

Agenda Item 7

**Pension Committee
22 September 2023**

Gloucestershire Pension Fund update – Part 1 Quarter ending 30 June 2023

Report of the Head of Pensions

Introduction

This report provides information in relation to the following areas of Fund for the quarter ending 30 June 2023:

- 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 table below shows the estimated funding position at 31 March 2022 and 30 June 2023. Please note that the asset value at 30 June 2023 shown in this table may differ to the actual asset value at that date because it is an estimate based on estimated cashflows.

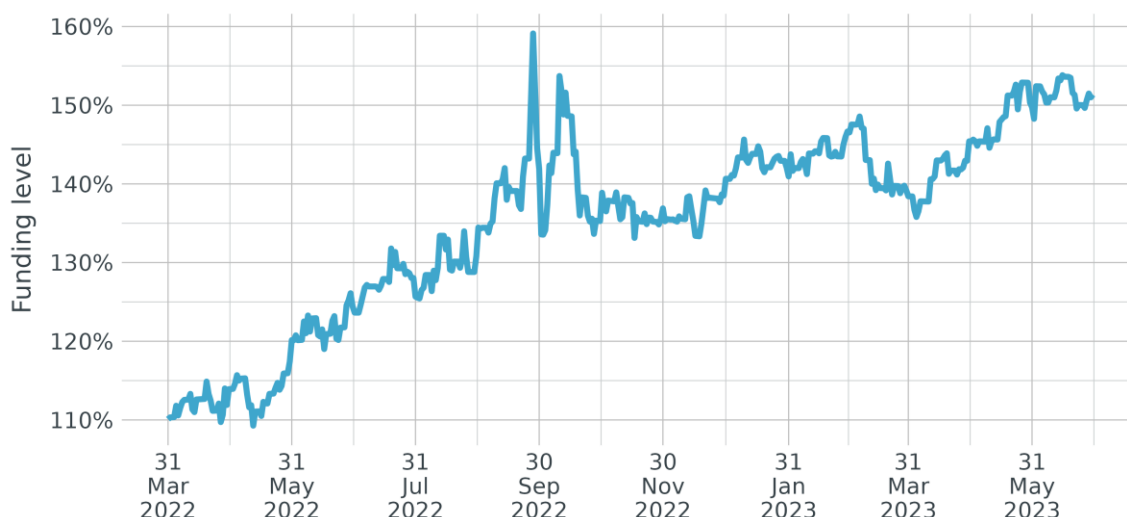
However, the estimated value is consistent with the liabilities and therefore gives a more reliable estimate of the funding position than the actual asset value at the same date.

The table also shows what assumed investment return would be required at each date for the deficit to be exactly zero, along with the likelihood of the investment strategy achieving this return. An increase in this likelihood corresponds to an improvement in the funding position.

Agenda Item 7

Monetary amounts in £bn	Ongoing basis	
	31 March 2022	30 June 2023
Assets	3.11	3.12
Liabilities		
- Active members	0.98	0.67
- Deferred pensioners	0.61	0.40
- Pensioners	1.24	1.00
Total liabilities	2.83	2.06
Surplus/(deficit)	0.29	1.06
Funding level	110%	151%
Required return assumption (% pa) for funding level to be 100%	3.7%	3.5%
Likelihood of assets achieving this return	81%	95%

The chart below shows the estimated funding level (ratio of assets to liabilities) over time between 31 March 2022 and 30 June 2023. It allows for changes in market conditions and other factors described in Appendix 1 attached.



Agenda Item 7

Investment

Performance

Over the quarter to 31 March 2023, the Fund's total market value increased by £61.370m, to £3,112.790m.

Over the quarter, total Fund assets produced a positive return of 1.5%, which was equal to the strategic benchmark.

Performance over the 3 years to 30 June 2023 was 6.0% annualised which is 0.1% ahead of benchmark.

The summary of investment performance is attached as appendix 2 to this report. The comprehensive performance report produced by Brunel has previously been circulated to Committee members and the link to the document can be found here: [Brunel Pension Partnership Investment Report - Gloucestershire County Council - 30 Jun 2023](#). This report contains detailed information and commentary on the individual portfolios as well as stewardship and climate metrics.

Responsible Investment

On 1 September 2022, the UK Government launched their [consultation](#) on Governance and Reporting of climate risks. The consultation closed on 24 November 2022. The relevant regulations were expected to be in force by April 2023 with our first report due by December 2024 covering the 2023/24 scheme year. At this time regulations have not been laid, therefore we expect a delay in the regulatory reporting requirements, however, based on the current activities of the Committee we will look to proceed to incorporate improved reporting in this area as part of the Responsible Investment policy currently being drafted.

The output of the workshop day held on 15 November were reported back to Committee in March 2023. We have now received the analysis to establish an emissions baseline as at 31 December 2019, and this also captures of progress against this baseline to 31 December 2022. This analysis will enable potential targets/measures to be set as part of the Funds responsible Investment Policy on the pathway to net zero.

The outcomes from the workshop on TCFD, TNFD and levelling up were also captured and assisted in the further defining of the investment and RI beliefs of the Committee, which will feed into an RI policy. A further ½ day workshop is being planned in October/November 2023 to receive the analysis and further develop the Responsible Investment Policy, with the anticipation that the Policy including targets/measures will be brought back to Committee at its December 2023 meeting.

Agenda Item 7

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 private markets (exc property) asset classes of:
 - Infrastructure - c£1.8m
 - Private Equity - c£6.5m
 - Private Debt - c£9.1m
 - Total - c£17.4m**

The current SAA is as follows:

Asset Class	Target Allocation %	Range +/- %	Allocation as at 31 March 2023 %	Variation from Target %
Equities	53.0	3.0	54.4	+1.4
Fixed Interest	17.0	2.0	17.4	+0.4
Alternatives*	30.0	2.0	28.2	-1.8

Detailed SAA analysis for each portfolio is attached as appendix 3 to this report.

**includes the monies being held in the DRF awaiting drawdown into the private markets portfolios*

Fund Equity Analysis

In order to provide members with more in depth analysis of the fund holdings within the specific portfolios, we provide an analysis of the Equity holdings at whole Fund level held as at 30 June 2023. Analysis of equity exposure by the top 20 companies, by sector and by countries are provided.

To improve transparency and greater awareness of the investments held by the Fund, this analysis is published on the Pension Fund website and a link to this analysis can be found here: [equity-holding-analysis-30-june-23.pdf \(gloucestershire.gov.uk\)](https://www.gloucestershire.gov.uk/equity-holding-analysis-30-june-23.pdf)

Agenda Item 7

Macro Market Commentary

The second quarter of 2023 began with an air of caution as investors continued to digest the events within the banking sector in March. However, sentiment soon improved as contagion fears waned – notwithstanding the closure of a third US bank in May – and risk assets rallied through much of the quarter. Overall, the outcome was positive for equity markets even as uncertainty persisted around inflation and the intentions of central banks. Although inflation continued to move lower, levels remained well above central bank targets. And with low unemployment keeping upward pressure on wages, central banks stayed on the monetary tightening path. The Fed announced one rate hike of 25bps in the quarter, while the Bank of England and European Central Bank continued with hikes at each meeting. The Bank of Japan remained resolute in keeping rates unchanged.

The MSCI AC World Index returned +3.4% in GBP in Q2. By region, Japan was a strong performer, hitting a 33-year high as overseas investors took advantage of a cheap yen to gain exposure to improving economic and business fundamentals. US equities maintained the good start to 2023, led by a small cohort of large tech stocks. European and Asian equity performance was more mixed, while emerging markets lagged developed peers for a second quarter – the MSCI EM Index returned -1.7% in GBP over the three months to June 2023.

The UK stock market, as measured by the FTSE All Share ex Investment Trusts Index, was among the poorer performers in posting a negative return of -0.4%. The drag from underperforming energy and materials sectors weighed on performance, as did the strength of the British pound which hit those companies' revenues. The bigger-than-expected rate hike in June and the prospect of a higher policy rate peak amid high inflation also dampened sentiment.

European markets posted positive returns in Q2, even as the ECB continued to raise interest rates. Markets were typically led higher by technology and financials with the energy sector the main laggard in the period.

The US Equity Index gained 8.7% in local terms for a year-to-date return of 16.9%, as investors put banking concerns aside, the Fed paused interest rate hikes, inflation eased, and a debt ceiling deal was achieved.

Japan's stock market recorded a very strong local currency return of 18.5%, touching its highest level in over three decades in the process. In the wider region, the MSCI Pacific ex-Japan Index recorded a negative return of -4.5% in GBP.

With the Bank of England following up a 25bps increase with a bigger-than-expected 50bps hike in June, UK Gilt yields rose across the curve; the 10-year yield rose from 3.67% to 4.39%. The iBoxx Sterling Non-Gilts returned -3.4% over the quarter.

Global government bonds recorded mixed returns in Q2. Although inflation trended lower in most countries, it typically remained above central bank targets – as a result, major banks continued to increase policy rates.

Agenda Item 7

On cash markets the SONIA returned 1.1% in the three months.

The AREF/IPD UK All Property Fund Index returned +0.3% for the quarter and -17.1% over the last 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.

Governance & Operations

Consultations update

On the 30 May, the Department of Levelling Up, Housing and Communities (DLUHC) issued a consultation on [‘McCloud’ remedy in the LGPS – supplementary issues and scheme regulations - GOV.UK \(www.gov.uk\)](https://www.gov.uk/government/consultations/mccloud-remedy-in-the-lgps-supplementary-issues-and-scheme-regulations). The consultation closed on 30 June. On Friday 8 September a response was issued by DLUHC to this consultation which advised regulations would be laid by 30 September. We will need to await further guidance and information to be able to apply the regulations once laid. Further clarifications and timeframes will be published shortly.

On the 11 July, the Department for Levelling-Up, Housing and Communities launched a consultation entitled: Next Steps on Investment. This related to the awaited consultation of pooling guidance. This particular consultation is covered under a separate agenda item at this meeting.

We are still waiting for the consultations/regulations on Good Governance, exit payments (£95k cap) and TCFD reporting.

Fund Administration

Key Performance Indicators

The key performance indicators (KPI's), which are attached as appendix 5 to this report are now based on the revised targets as agreed by Committee in June 2023. In addition the KPIs will now be developed on a rolling 12 month basis.

We have included a trend analysis against the new KPIs as if they had been applied since April 2020. This analysis also now tracks the case volumes and this reflects a marked increase in case volumes over the same period.

Agenda Item 7

Business Plan 2023/24

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 2023/24.

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

Governance

Task	2022/23	2023/24			
	Q4	Q1	Q2	Q3	Q4
Annual review against The Pensions Regulators Code of Practise	Moved onto the 2023/24 business plan				

Core projects tracking from 2023/24 business plan

Below is a brief tracking of the core projects identified in the 2023/24 business case.

1) Responsible Investment Policy and TCFD reporting	The Responsible investment policy aspect of the project is now scheduled for completion in December 2023, one quarter later than originally anticipated. The TCFD reporting aspect is still operating to target.		
2) Review pensions administration system contract	On schedule		
3) Pensions Dashboard (including a Data Improvement Strategy)	Commenced and on track with initial data check		
4) McCloud	Expected legislation effective from 1 October 2023		

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, but have been held. All other activities are operating to schedule. The development of a Fund Cyber Strategy has been rescheduled to coincide with the Core Project 1 of the business plan 2023/24.

Agenda Item 7

Action	Reason	Timescales	Current action/comment
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

Pension Fund Audit 2022/23 - Update

At its meeting in June 2023, Committee received and noted the Audit Plan, in relation to the audit to be undertaken by Grant Thornton (GT) on the Fund for 2022/23. This was followed by the draft Statement of Accounts in relation to the Fund which were provided to Committee at its September 2022 meeting.

I am now pleased to attach, as appendix 8, the draft Audit Findings Report (AFR) received from Grant Thornton, in respect of the audit on the Fund for 2022/23.

Headlines

Grant Thorntons audit work was completed remotely during July - September. Grant Thornton have not identified any adjustments to the financial statements that have resulted in an adjustment to the Pension Fund's reported financial position. Audit adjustments are detailed in Appendix D of the AFR. Grant Thornton have also raised recommendations for management as a result of their audit work in Appendix B of the AFR. Grant Thorntons follow up of recommendations from the prior year's audit are detailed in Appendix C of the AFR.

Conclusion

Grant Thorntons have substantially completed the audit of the Funds financial statements and subject to outstanding queries being resolved, they anticipate issuing an unqualified audit opinion. The outstanding items include:

- finalisation of GTs outstanding testing of journal entries, level 3 investments, cash, contributions, benefits, and purchases, sales, and management expenses;
- completion of final quality review by the engagement manager and key audit partner and any points arising from this;
- receipt of management representation letter;
- receipt and review of the final Annual report; and
- review of the final set of financial statements.

Agenda Item 7

At its meeting in June 2023, Committee requested an explanation of the differences between internal and external audit. The following table has been provided by the Institute of internal auditors. While sharing some characteristics, internal and external audit have very different objectives. These are explained in the table below:

	External audit	Internal audit
Reports to	shareholders or members who are outside the organisations governance structure.	The board and senior management who are within the organisations governance structure.
Objectives	Add credibility and reliability to financial reports from the organisation to its stakeholders by giving opinion on the report	Evaluate and improve the effectiveness of governance, risk management and control processes. This provides members of the boards and senior management with assurance that helps them fulfil their duties to the organisation and its stakeholders.
Coverage	Financial reports, financial reporting risks.	All categories of risk, their management, including reporting on them.
Responsibility for improvement	None, however there is a duty to report problems.	Improvement is fundamental to the purpose of internal auditing. But it is done by advising, coaching and facilitating in order to not undermine the responsibility of management.

Recommendations

1. That the Committee notes in accordance with the regulations, the Fund's position and governance activities as at the 30 June 2023 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 report and associated appendices.
3. That Committee acknowledge the Audit Findings Report provided by Grant Thornton for year to 31 March 2023.

Contact Officer

Matthew Trebilcock – Head of Pensions (01452 328920)