

**Workshop at MJ Hudson Offices – 2<sup>nd</sup> November 2022**

Minutes by: Dan Parsons, Senior Accountant

**Attendees:**

Cllr Keith Onslow – Chairman of Pensions Committee

Peter Turner – Director of Finance

John Arthur – MJ Hudson

Clive Lewis – Mercer

John Carnegie & David McIntyre – Baillie Gifford

Paul Harris & Eugene Philalithis – Fidelity

Elaine Alston & Benoit Anne – MFS

Gareth Dittmer & Steve Turner – Morgan Stanley Northhaven

Russell Smith & Remi Olu-Pitan – Schroders

Dan Parsons – Senior Accountant

**Introductions**

Attendees introduced themselves and Cllr Onslow opened the meeting by confirming that the focus of the meeting is investment returns. Secondly, cash flow would be discussed and levelling up also. Cllr Onslow said that as Bromley takes a long-term view, we do not tend to change our investment managers. Cllr Onslow described the various measures that were taken in the previous meetings to improve the fund cashflow.

The Director of Finance then outlined key themes from his perspective, which were whether the fund should de-risk or take more risk, the impact of inflation and passive versus active fund management. The PF was 110% fully funded at March 2019, meaning our projected liabilities are less than the projected value of assets. This means Bromley is one of the best funded in the country. The triennial valuation is currently underway, though not completed, is reasonably expected to show a healthy funding position.

Asset class / allocation is key to the triennial valuation, so he welcomed comments from the investment managers in attendance. He mentioned that comments would not be allocated to individual managers. The Director of Finance also confirmed that the fund was initially cash negative, but this was no longer the case. The benchmark for equities is 57.5% and we are currently slightly over this. The Director of Finance wanted to know what if any changes could be made with regards to infrastructure, private debt, or others. He also mentioned that Bromley has £100m of treasury

investments and views sought would assist in informing investment choices. The pension fund is actively invested.

### **Actuary perspective for the future**

Clive Lewis then briefed the room on the triennial valuation. He mentioned that LGPS pensions inflation is uncapped, compared to private pension funds which are capped at 5%. From the actuary perspective, real returns above inflation are key.

### **Future Return Expectations**

Clive described the difference between past service cost which is CPI + 1.5% (lower risk due to past good performance) and future service cost which is CPI +2%. The ER rate is 17.6%.

### **Cash flow**

The Chairman mentioned that the fund was cash positive to 2026. One attendee asked if changing equities investments from the £10m currently reinvested to income generating would be sufficient to alleviate any cash concerns which may arise at the next meeting in 3 years. The Senior Accountant confirmed it would be sufficient.

### **Views on Asset Classes**

The meeting then went into open discussion regarding the various asset classes summarised as follows:

- **Global Equities**

It was mentioned that we may be in a new interest rate regime, with supply chain issues and increasing volatility. There is a drive to resolve energy security and other societal issues. Equities will remain the strongest performer. Emerging markets already make up part of the UK performance. Active basis is the best way to select the best performing companies. Bromley has no passive investments. It was mentioned that long term market forecasts were over 8% but that the next 12 months would be difficult. It was noted that a few very strong performing companies (new winners) make large gains.

The Director of Finance asked if the attendees could provide further evidence that active management outperforms passive, as sometimes there is a reliance on overall averages rather than recognising that some active managers perform much better than others. The feedback was to view performance net of fees and identify managers who do not deviate from their stated strategies.

- **Global Real Estate**

It was mentioned that this is an extremely active investment with opportunities due to the volatility seen recently, to buy companies in distress and take advantage of interest rate volatility. All of this helps the RE portfolio.

- **Fixed Income**

Analysis of which stocks to pick is key, as default is possible, and resulting downgrading of credit rating. This is more likely in a recession environment, which most attendees think reasonably likely. It was mentioned that high yield bonds / corporate bonds in emerging markets will be very attractive.

- **Private Equity / Private Markets**

There is a premium for investing in this area if you can withstand the liquidity requirement. It was mentioned that public perception of asset stripping PE may not be suitable for Bromley, but the managers mentioned this is the large-scale PE engaging in leveraged buy outs. Medium or small PE is better as management are aligned to growth objectives without the LBO issue. It was noted that the environment that drove investment in PE in the last 10 years is now being challenged.

- **Infrastructure**

This asset class has come a long way in the last 10 years, and has inflation protection, differentiation of risk (into regulatory risk) and Bromley has sufficient liquidity. It was noted it is difficult to define what is infrastructure (communications, IT, servers etc)

### **Consideration of Asset Class Split**

The Director of Finance then asked for suggestions for changes to the asset allocation.

General comments were as follows:

- Equities gives flexibility and an option to profit from the misfortune of other pension funds which may now be forced sellers following the fall in the Liability Driven Investment portfolios.
- Current asset allocation is good if you want to benefit from a risk-taking position.
- Bromley may be underutilising its illiquidity element of its budget. It was mentioned that other funds have up to 20% invested in illiquid assets, but Bromley is at 5%, rising to 9% with further drawdowns in the International Property Fund.
- Bromley could invest in commodities, infrastructure and private credit though where to fund this from was not suggested.
- Do not increase illiquid assets due to the short-term volatility in interest and inflation arising from the energy crisis that will affect infrastructure.
- Public credit is more attractive than private.

- Stay largely in equities but go to previously avoided areas with growth opportunities.
- Diversify to global fixed income as it now has high yield opportunities as starting yields are now reasonably priced. Make fixed income type products work harder for your money.
- Equities gives flexibility, but how much do you want diversification, growth or income. Overall, as you value flexibility do not change allocation.
- Maximise equities as the world is growing, growth opportunities arise, and good managers will find them. As a long-term growth investor, equities are key. If you want more income, corporate credit is very attractive now.

The Chairman then noted that the managers may have to describe how much they are already doing to meet the social projects aspect of investing.

The Director of Finance asked for estimates of inflation in 12 months. The responses were as low as 5% and as high as 8.7%, with an average of 6.34%

The independent Investment Adviser then made several comments and the meeting closed with thanks expressed by the Director of Finance and Chairman.