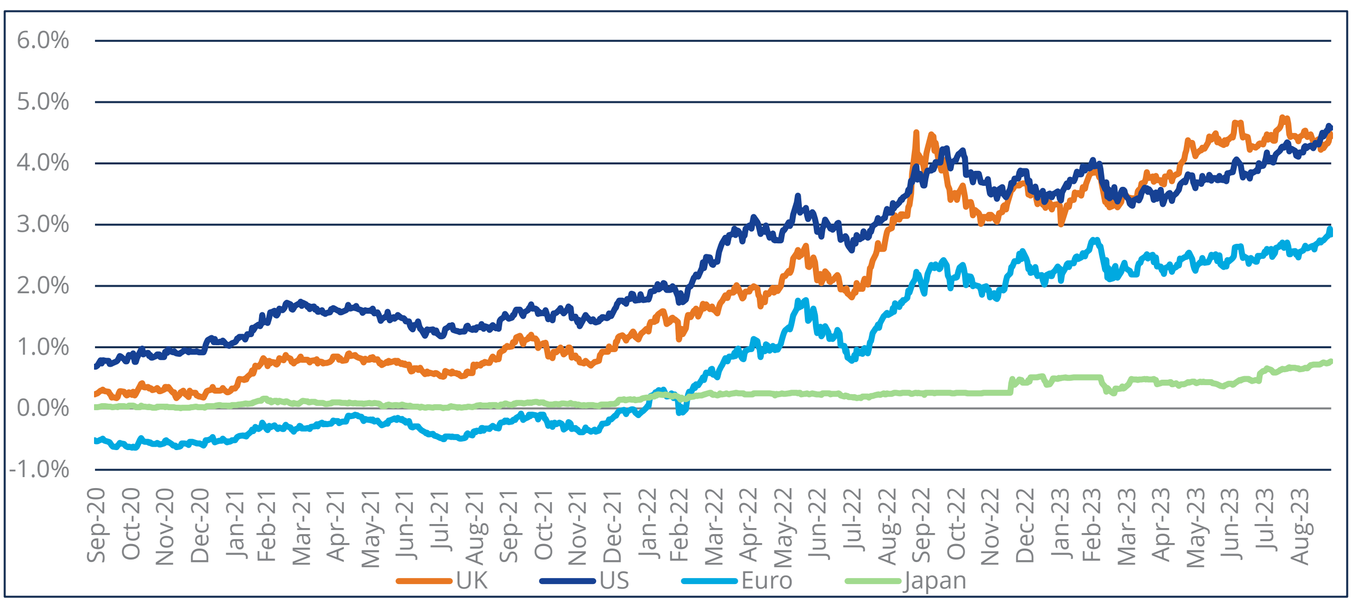
2) Economic growth continues to surprise forcing the US Fed to raise interest rates further. There is then a danger that they are forced into raising rates just as the cumulative effect of the existing interest rate rises hits the economy and forces a sharp slowdown.

3) Something breaks. We saw the effect of the rapid interest rate rises on the regional US banking system in spring of 2022 where a small number of banks holding long-term loans were unable to retain their deposit base as interest rates rose. There will still be other asset owners for whom the rapid rise in interest rates has undermined their investment model. The amount of volatility in long dated bonds is unprecedented. It is quite possible that the US Fed's hand could be forced if markets become particularly stressed. This could be either, by a buyers' strike forcing the US Fed to raise rates to get their bond issuance away or, by a collapse in a specific segment of the market which causes wider collateral damage and forces the US Fed to cut rates to calm markets. Either of these outcomes would be highly destabilising.

Despite the strong GDP growth in the US, it remains my opinion that there will be a US recession during 2024. It will be difficult for the global economy to show much growth in this scenario, particularly with China encountering structural economic change at the same time.

The chart below shows 10-year Government Bond yields. The weakness of the US 10-year bond in particular is noticeable over the last 3 months driven by the strength of the US economy but 10-year Government Bonds have been weak (yields rising, prices falling) across the spectrum of the developed world over the last six months and now sit at decade high yields.

**Chart 2: 10-year Government Bond Yields**




Source: Bloomberg. Notes: US Govt 10 Year Yield; UK Govt Bonds 10 Year Yield; Euro Govt Bond 10 Year; Japan Govt Bond 10 Year Yield

Outside of the US, in Europe and the UK we are seeing much greater economic weakness and, in the UK's case, more stubborn inflation. Interest rates are having a more obvious effect on consumption in these markets and whilst inflation is falling and may continue to do so in the near term, in the UK in particular, it is unlikely to reach the Bank of England (BoE) target of 2% as an element of the inflation appears more structural.

Markets will be cheered by falling inflation but both core inflation (excluding energy and food) and wage inflation are not consistent with a target for CPI of 2% and whilst interest rates may well have peaked, the market may be too optimistic about the pace at which they will fall from here.

**Table 1: Inflation**

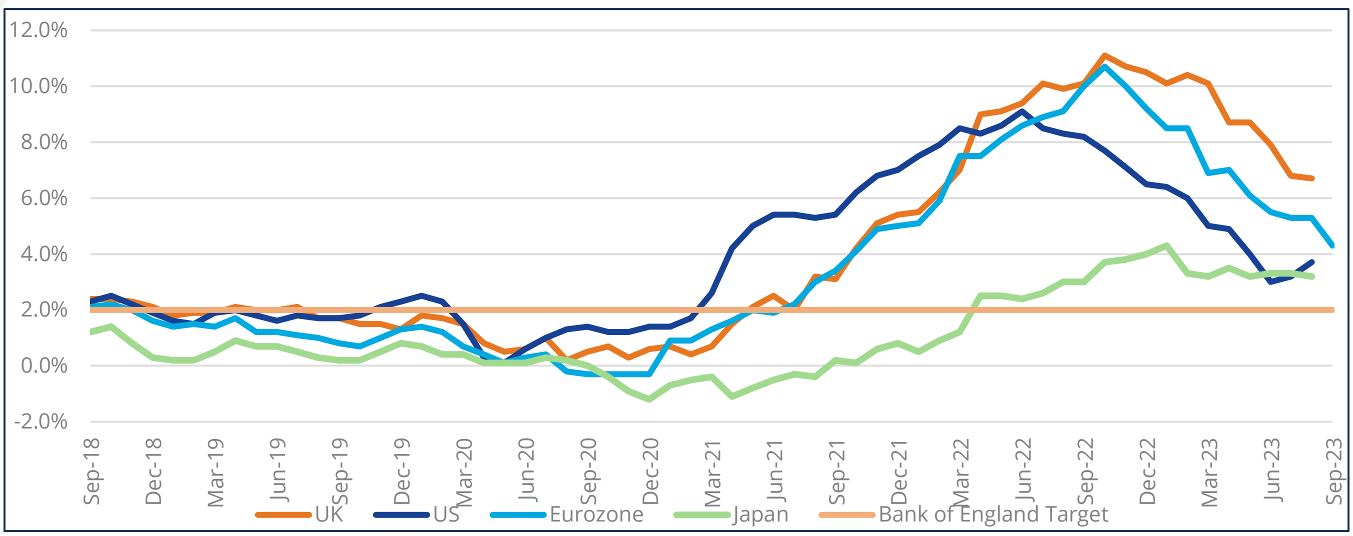
| | CPI | Core Inflation | Wage Inflation | Unemployment Rate |
|---|---|---|---|---|
| **US** | 3.2% | 4.1% | 4.6% | 3.9% |
| **EU** | 2.9% | 5.1% | 5.2% | 6.0% |
| **UK** | 4.6% | 6.1% | 7.9% | 4.2% |
| **Japan** | 3.0% | 2.8% | 1.2% | 2.6% |

Source : various

Longer term, it remains my opinion that we are moving into a period of more volatile inflation. The growth rate at which capacity constraints are encountered is lower than was previously thought, this is not helped by an unstable geopolitical situation. The effect of greater volatility in inflation will be felt in interest rates as central banks attempt to fulfil their twin briefs of low inflation and high employment. This is likely to cause shorter business cycles more akin to the 1970's and 1980's than the last two decades.

On a more positive note, long-term returns, particularly from bonds, are becoming more attractive and the opportunity to earn a return higher than inflation is again feasible at a level of risk that is potentially acceptable to well-funded LGPS Funds.

**Chart 3: Consumer price inflation (CPI)**




Source: Bloomberg

**Markets**

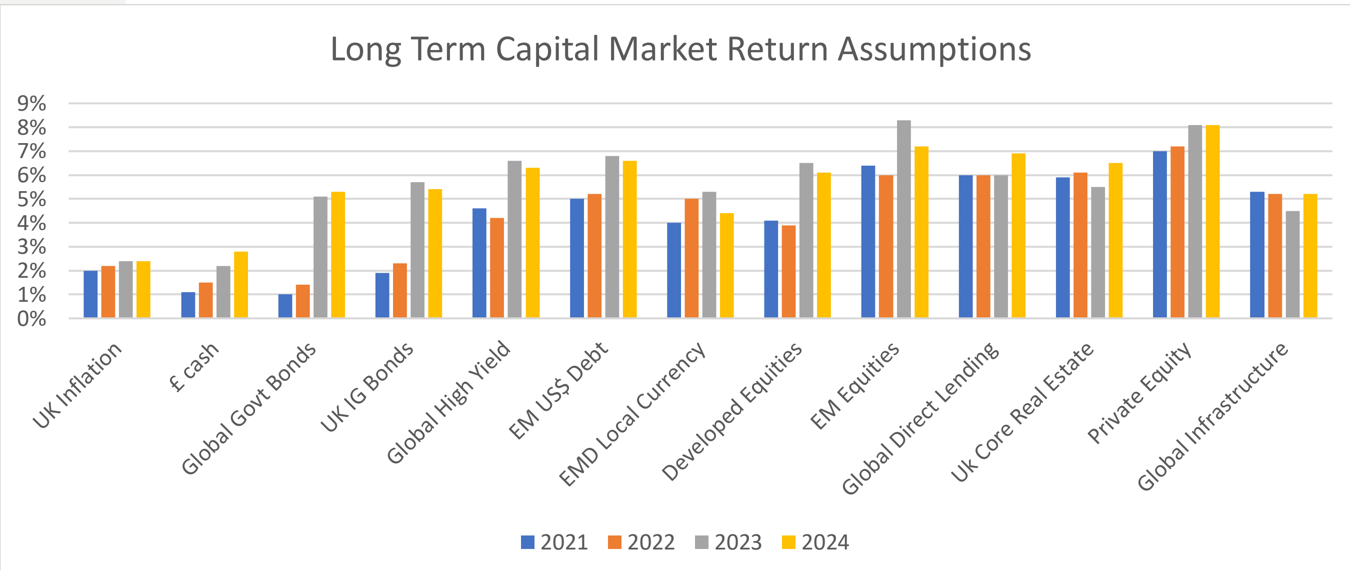
Given the above, my expectation is for interest rates to stay high for the majority of 2024. This continues to make current yields quite attractive, particularly the shorter duration end of the yield curve as short rates are still slightly higher than long rates at present.

In this higher interest rate and slowing economic growth environment I would not expect equities to perform that well, on the one hand they are a partial inflation hedge but when the risks are of a slowing economy and stubborn inflation, the ability to pass costs on to consumers may become constrained. In addition, the higher cost of financing debt will reduce free cash flow and thereby crimp investment.

For Alternatives, it has taken some time to see the effect of interest rate rises on valuations given the illiquid nature of these investments and the opaque nature of pricing but that is now coming through with Infrastructure valuations under some pressure this quarter. I see no rush to increase investments in this area at the current time and remain slightly wary of private equity valuations in particular as the one area where we have yet to see valuations fall but with limited transactions and very little pricing data this gives me little confidence in current valuations. Throughout the last decade an important element of the private equity business model has been the use of cheap debt to leverage up businesses and this will have become more difficult to engineer over the last year.

The chart below shows JP Morgan's Long-term Capital Market Assumptions. These are 10 year return forecasts produced each year with the forecast for 2024 having just been released. We know these forecasts will be wrong but they are built from a single set of assumptions and therefore are comparable with each other and over time. Unsurprisingly, it is the return forecasts for high quality bonds which have seen the largest change over the last 4 years with return expectations for UK Investment Grade Bonds rising from 1.9% p.a. in 2021 to 5.4% in 2024. Return expectations for Equities have also risen but less so.

**Chart 4: Forecast returns by asset class, comparing 2024 with earlier forecasts**




Source JP Morgan

What this chart does not show is the volatility and correlations estimates of these return assumptions. The volatility of returns should be lower in bonds than equities going forward but correlations between asset classes are likely to be more volatile with periods of positive correlation between equities and bonds similar to the period we have just been through in 2022 when both Equities and Bonds fell.

# Asset Allocation

**Table 2: The Funds current asset allocation against the Strategic Benchmark**

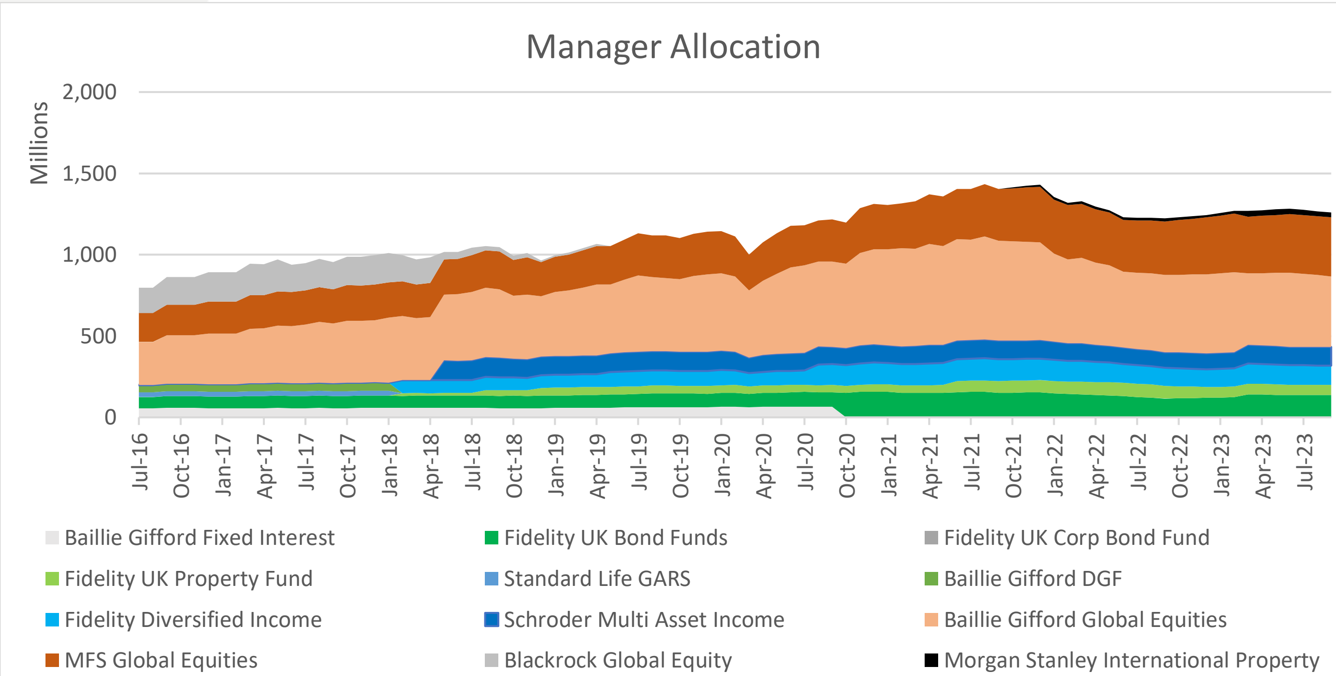
| Asset class | Asset Allocation as at 30/9/2023 | SAA Benchmark | Position against the benchmark | Cash over/under weight |
|---|---|---|---|---|
| Global Equities | 63.0% | 58% | +5.0% | -£63.5m |
| Fixed Interest | 10.7% | 13% | -2.3% | +£29.3m |
| UK Property | 5.0% | 4% | +1.0% | -£12.7m |
| Multi-Asset Income | 18.3% | 20% | -1.7% | £21.6m |
| Int'l Property +US$ cash | 2.9% | 5% | -2.1% | £26.7m |

Figures may not add up due to rounding

**The change in the asset weightings since 30/9/23 does not reflect the move of 5% of the Fund from Global Equities to a short dated bond fund managed by Fidelity.** Including this move will bring the Equity weighting down to on-weight against the Strategic Asset Allocation Benchmark and Bonds to slightly overweight.

The column on the right of this table shows the amount pf money which would need to be moved from each asset class to bring it to an on weight position against the Strategic Asset Allocation benchmark.

**Chart 5: Assets by manager/mandate.**




# Environmental, Social and Governance

**Taskforce for Climate Related Financial Disclosure (TCFD)**

The Financial Stability Board established the TCFD to develop recommendations for more effective climate-related disclosures that could promote more informed investment, credit and insurance underwriting decisions and, in turn, enable stakeholders to understand better the concentrations of carbon-related assets in the financial sector and the financial system's exposures to climate-related risks. The required reporting disclosure has four core elements:

- Governance: The organization's governance around climate-related risks and opportunities.
- Strategy: The actual and potential impacts of climate-related risks and opportunities on the organization's businesses, strategy and financial planning.
- Risk Management: The processes used by the organization to identify, assess and manage climate-related risks.
- Metrics and Targets: The metrics and targets used to assess and manage relevant climate-related risks and opportunities.

Each of these sections will require the Committee to think through its current approach to climate change, how this will evolve into the future and what metrics and targets it will monitor to hold itself to account. In essence, it will need to describe and quantify its existing practice and understanding and think through how this might change into the future.

TCFD reporting has already commenced for large, private sector pension schemes with the LGPS sector expected to follow using 2023/4 data. **I feel it is now best practice for LGPS Funds to complete TCFD reporting even if the current Government dos not specifically mandate action on this point.** It may be possible to get assistance from the LCIV with compiling this report but the Committee will need to discuss and agree its approach to climate change and it may make sense to start by creating a Responsible Investment Statement as part of the Fund's governance documents.

**Carbon Emissions data**

In order to illustrate the carbon intensity of the Fund I have asked each manager to provide the $CO_2$ equivalent ($CO_2e$) of six recognised greenhouse gases covered by the Kyoto protocol ($CO_2$, $CH_4$, $N_2O$, HFC's, PFC's and $SF_6$) and to show these as tonnes of $CO_2$ equivalent per £m of sales (tCO2e/£m) aggregated to the portfolio level. This gives a comparable carbon footprint for each portfolio and their respective index where possible. These figures relate to scope 1 & 2 emissions only. The exception is the property portfolio where the figure is the amount of carbon equivalent emitted (not divided by turnover as this is not appropriate for a property portfolio).

| Portfolio | tCo2e/£m | Benchmark equivalent. | Benchmark |
|---|---|---|---|
| Baillie Gifford Global Equity | 142.1 | 154.9 | MSCI All Countries World |
| MFS Global Equity | 88.06 | 118.11 | MSCI World (Developed Markets only) |
| Fidelity Multi-Asset Income | 205.91 | 10% below 2022 | |
| Schroders Multi-Asset Income | 131.5 | | |
| Fidelity Fixed Interest | 187.4 | | Composite Fixed Interest benchmark |
| Fidelity UK Property | 1,819 tonnes | Data being collected and monitored | Carbon emissions from the portfolio of 36 properties |

I believe these figures to be approximately comparable, they are expressed as a carbon equivalent per million pounds of sales at the company level. Where there is a comparable index figure the Fund's assets are managed with a noticeably lower carbon intensity than the index. Because of the multi-asset nature of the Multi-Asset Income portfolios it is not possible to provide a benchmark figure for carbon emissions for these two portfolios. Each manager has also noted a small number of companies where they are currently unable to provide this data, this is mainly for emerging market companies and where the portfolio is invested in third party funds. We, and the industry, continue to push for greater disclosure.

Because these figures are for scope 1 & 2 emissions only and do not include scope 3 emissions the figures should be seen as indicative only at this stage. What is obvious is the scale of the reporting from each manager is improving.

I will continue to discuss with each manager the best way to report this data going forward and suggest it should be reviewed annually with the intention of seeing the carbon intensity of the Fund's portfolios fall over time. This may be hampered in the short-term by filling out the missing data. Personally, I regard carbon reporting as similar to performance reporting for the Fund, the quarterly data is just a point in time and of itself is of limited use, what is more important is the direction of travel and level of volatility within the figures, each of which can lead to further discussion.

Carbon reporting is still developing and for many of the metrics relies on reporting three scopes of emissions:

- Scope 1 covers direct emissions from owned or controlled sources.
- Scope 2 covers indirect emissions from the generation of purchased electricity, steam, heating and cooling consumed by the reporting company.
- Scope 3 includes all other indirect emissions that occur in a company's value chain.

Whilst progress is being made by companies to quantify all three of these scopes, it is the last, covering the whole of the value chain, which is by far the most complex. The majority of carbon reporting available at present covers only scope 1 & 2 emissions.

# Market Summary

- Inflation has broadly continued to fall throughout Q3 and whilst the US Fed, European Central Bank (ECB) and BoE all raised interest rates during the quarter, the rate of increase has slowed. With inflation decreasing across the board (with the exception of a slight rebound in the US) it is likely that rates will not increase much further. However, the slow pace of the decline in core inflation, as well as an uptick in the US over the quarter and the risk of renewed energy supply shortages as winter approaches, suggest that rates are likely to remain high for a longer period than previously thought: 10-Year UK rates rose very slightly over Q3 to 4.5%, but US 10-Year rates have risen nearly 1% to 4.6%. Labour markets remain robust, especially in the US (unemployment at 3.8% and job openings up 5.8% Year-on-Year in August) and GDP growth remains slow but largely positive.
- Q3 showed a reversal in the first g=half trend for equities. Global equities (MSCI World) fell -3.4% in local currency terms over the quarter, with Value (-2.5%) proving more resilient than Growth (-5.1%) as a style. Japanese and UK equities were notable exceptions to the downward trend, with Japanese equities returning 2.5% (TOPIX Index) in local currency and UK equities returning 1.8%. Performance in Japanese equities as a whole was largely down to the weakening yen which fell further against the US Dollar, however, large growth stocks were negatively affected by the rising interest rates and yields resulting in a -3.4% performance in the Nikkei 225 Total return. UK equities, due to their energy tilt, benefitted from the rising oil prices caused by Russia and Saudi Arabia's extension of voluntary output cuts. US equities fell (-3.3%) as expectations of near term cuts in rates were disappointed. Bonds continued to face headwinds caused by rising interest rates, with all government bonds performing negatively over the quarter and long dated index-linked down over 10%. Investment grade performed better and spreads over government bond yields remained stable over Q3: European Investment grade indices rose marginally, while the US index fell -3.4%. Tightening spreads and higher carry (coupon) allowed high yield to outperform credit. Interest rate-sensitive alternatives (e.g. Real Estate, Infrastructure) also showed a modest decline.

**It is worth highlighting the following themes, impacting investment markets:**

- **Core inflation proving sticky, so interest rates may stay higher for longer.** Inflation fell across the board this quarter (barring the US) with UK annual CPI falling to 6.7% in August, compared to 3.7% for the US and 4.3% for the Eurozone in September (UK data for September is not yet available). Core inflation (excluding energy and food prices) has also been falling, but much more slowly. US and Eurozone core inflation are both above headline inflation at 4.1% and 4.5% respectively. This all suggests the high inflation / high rates environment may last for rather longer than previously thought. This was reinforced by the US Fed which revised median expected rates for 2024 and 2025 up by 0.5%.
- **The US Dollar – tension between reserve currency status and ratings downgrade might cause increased FX volatility.** The US Dollar Index (DXY) steadily increased throughout the first 10 months of 2022 (by around 17.5%) on strong economic data and ongoing geopolitical uncertainty. The net result of this is that the US Dollar is the strongest it has been (barring the 2022 peak) since the early 2000s. At the same time, Fitch became the second major ratings agency to downgrade US Treasuries from an AAA to an AA+ over concerns around the extent of the US government debt and deficit as well as political brinkmanship in the debt limiting process. Whilst the move from AAA to AA+ is unlikely to have major impacts in the short-term, it increases the risk of changes in sentiment toward the USD, causing significant volatility.
- **China's weak Covid recovery and ongoing property crisis remove a key engine of global growth.** Low consumption spending and industrial activity as well as the struggling real estate sector are likely to lead to weak Chinese growth. The composite PMI remains above 50 but is decreasing, with the largest fall seen in services. The property market accounts for a quarter of all Chinese economic activity with real estate employing millions and providing the bulk of most people's savings. As the property prices drop, many people's savings have reduced significantly and so spending has decreased. Local governments rely on land sales to developers, which have dropped and local governments are having to cut back on services as a result. Trust companies that invest heavily in development loans are now seeing significant losses too. In short,

the size and heavily debt-funded nature of the Chinese housing economy has caused it to spill over significantly into the rest of the economy. This has led Chinese growth to dip below US growth, after having been a leader of global growth since the Global Financial Crisis of 2008/9.

- Global equities fell in Q3, following the rally in the first half of the year. The VIX increased over the quarter from 14 to 18, back towards its 2022 level. The sell-off of global bonds has increased yields and put pressure on risk assets.
  - In the US, the S&P 500 fell by -3.3% and the NASDAQ composite also fell by -4%. Optimism over the end of policy tightening proved premature as inflation actually rebounded slightly this quarter and the US Fed indicated median rates would remain higher than expected through 2024.
  - UK equities increased by 1.8%, outperforming global equities. Inflation fell noticeably from 8.7% in May to 6.7% in August. This is the second quarter of significant falls from the highs of around 11% experienced in 2022. Therefore, after the August hike to 5.25%, the BoE kept the rate unchanged during September. The rising oil price contributed strongly to outperformance given the UK's energy tilt.
  - The Euro Stoxx 50 fell by -4.8% in Q3. Inflation continued to move downwards, aided by the ECB's double hike during the quarter. The ECB began to loosen its hawkish rhetoric as a result. The composite Purchasing Managers Index (PMI) has remained in marginal territory at 48.7 (below 50 equating to an economic contraction).
  - Japanese equities continued their strong run in Q3 (TOPIX returned 2.5%), but large growth companies underperformed, hence the Nikkei returned -3.4%. A weakening Yen has boosted exporters, as the BoJ maintains very accommodative monetary policy with core inflation remaining at 2.7%. The Yen fell a further -3.4% against the USD over the quarter. The extent of its weakening is beginning to cause some concern.
  - Emerging market equities fell by -2.9% as concerns over a more extended period of high US interest rates reduced risk appetites. Political uncertainty in Poland and falling Lithium prices in Chile contributed to the negative performance, but the underwhelming Chinese recovery and resurfacing issues with its housing sector were more significant contributors. Turkey notably outperformed following two rate rises, indicative of a more orthodox policy by the Central Bank.
- Medium and longer term bond yields rose over the quarter, as a result of predictions of more persistent high rates. This resulted in negative performance across the main government bond markets. The inversion of the US yield curve, as measured by the 10-year minus 2-year yields, reduced, ending the quarter at around -50bps, as mid and long term yields rose more than shorter bond yields. August saw Fitch downgrade the US's rating from AAA to AA+ leaving Moody's as the only major rating agency keeping US treasury debt at AAA. Fitch cited the increasing debt and deficit as well as 'erosion of governance' and political partisanship in the debt limiting process. In corporate bonds, high-yield credit outperformed as credit spreads tightened over the quarter.
  - The US 10-year Treasury yield rose in Q3, ending at 4.57% from 3.81%, while the 2-year yield rose from 4.90% to 5.05%. US Fed policy rates rose by 25 basis points to 5.25-5.50% in July.
  - The UK 10-year Gilt yield rose from 4.39% to 4.44% while 2-year yields fell from 5.25% to 4.90% due to an increase in demand in shorter-dated Gilts. BoE policy rates rose from 5% to 5.25% in August.
  - European government bonds fell in Q3 as yields rose. Yields rose more in the medium to long-term. German-Italian bond spreads widened as Italian bonds matured and were sold out, Italy's debt continues to grow a considerable amount and the Pandemic Emergency Purchase Program (PEPP) buyback scheme stopped buying new bonds.
  - US high-yield bonds outperformed investment grade, returning +2.2% and -3.4% respectively. European high-yield bonds returned +3.8%, outperforming the +0.7% for European investment grade and -1.0% for UK investment grade.
- Energy prices rose during Q3, as gas prices continued to rebound this quarter, although still sharply down from the pre-winter figures. Oil prices were also a major driver as Russia and Saudi Arabias, extended their voluntary output cuts.
  - US gas prices rose 32% in Q3. Prices remain low compared to their 2021/ 2022 peaks.

- Brent crude oil rose 19.5% over Q3, to $95 per barrel. OPEC production cuts last quarter have now fed through into the price. The US started restocking its Strategic Petroleum Reserve, but slowly. However, it has as little as half of its pre-2022 inventory.
- Gold and Copper fell -6.1% and -8.7% respectively over Q3. Precious metals prices generally fell, while industrial metals went up. Copper is a notable exception partly due to strong links to the Chinese markets. Gold fell given the high yields available on cash alternatives. Gold and Copper closed Q2 at 1,848 USD/toz and 374 USD/lb, respectively.

- Global listed property continued to decline, with the FTSE EPRA Nareit Global Index falling -3.9% in Q3.
  - The Nationwide House Price Index in the UK has declined after its increase last quarter, with the price index down -4.7% for the quarter, but up +4.5% for the last 12 months.
  - European commercial property has also continued to decline in the face of higher interest rates, with the Green Street Commercial Property Price Index down by -1.4% this quarter and -11% over the past 12 months.
- In currencies, the US Dollar strengthened generally throughout the quarter (DXY +3.6%), strengthening against Sterling, the Euro and the Japanese Yen. UK inflation is now in its second quarter of significant decrease. Bitcoin and Ethereum saw strong loses as the US increased regulation, although Ethereum's proof of stake concept has worked well so far since its introduction.

# Performance report

| Asset Class/ Manager | Global Equities/ Baillie Gifford via the LCIV |
|---|---|
| Fund AuM | £436m Segregated Fund; 34.5% of the Fund (inc £4m still held directly with BG) |
| 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 |

This portfolio is now held within the London CIV. It has now underperformed over the last 5 years. I have downgraded the manager to amber given the poor recent performance but remain supportive of their investment approach.

A disappointing quarter for Baillie Gifford, underperforming by 5%, having had two more stable quarters recently. This was a difficult quarter with energy stocks again accounting for much of the gain in the index. Baillie Gifford was underweight these stocks in total. However, markets are rarely entirely rational and at present are being buffeted by short-term noise on the macro outlook with many investors trying to pick the peak in US interest rates as a time to invest. I believe Baillie Gifford has worked hard on reappraising its investments to ensure they are fit for a higher interest rate environment and, once markets revert to looking at stock specific fundamentals, we will see this portfolio start to outperform.

Across the developed world, the non-inflationary rate of growth is now lower than in the past due to a number of inflationary trends being nearer the surface. It is quite possible that we are entering a period of medium-term low growth during which I would expect this portfolio, which concentrates on higher growth companies, to outperform driven by earnings growth and some upside in valuations.

Since quarter-end, £65m has been divested from this portfolio as agreed at the last Pension Committee meeting.

| Asset Class/ Manager | Global Equities/MFS |
|---|---|
| Fund AuM | £364m Segregated Fund; 28.7% 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/Paul Fairbrother/John Arthur 4/12/23 |

The MFS portfolio returned 1.3% over the quarter, outperforming its benchmark by 0.7%. The portfolio has outperformed over the medium and longer term adding 1.4% p.a. over the benchmark since inception in January 2013. MFS retain a 'value' bias within the portfolio and 'value' stocks held better than 'growth' stocks as markets feared higher for longer interest rates given the strength of the US economy.

MFS remain cautious of the economic outlook at present and are stress testing their investments for the durability of the business franchise as well as concentrating on valuation support. Given that I remain somewhat cautious over the market outlook and expect that we are entering a lower growth, more challenging situation for many corporates I do think that it is possible that both the Fund's equity managers could outperform over the next few years as both seem to have an investment approach that fits well with current market dynamics.

| Asset Class/Manager | UK Aggregate Bond Fund and UK Corporate Bond Fund/ Fidelity |
|---|---|
| Fund AuM | £136m pooled fund; 10.7% of the Fund |
| Performance target | 28.8% Sterling Gilts; 28.8% Sterling Non-Gilts; 42.5% UK Corporate Bonds +0.75 p.a rolling 3 year |
| Adviser opinion | Manager continues to meet long-term performance targets |
| Last meeting with manager | Tom Jeffery; Jessica Miley/John Arthur 30/8/23 |

The Fund hold two similar Fidelity Fixed Interest portfolios. The UK Aggregate Bond Fund which has a benchmark that 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.

During the quarter the combined portfolio fell by -0.15% underperforming the benchmark by 0.9%. These performance figures are taken from the  performance report produced by Fund's custodian and differ from the managers report slightly. Any differences are usually due to a different hierarchy of pricing sources and will even out over time but I will query this quarter with the manager. Over the longer term, the portfolio has outperformed, adding 0.7% p.a over the benchmark since inception 25 years ago. I regard this as a highly credible performance.

The third quarter was affected by investors reappraising their interest rate expectations, especially in the US and at the longer duration end of the curve. Longer duration bond yields rose as investors recognised that the US economy continues to grow strongly and that inflation was unlikely to come under control unless US interest rates stayed higher for longer. The Fund's fixed interest portfolio has an average duration of 7.3 years and so was partly affected by this long duration sell off. The current yield of the combined portfolio stands at 6.2% which is usefully above the Fund's actuarial assumed future investment return. This makes current yield attractive and since quarter end the Fund has invested a further £65m into a short duration UK bond fund managed by Fidelity. I would expect to recommend rolling this short duration portfolio into the existing Fixed Interest portfolio, thereby lengthening the duration of the Fund's fixed interest assets, at some stage of over the next 2-5 years as the outlook for consistently lower inflation becomes more believable.

| Asset Class/Manager | Mult-Asset Income / Fidelity |
|---|---|
| Fund AuM | £119m Pooled Fund; 9.4% of the Fund |
| Performance target | LIBOR +4% including a yield of 4% per annum |
| Adviser opinion | |
| Last meeting with manager | Eugene Philalithis; Tom Jeffrey; Jessica Miley/John Arthur 28/9; 24/10; 27/11 |

| Asset Class/Manager | Multi-Asset Income / Schroders |
|---|---|
| Fund AuM | £113m Pooled Fund; 9.0% of the Fund |
| Performance target | LIBOR +5% including a yield of 4% per annum |
| Adviser opinion | |
| Last meeting with manager | John Arthur/ Russel Smith/Remi Olu-Pitan 31/10/23 |

These portfolios are designed to provide yield which is paid back to the Fund each quarter. By guaranteeing that the Fund always has enough cash to pay pensions, under any circumstances, the Fund never becomes forced to sell into unfavourable market conditions but can continue to invest for the long-term.

During the quarter the Fidelity portfolio was flat whilst the Schroders portfolio rose by 1.4%. Over the last year a noticeable performance gap has opened up between the two portfolios with Fidelity up 0.2% and the Schroders portfolio up 5.0%. This is during a period when the Fund's UK Bond portfolios rose by 0.9% and Global Equities were up over 11% in Sterling terms. Because of this period of poor performance by Fidelity, both when compared to Schroders and to the performance of the major asset classes, I have included a more detailed review of the Multi-Asset Income portfolios at the end of this report.

The divergence in performance is less noticeable over the longer term with the Fidelity portfolio down 0.9% p.a over 5-years against the Schroders portfolio up 0.2% p.a. over the same period which confirms that the performance issue has been only over the last year. This compares to the Funds fixed interest portfolio, also run by Fidelity, down -2.25% p.a. over 5-years and global equity markets (as measured by the MSCI All Countries index) up 8.4% p.a. over 5 years. This 5-year performance does bring to the surface that during the era of ultra-low interest rates, both managers were investing heavily into high yielding fixed interest investments as a way of generating the required yield from their portfolio and have delivered performance which is more heavily influenced by bond returns than equities over the medium term.

The Fidelity portfolio remains the more diverse of the two portfolios with a much lower exposure to global Equities. I would regard it as more defensively positioned at the current time.

| **Asset Class/Manager** | UK Commercial Property / Fidelity |
|---|---|
| Fund AuM | £63m Pooled Fund; 5.0% of the Fund |
| Performance target | IPD UK All Balanced Property Index |
| Adviser opinion | |
| Last meeting with manager | Alison Puhar; Tom Jeffery; Jessica Miley/ John Arthur 24/10/23 |

The UK property portfolio fell by 3.0% over the quarter, underperforming a flat benchmark. Over the last 5 years the portfolio has returned 1.8% per annum, in line with its benchmark but above the return from the Fund's Fixed Interest portfolio which has fallen by -2.3% p.a. over the 5-year period.

The portfolio is now yielding 4.5%. This yield is paid back to the Fund to help cover pension payments. The portfolio is mainly exposed to the Industrial segment (48.5% of the portfolio) with a number of Distribution facilities. With 42.5% of the portfolio in the Office segment. The manager sold one portfolio during the third quarter raising £12.3m and has sold a further property since quarter end.

I continue to see this portfolio as well managed and providing an element of diversification from the Fund's heavy global equity exposure.

Given the current state of the UK Commercial property market, the Fund does have a number of investors looking to sell their holdings at the current time. These are predominately corporate defined benefit pension schemes who are looking to move to buyout and therefore need their investments to be liquid and easily valued. I will continue to monitor this going forward to ensure that the manager does not come under undue pressure to realise assets in difficult market conditions.

| | |
|---|---|
| **Asset Class/Manager** | International Property / Morgan Stanley |
| Fund AuM | USD80m(£57.5M) committed / £22.9m drawn. Limited Partnership; 1.8% of the Fund |
| Performance target | Absolute return |
| Adviser opinion | |
| Last meeting with manager | John Arthur/Gareth Dittmer New Haven AGM 11/11/23 |

When the Pensions Committee decided to invest into International Property it was to provide diversification from the Equity and Bond holdings which made up the majority of the Fund. To achieve this the Committee agreed for the mandate to be opportunistic rather than invest in core international property, selecting a manager in Morgan Stanley/New Haven who would be able to adapt to changing market circumstance and who would work with a total return target rather than a formal property index as its benchmark. Given the disruption caused to property markets globally over the last two years by rising interest rates and higher debt costs, I believe this to have been a good decision.

The capital raising for this fund completed in January 2021 and was due to be completed by December 2024, a four-year investment period. The manager has been relatively slow to commit capital into the property market, particularly during 2022 as interest rates rose substantially undermining many regional property markets. The investment rate is now picking up and the manager has now invested 56% of the committed capital of this fund of which 25% has been in the last year post the rise in interest rates, nonetheless, the manager has asked for a 1-year extension to the investment period to end 2025 as a precaution. This request has been sent to the fund's Advisory Committee. During this 1-year extension to the investment period, the managers fee will be based on invested capital only not committed capital. I regard this as acceptable and prudent given the delay in committing capital to date which will have been advantageous to this fund.

The existing portfolio continues to perform well with only 1 investment of concern, a UK logistics site purchased during the lower interest rate environment. Even here the manager does not expect to lose any capital, but is now forecasting a noticeably lower return on this property. Outside of this the manager is still forecasting an Internal Rate of Return (IRR) for the portfolio already purchased only marginally below the level predicted where interest rates were at 1% in many countries. The current environment for investing is more attractive and I would expect new investments, now being made, to outperform the original expectations for this fund and as such for this fund to reach its original return expectations over its full life.

The Fund held $13.7m as US Dollar cash to cover future draw downs into this portfolio. I would expect this amount to cover at least the next 6 months of drawdowns but I will continue to monitor this amount.

# Multi-Asset Income

**Conclusion**

Undoubtedly, markets have changed over the last 18 months and the rise in bond yields has now made them a useful source of income. However, this may not last. My expectation is for more volatile inflation as we are nearer to hitting capacity constraints in a number of areas than was previously assumed. This will mean more volatile interest rates, as central banks attempt to fulfil their twin aims of low inflation and high employment, and the likelihood of shorter economic cycles and more volatility across asset classes. It is quite possible that over the next 5 years we could see interest rates in the UK range between 2%, as the Bank of England (BoE) cuts interest rate in a recession, to 6% as inflation reignites and the BoE raises rates. In the former case of cutting interest rates, yield will again become hard to find.

At the last Strategic Asset Allocation (SAA) review it was calculated that the Fund had a Value at Risk (VaR) of approximately £150m which indicates that once in twenty years the Fund could fall in value by £150m. Given this, I would not recommend raising the risk and hence volatility of the assets within the Fund. In addition, a cash flow analysis of the Fund continues to show a position where pension payments are not covered by pension contributions in the future and therefore some element of investment income is required by the Fund.

I therefore continue to see a Multi-Asset Income portfolio as an appropriate allocation given the Fund's continuing cash flow concerns and the need to secure income from elements of the investment portfolio to cover any shortfall in pension payments in whatever the investment environment in the future.

In the absence of the Multi-Asset income allocation, I would recommend that the Fund hold an income generating asset class that will provide diversification from the predominately equity and bond based current asset allocation of the Fund. Infrastructure could provide a valid alternative with the potential to access the asset class through the secondaries market, a potentially interesting solution at the current time. Alternatives could be Social/Affordable Housing or potentially asking Fidelity to alter their existing Multi-Asset Income portfolio to focus more on Alternative assets (Private Equity, Private Debt and Infrastructure). Because Bromley are the only investors in the specific Multi-Asset Income portfolio managed by Fidelity this latter approach is a feasible option but would require careful consideration as to whether Fidelity are the best managers across these Alternative asset classes. This latter approach would increase the level of diversification within the Fund.

**Background**

As an open Defined Benefit Pension Fund, the LBBPF has never-ending duration unlike a Scheme which is closed to new members and future accrual. It will not move into run-off whilst it continues to accrue benefits for existing members and new employees of LBB and other admitted bodies are enrolled in the Fund and their pension contributions paid. This gives the Fund a number of significant advantages over other investors. Firstly, it does not invest borrowed money so will never be beholden to an outside party for repayments; secondly, it has infinite longevity and so can invest over the long-term and, lastly, its cash flows, in terms of pension payments offset against pension contributions and income from investments, are broadly predictable. This means that the Fund should be able to plan its investments such that it never has to sell assets into stressed market conditions. With a bit of planning, therefore, the Fund should never require markets to provide it with liquidity to trade as it will never be a forced seller of assets. Instead the Fund becomes a provider of capital to markets and during periods of market stress can demand a premium return for doing this.

**Why does LBBPF hold Multi-Asset income Funds?**

Following the 2016 Actuarial triannual revaluation, LBBPF conducted a SAA review which made the following comments regarding cash flow:- '*Based on calculations by Officers and the Scheme Actuary, the Pension Fund will move into a negative cash flow situation in fiscal 2017 as total benefit payments and other expenses exceed the total contributions'*: This raised the issue of the Fund needing to take investment income to cover a negative cash flow. To have not acted to provide a stable cash flow from investments at that time would have undermined the ability for the Fund to remain unbeholden to market conditions.

Following this SAA Review, in Q1 2018 10% of the Fund was moved from a Baillie Gifford Multi-Asset portfolio to the Fidelity Mult-Asset Income portfolio and 5% of the Fund was switched from the Standard Life Multi-Asset (GARS) portfolio into the Fidelity UK Commercial Property portfolio. Additionally, in Q2 2018, a further 10% of the Fund was switched from a Blackrock Global Equity portfolio to the Schroders Multi-Asset Income portfolio. The income from the three new portfolios was not reinvested as all income had been in the past but returned to the Fund to cover any cash flow shortfall.

In subsequent Actuarial revaluations the cash flow of the Fund has been reanalysed and whilst the figures have changed, the direction of travel towards a negative cash flow for the Fund with pension contributions no longer covering pension payments has remained.

**Should Multi-Asset Income funds perform any better than plain Multi-Asset funds?**

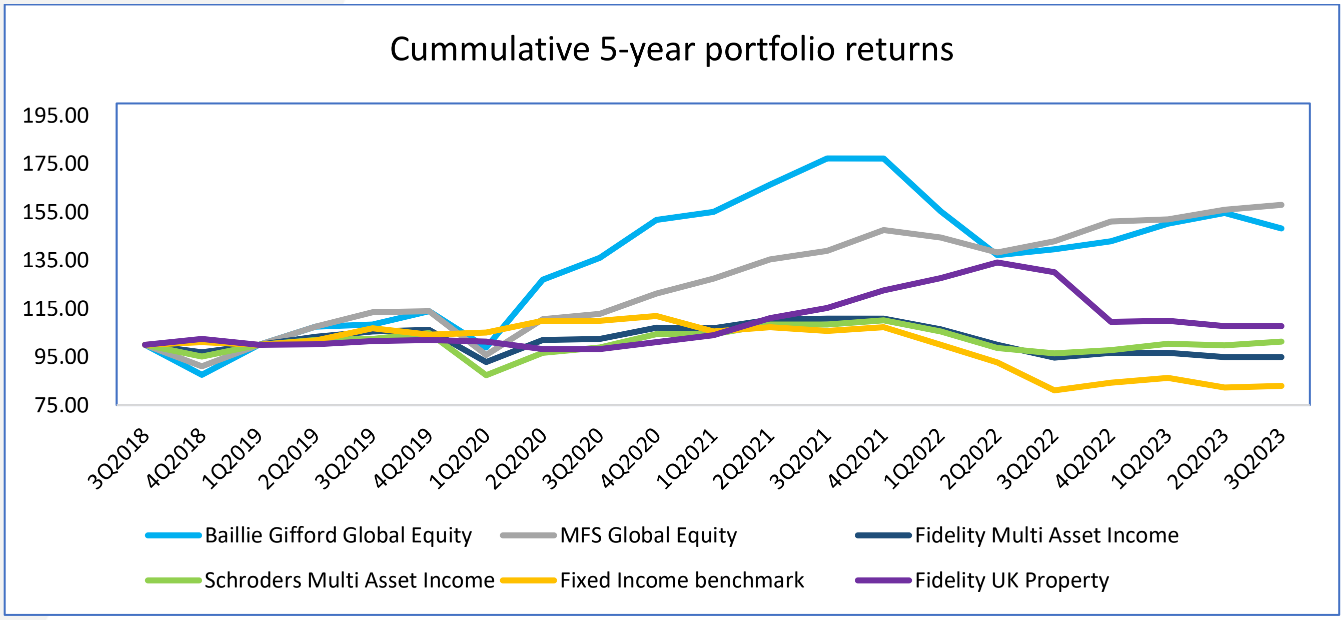
In theory, Multi-Asset Income funds should provide a less volatile return and more stable income than plain Multi-Asset funds. The Focus on income requires the fund manager to concentrate on the balance sheet of any investment and analyse the repeatability of interest or dividend payments. This should lead to a concentration on less risky investments with more secure cash flows. In addition, I personally feel that Multi-Asset funds which target a level of volatility and thereby risk, are at a disadvantage. The opportunity to add value (alpha) from asset allocation decisions is not linear over time. There are occasions when markets are volatile and stressed and asset prices will be out of balance. In these circumstances, an asset allocator can make decisions with high levels of confidence and conviction. In less stressed market conditions asset prices are less likely to be wildly out of line with their fair value and yet an asset manager working from a set risk budget still needs to make decisions and allocate risk despite having a low level of conviction that any assets are mis-priced. This is much less of an issue with Multi-Asset Income funds where the primary focus is on the generation of a repeatable income. These views are supported by the long-term performance of Fidelity's Multi-Asset Income portfolio when compared to the other Multi-Asset portfolios it manages.

**Has the allocation to Multi-Asset income Funds worked?**

The two Multi-Asset Income portfolios have delivered a yield of approximately 4% throughout the period from initial investment to the present day. Current yields are at 5-6% due to higher bond yields but for much of the time the Fund has been invested in these portfolios income has been hard to come by as Government bond yields approached 1% across much of the developed world.

Whilst the cash flow out of the Fund has not been as negative as initially predicted in the actuarial reviews it has been negative and required an element of investment income to contribute towards the payment of pensions. By receiving income from the two Multi-Asset Income portfolios and the UK Property portfolio the Fund has covered any cash flow shortfall. This has meant that the Fund was not forced to sell assets at any stage over the last 5 years, even during the market turbulence induced by the Covid outbreak. In fact, early on in the Covid outbreak, and again as inflation took off following the Russian invasion of Ukraine, a major focus of the pension officers and myself has been to stress test the cash flow models and forecasts for the Fund to ensure that, even under periods of stress, the Fund did not have to sell assets to meet pension payments.

**Chart 1 – Portfolio returns over the last 5 years**




As can be seen in the chart above, the two equity portfolios have returned cumulatively around 50% over the last 5 years whilst the Fund's bond portfolio, which is focused on UK Investment Grade Corporate Bonds, has fallen close to 20%, with UK Commercial property up 7% over the last 5 years. The two Mult-Asset Income funds are flat (Schroders) and down 5% (Fidelity).

The Fund remains committed to investing in global equities to provide long-term investment growth and this is stated in the Fund's Investment Strategy Statement (ISS) but to do this I do feel the Fund needs other assets to diversify the equity risk especially as we may be entering a period where there is a positive rather than negative correlation between equities and bonds making true diversification harder to come by..

**It is my view that by having an allocation to Multi-Asset Income the Fund is better placed to retain a higher allocation to more volatile asset classes including global equities. The Multi-Asset Income portfolios provide an element of diversification but also the security of cash flow.**

**How have Multi-Asset Income portfolios performed over the last 5 years?**

The answer is mediocre at best. The two Multi-Asset Income portfolios have produced a return roughly equivalent to a portfolio invested 80% in Bonds and 20% in Equities and yet, in reality, their actual allocation is roughly 20% Equities, 60% Bonds including high yield and 20% Alternatives. The disappointing performance is, in part, because the only assets to have added value over the last 5 years have been equity based investments. Anything with a long duration has been hit hard by rising interest rates, this includes Bonds, Property and more recently Infrastructure.

The Chart above shows Fidelity's asset allocation within their Multi-Asset Income portfolio over time. The allocations do not add up to 100% due to the use of some derivatives, often as hedges. The poor performance of the last year in particular has been driven by the increased allocation to Government Bonds through early 2022 prior to the market sell-off in late 2022. Schroders take slightly more equity risk than Fidelity in their Multi-Asset Income portfolio as they have a return target of cash +5% to Fidelity's cash +4%. This has aided Schroders performance over the last 5 years as they have held a slightly higher allocation to equities.

The Fidelity Multi-Asset Income portfolio has lagged the similar Schroders product and, to my knowledge, other similar products in the market by 5% over the last year, mainly through a higher allocation to Government Bonds through 2022 but also through an allocation to Chinese government debt which was affected negatively by the problems in the Chinese real estate market.

Because the two Multi-Asset Income portfolios target income there is only a partial overlap with the Fund's other investment managers. Schroders do use passive index products to gain exposure to equity markets on occasion but both managers also target high yielding stocks which are much less likely to be held directly by either of the Fund's two Global Equity managers. Both Schroders and Fidelity also invest into Emerging Market debt and High Yield debt which the Fund is not otherwise exposed to. The main overlap with the Fund's other managers would be in Investment Grade Bonds but neither manager has had a particularly high exposure to this asset class in the past as it has not provided enough yield.

Post the period of poor performance by Fidelity, the lead manager of this portfolio has been changed. I have met with the new manager who is experienced having run similar portfolios at JP Morgan and Jupiter. It makes sense to bring in a new pair of eyes at this stage although the new manager strikes me as more combative and will need to build a good relationship with the existing team. Fidelity have also invested in better monitoring software to look through the holdings within the portfolio to access whole portfolio risk better. I am agnostic regarding the manager change at the current time seeing it as a reaction to a short period of poor performance and a desire to show change.

I have had a number of discussions with the existing manager and the head of Multi-Asset investing at Fidelity about the level of diversification within this portfolio, this stems from my expectation that equities and bonds will be positively rather than negatively correlated going forward and that the level of that correlation will itself be more volatile than in the past. I have encouraged that manager to look for stronger diversification outside of equities and bonds rather than use long duration bonds as a diversifier from equity risk.

Going forward, it is unlikely that global equities remain the only asset class offering a positive return over time. Diversification has not worked over the last 5-10 years but perhaps this is because we have not had a conventional recession over that period.

As noted at the start of this report, it remains my advice that the Fund continues to invest in a Multi-Asset Income portfolio to meet its cash flow requirements. In addition, I remain supportive of both the manager currently used despite the recent poor performance by Fidelity. I see this period of poor performance as being due to one bad tactical allocation to Chinese Government debt and one more fundamental mistake in seeing long duration UK bonds as diversifiers and insurance against a poor equity market environment when in fact the problem was in the long duration bond market when interest rates rose sharply. The manager recognised the issues and has acted to alter the management team and processes to assist in rectifying the issue.

## London Borough of Bromley Pension Fund

## LGPS Updates

| Investment | | | |
|---|---|---|---|
| **Topic** | **Description** | **Timescale** | **LBB Status** |
| 1. 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 mean that administering authorities will have to set out their strategies and metrics for managing climate-related risks and opportunities. | We await the final regulations.<br><br>DLUHC have confirmed that implementation of climate reporting obligations will be delayed at least until next year. (Click Here)<br><br>Presuming regulations are forthcoming in time for 1st April 2024, reports covering the period 1 April 2024 - 31 March 2025 would need to be produced by December 2025.<br><br>In the meantime, the Responsible Investment Advisory Group (RIAG) will look at what advice could be given to funds wishing to do a shadow reporting year, and also what could be done to standardise the development of climate reporting approaches at the pool level. | Officers assessed several methods of complying with TCFD requirements. Officers now suggest the most cost-effective solution is to align with the other 32 London Boroughs and allow the London CIV (LCIV) to contact Bromley's Investment Managers to produce a TCFD consolidated report and sensitivity analysis on behalf of Bromley. **Officers have engaged LCIV to produce a climate analytics report pro bono. Officers will consult with Members on which scenarios are to be modelled, and for approval of the final report. Apex has been approached to cover any TCFD requirements not covered by the LCIV service.** |
| 2. Investment Policy - pooling | DLUHC issued a consultation in 2023 on a number of investment-related proposals for the LGPS. After having considered the responses, the Government has announced (see here) that the statutory guidance on investment strategy statements (ISS) will change to say that funds should **transfer all assets into their respective investment pools by 31 March 2025**, with 'comply or explain' provisions backing this expectation. The revised guidance will also require that funds formulate plans to **invest up to 5% of their assets in levelling-up projects** (actual investments may be more or less than 5%, depending on what is appropriate for the fund) whilst other guidance will expect them to report on | We await revised pooling guidance. | LBB provided a full response to the consultation, after consideration by Members at the 11 September meeting. |

| | | | |
|---|---|---|---|
| | progress against the plan. The ISS guidance will reflect the Government's 'ambition' for funds to **invest 10% in private equity**; they will be encouraged to explore suitable opportunities with the British Business Bank. | | |
| 3. The Boycotts, Divestments and Sanctions Bill | The Economic Activity of Public Bodies (Overseas Matters) Bill, also known as the Boycotts, Divestments and Sanctions Bill had its second reading in the House of Commons on 3rd July 2023. The Bill seeks to ban LGPS administering authorities from making investment decisions influenced by political and moral disapproval of foreign state conduct, except where this is required by formal Government legal sanctions, embargoes, and restrictions.<br><br>In the course of the debate, significant concerns were expressed about the Bill. These centred around its rationale, its practicability and also whether it constituted a significant over-reach of Ministerial authority. | The Bill has reached the 3rd reading stage in the House of Commons. | 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:<br>• The LGPS senior officer<br>• Workforce strategy<br>• Monthly data collection mandated<br>• Administration KPIs<br>• Enhanced training requirements<br>• Demonstrating compliance and offering resilience | • Consultation on final regulations is expected in 2024. | As and when related regulations are published by DLUHC an action plan will be produced. |

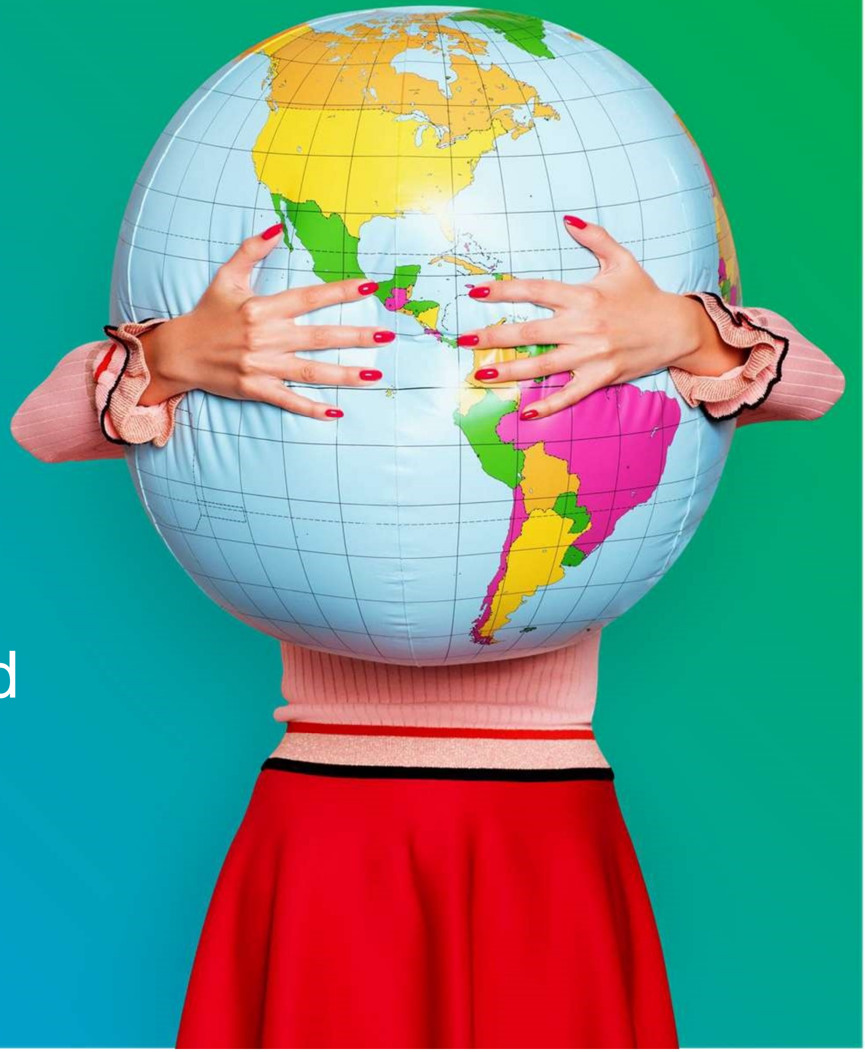
| Administration | | | | |
|---|---|---|---|---|
| | **Topic** | **Description** | **Timescale** | |
| 1. | Exit Payment Cap | The Government has stated its intention to bring back the exit cap (also known as the £95K cap). In addition, we understand that it still plans to introduce changes to LGPS and 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:<br>• the age requirement for underpin protection will be removed;<br>• the remedy period will end on 31 March 2022;<br>• the underpin calculation will be based on final pay at the underpin date,<br>• even when this is after 31 March 2022;<br>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. | In accordance with section 131 of the Public Service Pensions and Judicial Offices Act 2022, the McCloud remedy (to the extent not already in force) came into force on 1 October 2023.<br><br>The Local Government Pension Scheme (Amendment) (No. 3) Regulations 2023 also came into force on 1 October 2023. These regulations extend the statutory underpin so that all eligible members benefit from a guarantee that their benefits under the reformed LGPS, in respect of relevant service, will not be less than the amount they would have been entitled to under the legacy LGPS. | Data collection exercise:<br>Under the SAB and LGA guidance, LBB has completed the McCloud data collection exercise (most employers have responded).<br><br>Resources:<br>Resourcing impact considered and being addressed with Liberata and additional in-house resource<br><br>Action required (subject to SAB and LGA guidance):<br>- Project management<br>- 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.<br><br>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 2024 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. 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.<br><br>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. |
| 4. 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.<br><br>The Pensions Dashboards Regulations 2022 were given approval by Parliament, empowering PDP to set dashboards standards that underpin legislation. | The Department for Work and Pensions (DWP) has laid the Pensions Dashboards (Amendment) Regulations 2023. A revised staging timeline will be set out in guidance, and all schemes in scope will need to connect by 31 October 2026. The staging timeline will indicate when schemes (by size and type) are scheduled to connect.<br><br>There will be engagement between the Pensions Dashboards Programme (PDP), DWP [Department for Work and Pensions], industry, and regulators on draft guidance before it is finalised. | 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. LBB, along with all Pensions administering authorities, now awaits the update on the new connection deadline. |

Mercer

# Actuarial Valuation - Climate Change Scenario Analysis



## London Borough of Bromley Pension Fund

March 2023

welcome to brighter

# Introduction

Funds are required to undertake climate change scenario analysis as part of the funding valuations both as good practice and also for the purpose of the Section 13 report. We have worked with GAD and the other actuarial firms to develop the principles underpinning the approach Funds will be required to take for this.

The analysis aims to illustrate the different elements of risk under two alternative climate change scenarios based on the current strategic allocation. The scenarios are not meant to be predictors of what may happen and are only a small subset of a very wide range of scenarios that could arise depending on the global actions taken in relation to climate change. The actions taken (both historically and in future) by the Fund in relation to making its asset portfolio more sustainable is or will be set out in the separate Taskforce for Climate Change (TCFD) reports. This will include analysis of the asset portfolio, adopting the same (or similar) scenarios.

**Next steps**

Whilst this basic analysis has been prepared to satisfy the requirements for the 2022 actuarial valuation, it could be developed further in order to improve understanding and therefore management of climate risks for pension scheme funding. We would be happy to work with the Fund in conjunction with your investment adviser to extend this over the course of 2023. For example to consider the impact of alternative climate change scenarios over a longer time horizon to better illustrate the associated risks (noting the long-term nature of both the Fund and the impacts of climate change); and of adopting alternative investment strategies which could, for example, be used to illustrate the potential impact of increasing sustainable tilts on overall risk. Whilst asset returns will be a key part of the further analysis undertaken, incorporating potential liability impacts provides more insight into the potential financial consequences in terms of contribution outcomes, and has the benefit of maintaining consistency with the analysis undertaken for the 2022 and future actuarial valuations. We will also incorporate the impact of other factors e.g. life expectancy in 2023 as the thinking on climate change evolves.



We look forward to discussing the contents of the report with you.

Clive Lewis FIA

# Overview

We have considered climate change scenario analysis using our model which has been developed in partnership with Ortec Finance. Ortec Finance develop a broad range of scenarios and long-range projections on how the climate crisis could impact funding and investments, from a “rapid transition” that limits warming to 1.5°C to a “failed transition” with warming above 4°C. The collaboration enables us to provide you with analysis to better understand the strategic risks and opportunities presented by climate change. We have modelled the climate shock impacts over 20 years and included the two funding level projection scenarios noted above - a “rapid transition” and a “failed transition” – which is in line with the core requirements for the 2022 valuation. This is compared to the baseline (a projection using both the valuation assumptions and the best estimate – i.e. valuation assumptions with prudence removed) to show the overall prudence built into the valuation, and how much of this could potentially be eroded by climate change. We have also shown the impact on a relative basis which is the critical metric. For the actuarial valuation report we will show the relative impact as this measures climate risk but we will also comment on the level of prudence built into the assumptions. The approach taken will also be summarised in the Funding Strategy Statement.

Our scenarios apply a more nuanced approach to understand what is/is not priced in to the markets in terms of transition and physical risks. They include assumptions about what is currently priced into markets, and later price in shocks when the markets account for future impacts (both physical and transition impacts). There is also a granular insight into sector and regional impacts for equities, corporate bond and high yield allocations, with fixed income analysis considering the impact of changes in yield, spread, transitions and defaults.

It is important that we ensure any messaging is understood and recognises the potential risks of the impact of Climate Change as well as what the Fund is doing to address this via its investment strategy.

# Why is Climate scenario Analysis important?

## Where are we currently heading?

- Climate change is a systemic risk.
- The world is already experiencing ~1.2ºC of warming compared to pre-industrial times.
- The Paris Agreement (2015) aims to keep global mean surface temperatures to “well below 2ºC above preindustrial levels and to pursue efforts to limit the temperature increase to 1.5ºC”.
- Under global policies we are currently on track for ~2.7ºC of warming to the end of the century. More remains to be done to meet the ambition of the Paris Agreement.
- It is important that investors assess their portfolio’s resilience to different climate scenarios and also consider the impact of their portfolios on future climate trajectories.

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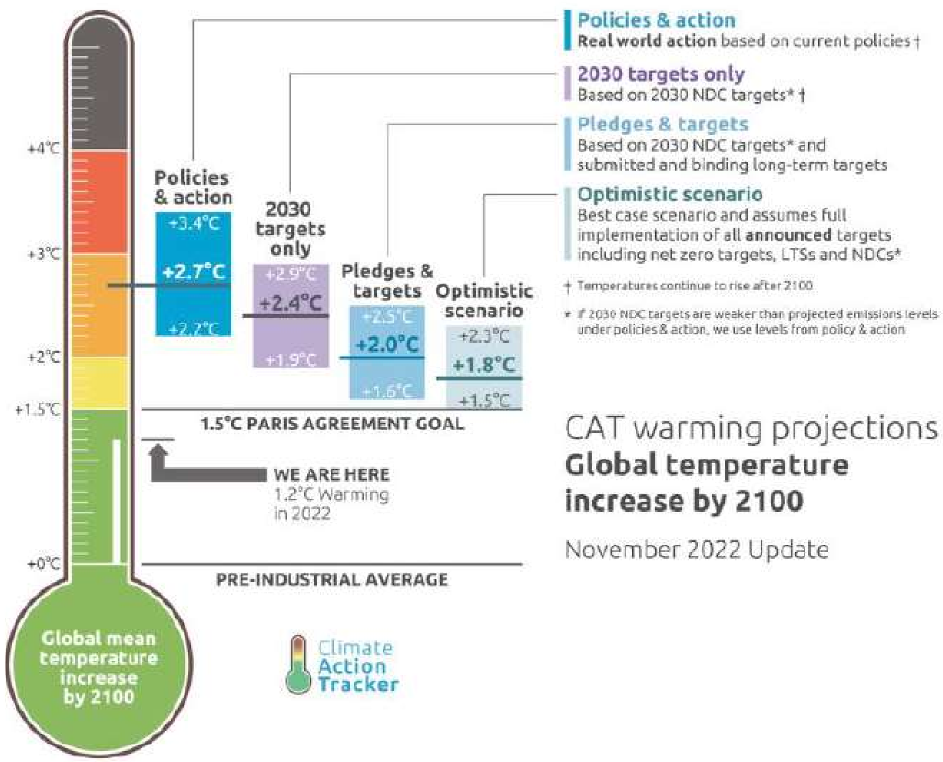


Source: https://climateactiontracker.org/

# Climate scenario analysis
## What is transition and physical risk?

### Risk Factors

| Transition |
| --- |
| Technology |
| Policy |

| Physical damages |
| --- |
| Availability of natural resources (inc biodiversity) |
| Chronic Damage (including productivity) |
| Acute Damage (catastrophes) |

Sudden asset re-pricing risk

Opportunities from the low carbon transition

Sector performance divergence – energy, transport and agriculture most impacted

Physical risks increasingly dominate over longer term

**In order to fully assess climate-related risks and opportunities, we must consider both transition and physical impacts.**

Mercer

# Mercer's Climate Scenarios

Our Mercer scenarios are constructed to explore a range of plausible futures over the projection period (up to 40 years can be considered), rather than exploring tail risks. In shorter timeframes, transition risk tends to dominate while over longer timeframes physical risk will be the key driver of climate impacts. A key strength of our scenarios is that they allow for climate impacts to be "priced-in" before they happen. This reflects likely market dynamics and means climate impacts are more likely to fit within investment timeframes.

The two scenarios considered for the purpose of the core analysis are as follows:

- **A Rapid Transition** – Average temperature increase of 1.5°C by 2100. Sudden divestments across multiple securities in 2025 to align portfolios to the Paris Agreement goals which have disruptive effects on financial markets with sudden repricing followed by stranded assets and a sentiment shock. Following this shock there is a partial recovery.

- **A Failed Transition** – Average temperature increase above 4°C by 2100. The world fails to co-ordinate a transition to a low carbon economy and global warming exceeds 4°C above pre-industrial levels by 2100. Physical climate impacts cause large reductions in economic productivity and increasing impacts from extreme weather events. These are reflected in repricing events in the late 2020s and late 2030s.

Our assumptions for modelling the **Rapid Transition** and **Failed Transition** scenarios are shown on the next page.

Mercer supports limiting warming to 1.5°C but recognises that given the current warming trajectory, based on existing policies and actions, this pathway may represent a short term shock to investment portfolios. Investors should position their portfolios for a low carbon transition while also understanding the potential impact of physical damages

# Modelled Strategy

| Modelling Asset Class | New Strategy Partially Sustainable SAA (%) |
|---|---|
| MSCI ACWI Equity | 58.0% |
| UK Investment Grade Credit | 9.3% |
| Global Real Estate | 5.0% |
| UK Sovereign Bonds | 3.8% |
| UK Real Estate | 4.0% |
| Multi Asset Credit | 20.0% |

**The table illustrates the asset allocation we have modelled (taken effective as at 31 March 2022 for simplicity). The projections are from 31 March 2022 with an initial asset value of £1,339m and an initial liability value of £1,163m*. We have made some simplifying assumptions that contributions and accrual into the Scheme offset benefits paid out of the Scheme. This should not have a material impact on the outcome.**

**Under the two baseline scenarios on slide 9 assets are projected assuming an average best estimate expected return (CPI+3.6% p.a.) and prudent valuation assumption (CPI + 1.0% p.a.) from 31 March 2022, to be consistent with the valuation position. Liabilities are projected on the basis of unwinding the valuation discount rate of CPI+1.0% p.a. only.**

*includes economic / inflation reserve for those employers who have requested it



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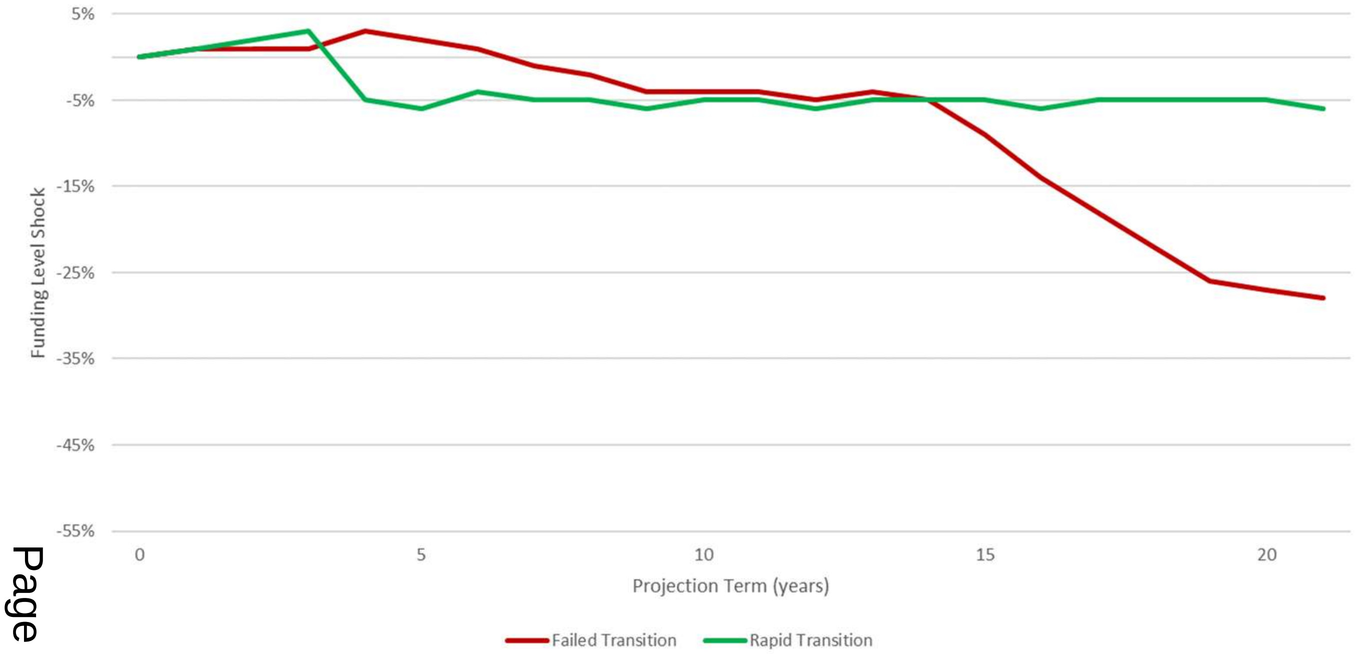
# Analysis Outcome
## Funding Level Projection – Relative impact

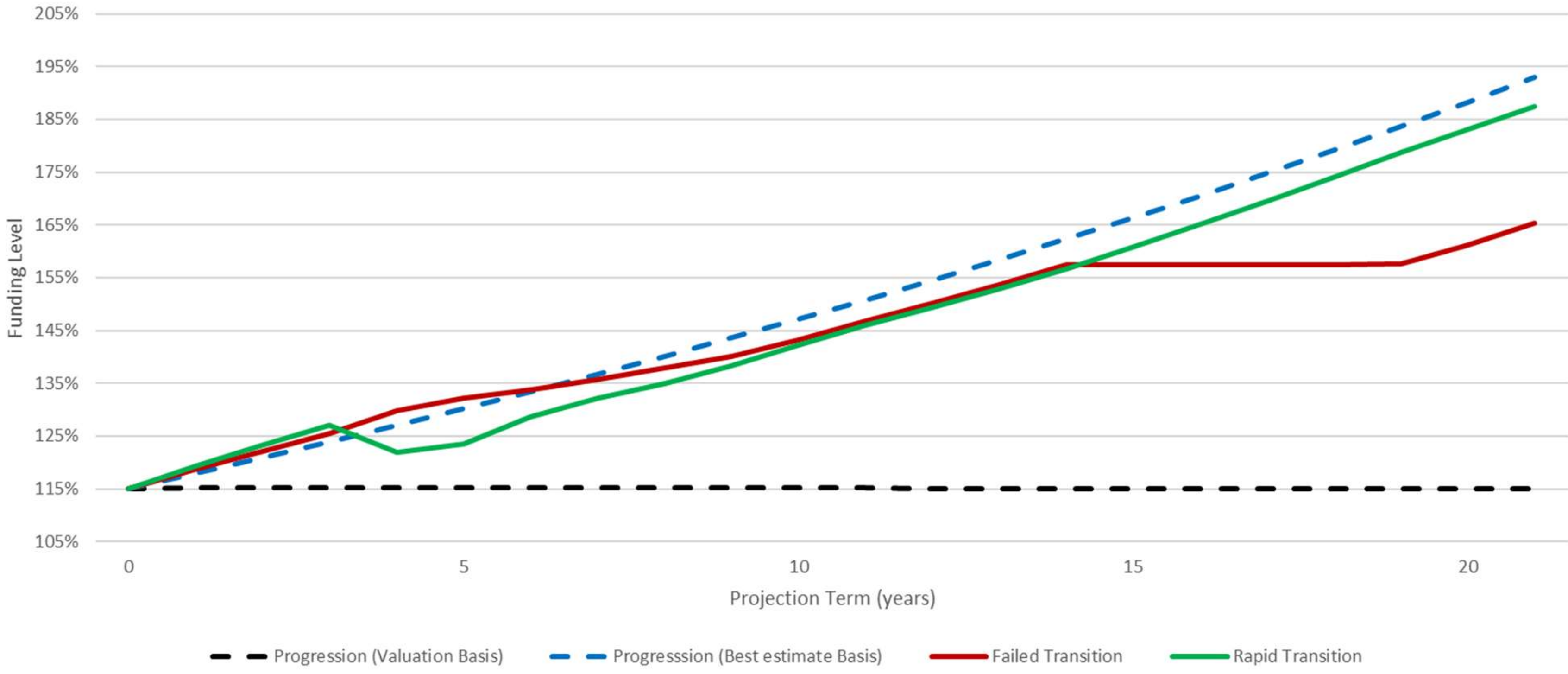



Key points at different time frames :

Over the short term, transition risk dominates. The Rapid Transition is the most impactful scenario. Under this scenario there is a shock which reduces the funding level by about 5% relative to baseline. The Failed Transition funding level is marginally higher than the baseline in the short term due to transition costs not materialising.

As longer term physical damages begin to be priced in, the Failed Transition becomes the most impactful scenario. Extending the projection period out further would provide greater insight into these impacts

# Analysis Outcome
## Funding Level Projection – Absolute impact






Overall, across a range of timescales, climate impacts have the potential to impact prudence margins from the actuarial basis (which is illustrated as the difference between the two dash lines). This would leave the funding strategy more exposed to other risks e.g. economic, market and demographic risks. Given the long-term nature of the Fund we recommend this analysis is further extended to consider the impact of alternative investment strategies and the longer time horizon.

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# Supporting Information

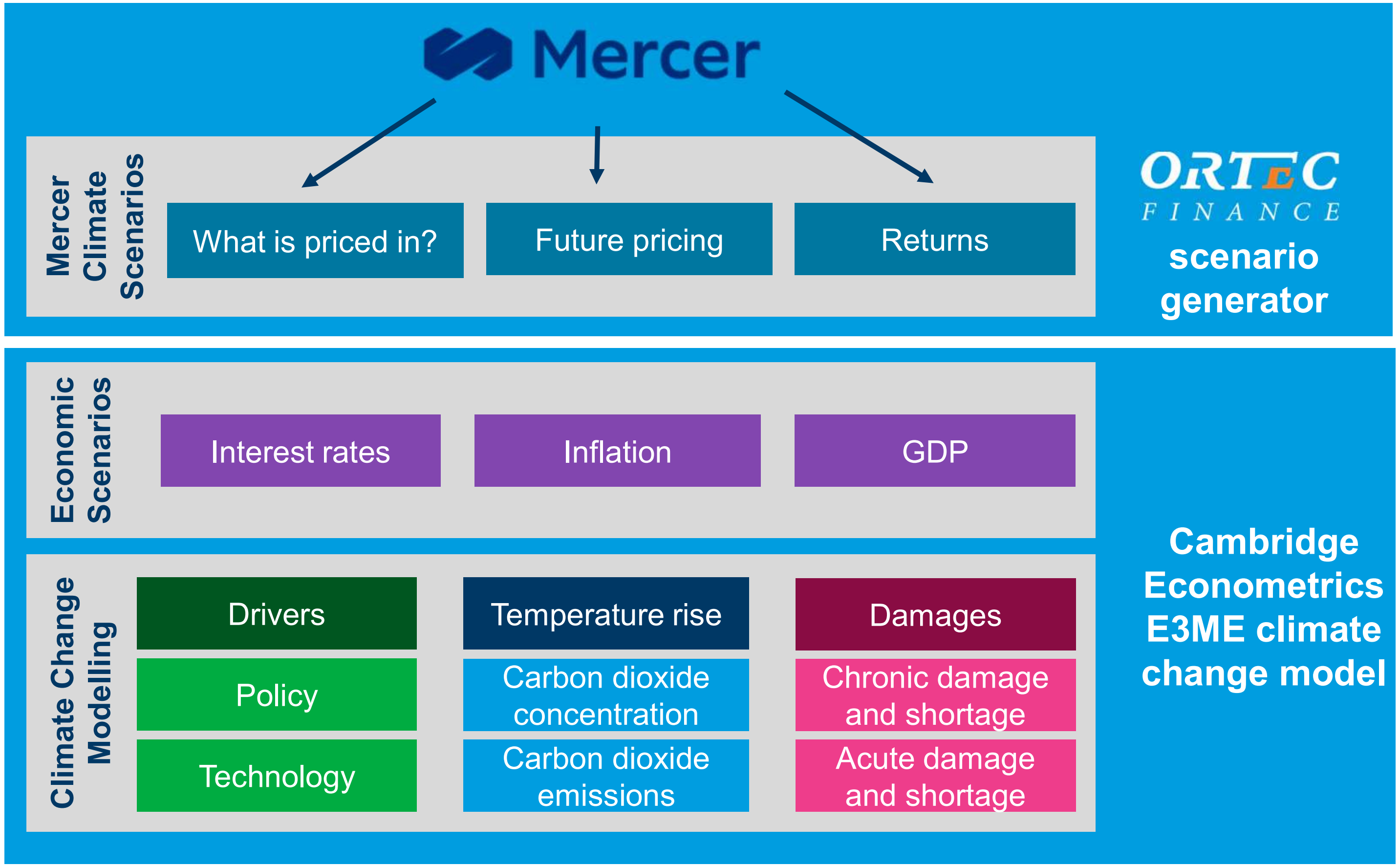
# Introduction to Climate Scenario Analysis
## Scenario Construction

**Mercer has partnered with Ortec Finance and Cambridge Econometrics to develop climate scenarios that are grounded in the latest climate and economic research and give practical insights.**

Mercer's climate scenarios are developed by building the investment modelling on top of the economic impacts of different climate change scenarios within the E3ME climate model.

Each climate scenario covers a specific level of warming driven by levels of carbon dioxide ($CO_2$) and other green house gases. These levels are determined by the policies enacted and the technological developments. The impacts of the warming are shown in the physical damages. E3ME maps this to economic impacts and Ortec's scenario generator maps the economic impacts to investment return impacts by making assumptions on what is priced in currently and how future pricing shocks will occur.

Mercer's scenarios include our own views on what is priced in and are built on Mercer's climate aware capital market assumptions.



# Modelling Assumptions – Background

| | Failed transition | Rapid transition |
|---|---|---|
| **Summary** | **The world fails to meet the Paris Agreement goals and global warming reaches 4.3°C above pre-industrial levels by 2100. Physical climate impacts cause large reductions in economic productivity and increasing impacts from extreme weather events.** | **Sudden divestments in 2025 to align portfolios to the Paris Agreement goals have disruptive effects on financial markets with sudden repricing followed by stranded assets and a sentiment shock.** |
| **Temperature change** | Average temperature increase of >4°C by 2100. | Average temperature increase stabilises at 1.5°C around 2050. |
| **Cumulative emissions** | 5,127 $GtCO_2$ (2020-2100) | 416 $GtCO_2$ (2020-2100) |
| **Key policy & assumptions** | Existing policy regimes are continued with the same level of ambition. | An ambitious policy regime is pursued to encourage greater decarbonization of the electricity sector and to reduce emissions across all sectors of the economy.<br>Higher carbon prices, larger investment in energy efficiency and faster phase out of coal-fired power generation. This is earlier and more effective under a Rapid Transition than the Orderly Transition, which allows for less investment in energy efficiency and bioenergy with carbon capture and storage. |
| **Financial climate modelling** | Physical risks are priced in two different periods: 2026-2030 (risks of first 40 years) and 2036-2040 (risks of 40-80 years). | Pricing in of transition and physical risks of the coming 40 years occurs within one year in 2025. As a result of this aggressive market correction, a confidence shock to the financial system takes place in the same year. |
| **Physical risks considered** | Physical risks are regionally differentiated, consider variation in expected temperature increase per region and increase dramatically with rising average global temperature. Physical risks are built up from:<br>• Gradual physical impacts associated with rising temperature (agricultural, labour, and industrial productivity losses)<br>• Economic impacts from climate-related extreme weather events<br>Current modelling does not capture environmental tipping points or knock-on effects (e.g., migration and conflict). | |

# Modelling Assumptions – Cumulative Climate Return Impacts for:

| | Failed Transition | | Rapid Transition | |
|---|---|---|---|---|
| | 30/06/2022 | | | |
| Asset Class | 5 Years | 20 Years | 5 Years | 20 Years |
| MSCI ACWI Equity | 2.9% | -28.9% | -11.6% | -7.8% |
| UK Investment Grade Credit | 0.3% | -2.5% | -2.3% | -2.3% |
| Global Real Estate | 0.8% | -21.7% | -4.3% | -0.6% |
| UK Sovereign Bonds | 0.3% | -0.4% | 0.2% | 0.5% |
| UK Real Estate | 0.8% | -28.9% | -6.3% | -1.3% |
| Multi Asset Credit | -0.3% | -2.1% | -3.1% | -4.7% |
| MSCI ACWI ESG Equity | 2.2% | -29.6% | -8.8% | -4.4% |

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# Actuarial advice

- We have prepared this document for the Administering Authority for the purpose of advising on the 2022 valuation
- "Technical Actuarial Standard 100: Principles for Technical Actuarial Work" issued by the Financial Reporting Council applies to this presentation and the associated work, and we confirm compliance with this standard. This presentation should be read in conjunction with our report on the actuarial valuation of the Fund as at 31 March 2019.
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