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Pension Committee

2 March 2023

Gloucestershire Pension Fund update – Part 1 Quarter ending 31 December 2022

Report of the Head of Pensions

Introduction

This report provides information in relation to the following areas of Fund for the quarter ending 31 December 2022:

- Funding
- Investment
- Governance and Operations

This report fulfils the requirements under the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016.

Funding

The below information is to provide an update on the funding position at 31 December 2022.

Reported funding position	31 March 2022	31 December 2022
Assets (£m)	3,111	2,948
Past service liabilities (£m)	2,826	2,063
Surplus/(Deficit) (£m)	285	884
Funding level	110%	143%
Assumed future investment return (% p.a.)	4.2%	6.0%
Likelihood of achieving this return*	75%	75%
Fully funded target	31 March 2022	31 December 2022
Funding target	100%	100%
Future investment return required to be 100% funded (% p.a.)	3.7%	4.0%
Likelihood of achieving this return*	81%	91%

*likelihood of the Fund's portfolio achieving these returns over the next 20 years

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The funding position is being reported with the following notes:

- The assumptions underlying this funding assessment have been set based on the proposed Funding Strategy Statement, updated for market conditions as at 31 December 2022.
- Caution should be exercised when relying on the above information to inform real world decision making for the following reasons:
 - Future inflation expectations are uncertain, and the effect of Government and Bank of England policy decisions may lead to significant changes in short term inflation expectations between now and the date of any future cessation calculation.
 - The value of the liabilities as at 31 December 2022 recognise the expected 2023 Pension Increase Order of 10.1% that is likely to apply in 2023.
 - This also represents a whole of fund position however the funding positions of individual employers will vary.

Investment

- **Performance**

Over the quarter to 31 December 2022, the Fund's total market value increased by £60.4m, to £2,947.9m.

Over the quarter, total Fund assets produced a positive return of 2.1%, compared to a target of 2.0%, outperforming the strategic benchmark by 0.1%.

Performance over the 3 years to 31 December 2022 was 3.7% annualised which is 0.1% behind benchmark.

The strategic benchmark of the Fund has been recalculated with effect from this quarter to ensure it produces a benchmarking outcome more closely aligned to the agreed strategy.

The summary of investment performance is attached as appendix 1 to this report. Attached at appendix 3 is the more comprehensive performance report produced by Brunel, which contains detailed information and commentary on the individual portfolios as well as stewardship and climate metrics.

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- **Investment Activities and Strategic Asset Allocation (SAA)**

During the Quarter the following investment activity took place:

- During the quarter there has been a number of calls into the alternative asset classes of:

○ Infrastructure	-	c£14.9m
○ Private Equity	-	c£2.6m
○ Private Debt	-	c£14.8m
Total	-	c£32.3m

- £25m was redeemed from the DRF in the quarter to fund the above calls.

The current SAA is as follows:

Asset Class	Target Allocation %	Range +/- %	Allocation as at 31 December 2022 %	Variation from Target %
Equities	53.0	3.0	57.1	+4.1
Fixed Interest	17.0	2.0	17.2	+0.2
Alternatives*	30.0	2.0	25.7	-4.3

Detailed SAA analysis for each portfolio is attached as Appendix 2 to this report.

The above target allocations are now based on the SAA agreed by Committee in December 2022. Further information in respect of addressing the variations from the target allocations is contained in the Fund Update - Part II report, later on the agenda.

- **Market Commentary**

The final quarter of 2022 brought some relief to investors as equities partially recovered the year's losses and global bonds generally improved on a shift in central bank messaging and signs that inflation may have peaked. The quarter was not without volatility as central banks indicated a slowing in the pace of rate hikes but also flagged rates may peak at a, higher than previously expected, level.

Positive inflation surprises in the US bolstered sentiment, while lower energy prices in Europe, a weaker dollar, and China's reversal of COVID restrictions also provided tailwinds. Although stock markets retreated in December, healthy gains in October and November underpinned a total return for the MSCI AC World Index of 2.0% in GBP. For the full year, the index returned -7.6% in GBP. The MSCI Emerging Markets Index rose 1.9% in GBP over the quarter.

The UK stock market, as measured by the FTSE All Share (excl Investment Trusts) Index, returned 9.2% in Q4 to take the full-year return into positive territory (+1.6%). Because the

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index is heavily weighted in strong-performing global consumer staples and commodity related stocks that also benefited from a weaker sterling, the performance does not particularly reflect the UK economy's recent challenges.

European markets had a robust end to 2022 despite the continuing war in Ukraine, soft economic data, and hawkish signals from the ECB. An overall mild start to winter eased concerns about energy supplies and costs, while the reopening of China's economy and slowing pace of US rate hikes also aided sentiment.

The US equity index gained 7.5% in local terms in Q4, the only quarter of positive returns in a year when it fell -18.1%. Sentiment was buoyed by inflation slowing to 7.1%, its lowest level in a year, and by the Fed slowing the pace of rate hikes.

Japan's stock market rose a modest 0.7% in local terms in Q4 as the Japanese yen rallied versus the weakening US dollar. The Bank of Japan's move to increase the yield cap in its yield curve control policy to 0.50% from 0.25% also boosted the currency, which is a headwind for the export-oriented nature of many Japanese stocks. In the wider region, the ex Japan Index returned 7.4% in GBP terms.

UK Gilts rebounded as previously announced government spending plans were reversed and as hopes mounted for a more dovish Bank of England approach in 2023. The iBoxx Sterling Non-Gilts returned 5.7% over the quarter.

The global economy limped to the end of 2022. The purchasing managers' indices (PMI) of leading countries were soft, such that the latest readings are indicative of contracting activity as businesses feel the impact of fiscal and monetary tightening. The International Monetary Fund reduced its 2023 global GDP growth forecast to 2.7%, which would be the lowest outcome since 2001; it projects Europe, in particular, as struggling in the coming year on the effects of rate hikes, inflation and ongoing war in Ukraine. Among commodities, oil prices steadied after steep losses in Q3 on economic concerns, while precious and industrial metals attracted support in the quarter.

On cash markets the SONIA returned 0.7% in the three months.

The AREF/IPD UK All Property Fund Index returned -13.4% over the quarter and -10.0% for the full year.

- **Independent Advisors Fund report and analysis**

John Arthur has prepared a report, attached as appendix 4, in his role as independent advisor to the Fund.

The report provides further detailed analysis on the overall performance of the Fund, the underlying managers and investment mandates held by the Fund and the Long-term Capital Market Assumptions used in establishing the SAA.

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Governance & Operations

- **Consultations update**

As previously advised, on 1 September, the UK Government launched their [consultation](#) on Governance and Reporting of climate risks. The consultation closed on 24 November 2022,

A formal response was submitted by the Fund. The relevant regulations are expected to be in force by April 2023 with our first report due by December 2024 covering the 2023/24 scheme year, but at the time of preparing this report, we have not seen any further response or progress from Government on this matter.

We are still waiting for the consultations/regulations on McCloud, pooling guidance, exit payments (£95k cap), but The Department of Levelling Up, Housing and Communities (DLUHC) is consulting on changes to the LGPS Regulations 2013 to give effect to the change in the annual revaluation date from 1 April to 6 April. This consultation is seeking views on changing the Local Government Pension Scheme for England and Wales (LGPS) annual revaluation date from 1 April to 6 April. This is to mitigate against the impact of high inflation on LGPS revaluation this year and consequent tax liabilities arising as a result. These tax liabilities would arise because the timing of LGPS revaluation on 1 April is not aligned with HMRC's process for assessing the annual allowance tax charge. The proposed change would bring it into alignment. DLUHC are also seeking views on draft regulations to effect this change.

The [consultation](#) was launched on 10 February 2023 and will last for 2 weeks to 24 February 2023. A verbal update will be provided at the meeting.

- **Fund Administration**

The current reportable performance indicators, which are attached as appendix 5 to this report have continued to improve in the majority of the key deliverable areas, which reflects that the activity of year end, annual benefit statement and the majority of the triennial valuation processes has been completed.

The volume of casework continues to increase. We have had to continue to embed new Transfer Out requirements, which require more due diligence checks to be undertaken by the team before payment can be made.

The focus remains for the team to provide an equal service to all members of the Fund, which is demonstrated by the average days taken in all cases v the average day taken in cases that exceed the target, and I can advise that all payments are being made within statutory timeframes in accordance with the regulations.

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As reported to Committee at its previous meeting, Aon have been commissioned to undertake a review, as part of the governance workplan, in relation to the administration strategy.

The scope of the work will cover the following areas:

- Processes
- Performance standards
- KPIs
- Resources and structure

Current progress on this against the indicative timetable is shown below:

Funds to provide information and data required by the review	December 2022	✓
Project initiation meetings / discussions	December 2022 / January 2023	✓
Virtual/physical meetings with team officers/senior managers	December 2022 / January 2023	✓ - completed in February 2023
Aon analyse information and start drafting report on findings	February 2023	Expected March 2023
Onboarding of new Pensions Administration Manager (PAM)	March 2023	✓
Progress update provided to Pensions Committee	March 2023	Verbal
Discuss report / findings with Fund's management (including new PAM)	March/April 2023	On schedule
Aon provide final report	May 2023	On schedule
Report provided to Pensions Committee	June 2023	On schedule

The outcome is still scheduled to be brought to Committee at the June 2023 meeting.

- **Staffing update**

Andy Cunningham has commenced in the role of Pensions Administration Manager with effect from 1 March 2023.

The remaining 3 x Pension Officer posts have now successfully been recruited to and the posts will be taken up during March 2023.

Overall, we now have 50% of the administration team who are new in their posts (this

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includes existing team members successful in obtaining new roles).

We continue to manage the onboarding and upskilling of the whole team, using various resources to ensure a balance between service delivery and long term improvements such as:

1. Hymans have been retained to provide a help desk facility for senior members of the team to seek technical guidance on complex case work, thereby alleviating the continual burden on internal knowledgeable persons and creating more resilience.
2. Hymans have commenced delivery of a programme of high-level administrator training sessions to new and existing team member, via multiple streams (such as in person and online) on the key elements that go into administering the scheme.

Stage 2 of the recruitment plan will commence later in 2023. The remaining vacant posts are:

- Lead Employer Liaison Officer
- Pensions Technical Officer
- Finance Officer

- **Business Plan 2022/23**

The following is a summary, together with commentary of the amber key tasks from the work plan agreed as part of the business plan for 2022/23.

A detailed report against all items is attached as Appendix 6 to this report

Governance

Task	2021/22	2022/23			
	Q4	Q1	Q2	Q3	Q4
Annual review against The Pensions Regulators Code of Practise	✓ - on the 2022/23 business plan				x – Awaiting the single code of practise
Approval of audited Fund accounts			✓ - draft accounts provided. Audit ongoing	✓ - Draft audit opinion provided.	x – Awaiting formal audit opinion

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Core projects tracking from 2022/23 business plan

Below is a brief tracking of the core projects identified in the 2022/23 business case. Further updates are provided in Appendix 6 to this report

1) 2022 Actuarial valuation and associated tasks	On track and operating to schedule	
2) Review pensions administration system contract	On schedule – project planning in phase	
3) Pensions Dashboard (including a Data Improvement Strategy)	Commenced and on track with initial data check	
4) McCloud	Awaiting guidance	

- **Governance Review**

A detailed report on the tasks from the work plan agreed by Committee in September 2021 is attached as Appendix 7 to this report.

The following activities were scheduled to commence in the previous quarter, but have been held due to dependency/impact on other projects. All other activities are operating to schedule

Action	Reason	Timescales	Current action/comment
Develop a Fund Cyber Strategy	Expected to be included in TPR New Code. We understand that the Fund currently relies on the Council's approach to Cyber Security.	Q4 2022 – Q1 2023	Strategy will be developed in conjunction with the procurement exercise surrounding the Pensions Administration Software.
Carrying out a review of Fund's practices against TPR's New Code of Practice	As part of best practice, we would expect the Administering Authority to carry out a regular review of their practices against the New Code.	Awaiting code of practice from TPR	On hold

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- **LGPS National Knowledge Assessment results**

In accordance with the Funds approved training strategy and training plan we partook in the the 2022 National Knowledge Assessment (NKA).

16 LGPS funds and over 200 members have participated in this National Knowledge Assessment of Pension Committee ('Committee') and Pension Board ('Board') members.

The findings from this assessment, attached as appendix 8 to this report, provide a quantitative report of the current knowledge levels of the individuals responsible for running the Fund, aiding the development of more appropriately targeted and tailored training plans for both groups.

This report is also a key document in evidencing our commitment to training – a key cornerstone to the good governance of the Fund.

The assessment consisted of 48 multiple choice questions across 8 key areas

- a) Committee Role and Pension Legislation
- b) Pensions Governance
- c) Pensions Administration
- d) Pensions Accounting and Audit Standards
- e) Procurement and Relationship Management
- f) Investment Performance and Risk Management
- g) Financial Markets and Product Knowledge
- h) Actuarial Methods, Standards and Practices

Gloucestershire Pension Fund ranked 5 with a score of 58.54 from a total of 16 funds which completed the assessment. The Fund had an overall engagement score of 60.50, with 50% of Committee and 71% of Board members completing the assessment.

The performance of the Board (average overall score of 63 %) was stronger than that of the Committee (average overall score of 54 %). This may reflect the fact that the Board's Independent Chair is the Head of Pensions at the Oxfordshire Pension Fund, who also completed the assessment.

The performance for the Committee and Board diverged the most in the Pensions Accounting and Audit Standards section, when Board results were 23 % higher than the Committee.

The Committee performed most strongly in the area of Pensions Governance and Financial Markets and Product Knowledge.

The board's areas of strongest Knowledge were Pensions Governance and Procurement and Relationship Management.

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Overall, for both groups, the area with least knowledge was Pensions Accounting and Audit Standards.

Based on the results of this assessment and with individual Committee and Board results, a training plan has been developed which has been included in the Fund 2023/24 business plan.

Recommendations

1. That the Committee notes in accordance with the regulations, the Fund's position and governance activities as at the 31 December 2022 and requests such clarifications and further information from officers as may be required.
2. That the Committee notes the performance of the investments as detailed in appendix 1.

Contact Officer

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