

# **Pension Fund Committee**

## **Thursday, 10 September 2020**

### **Pension Fund Administrator's Report**

#### **For Decision**

**Local Councillor(s):** All

**Executive Director:** A Dunn, Executive Director, Corporate Development

**Report Author:** David Wilkes  
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**Report Status:** Public

#### **Recommendation:**

That the Committee:

- i) Review and comment upon the activity and overall performance of the pension fund.
- ii) Note the progress in implementing the strategic asset allocation.

#### **Reason for Recommendation:**

To ensure that the pension fund has the appropriate management arrangements in place and are being monitored, and to keep the asset allocation in line with the strategic target.

#### **1. Executive Summary**

The purpose of this report is to update the Committee on the pension fund's funding position, and the valuation and overall performance of the pension fund's investments as at 30 June 2020. The report provides a summary of the performance of all external investment managers and addresses other topical issues for the pension fund that do not require a separate report.

The estimated value of the pension fund's assets at 30 June 2020 was £2,997M compared to £2,696M at the start of the financial year. This was driven by rises

across all listed markets after the falls in March 2020 in reaction to the impact of COVID 19. These gains were offset by falls in private markets where assets are typically valued on a 'lagged' basis.

This estimated funding position at 30 June 2020 is 85% i.e. assets were estimated to be 85% of the value needed pay for the expected benefits accrued to that date. This compares to 92% calculated by the pension fund's actuary following their full assessment as at 31 March 2019 for the most recent triennial valuation.

The total return from the pension fund's investments over the financial year to 30 June 2020 was 11.1%, compared to the combined benchmark return of 10.6%. Over the last 12 months the pension fund's investments have returned -2.8%, below the Fund's combined benchmark return of -1.1% the actuarial discount rate of 5.0%.

As at 30 June 2020, approximately 34% of the pension fund's liabilities were hedged against inflation sensitivity through the Liability Driven Investment (LDI) mandate with Insight Investment.

Mark Mansley resigned as Brunel's Chief Investment Officer in May 2020 and has left the company. Interviews for a replacement have taken place and an appointment is expected to be announced shortly.

James Russell-Stracey has been appointed to the Brunel company board as Chief Stakeholder Officer and is leading a review of the partnership governance arrangements.

The draft pension fund accounts for 2019-20 have been completed and are now subject to review by the administering authority's external auditors.

## **2. Financial Implications**

The Local Government Pension Scheme (LGPS) is a national pension scheme administered locally. Dorset Council is the administering authority for the LGPS in Dorset which provides pensions and other benefits for employees of the Council, other councils and a range of other organisations within the county.

The LGPS is a 'defined benefit' scheme which means that benefits for scheme members are calculated based on factors such as age, length of membership and salary. Member benefits are not calculated on the basis of investment performance as they would be in a 'defined contribution' scheme.

Administering authorities are required to maintain a pension fund for the payment of benefits to scheme members funded by contributions from scheme members and their employers, and from returns on contributions invested prior to benefits becoming payable.

Contribution levels for scheme members are set nationally, and contribution levels for scheme employers are set locally by actuaries engaged by administering authorities.

As scheme member rates cannot be changed locally and benefits are defined, the risk of investment underperformance is effectively borne by scheme employers.

### **3. Climate implications**

The pension fund's Investment Strategy Statement requires all external investment managers to consider and manage all financially material risks arising from environmental issues, including those associated with climate change.

### **4. Other Implications**

No other implications arising from this report have been identified.

### **5. Risk Assessment**

The risks associated with the pension fund's investments are assessed in detail and considered as part of the strategic allocation. In addition, risk analysis is provided alongside the quarterly performance monitoring when assessing and reviewing fund manager performance.

### **6. Equalities Impact Assessment**

There are no equalities implications arising from this report.

### **7. Appendices**

- Appendix 1: Brunel Performance Report Q2 2020
- Appendix 2: Corporate Bonds Report (RLAM) Q2 2020
- Appendix 3: Multi Asset Credit (CQS) Q2 2020
- Appendix 4: Property Report (CBRE) Q2 2020
- Appendix 5: Liability Driven Investment (Insight) Q2 2020
- Appendix 6: Pension Fund Draft Accounts 2019-20.

### **8. Background Papers**

- Investment Strategy Statement (March 2018)
- Funding Strategy Statement (March 2020)

## 9. Asset Valuation Summary

9.1 The table below shows the pension fund's asset valuation by asset class at the beginning of the financial year and as at 30 June 2020, together with the target allocation as agreed at the meeting of the Committee on 13 September 2017.

<b>Asset Class</b>	<b>31-Mar-20</b>		<b>30-Jun-20</b>		<b>Target Allocation</b>	
	<b>£M</b>	<b>%</b>	<b>£M</b>	<b>%</b>	<b>£M</b>	<b>%</b>
UK Equities	491.0	18.2%	545.0	18.2%	599.4	20.0%
Overseas Equities	682.8	25.3%	811.5	27.1%	659.3	22.0%
Emerging Markets Equities	83.8	3.1%	99.5	3.3%	89.9	3.0%
<b>Total Listed Equities</b>	<b>1,257.6</b>	<b>46.6%</b>	<b>1,456.0</b>	<b>48.6%</b>	<b>1,348.6</b>	<b>45.0%</b>
Corporate Bonds	220.6	8.2%	237.8	7.9%	179.8	6.0%
Multi Asset Credit	120.4	4.5%	135.4	4.5%	149.8	5.0%
Diversified Growth	152.8	5.7%	171.5	5.7%	239.8	8.0%
Infrastructure	195.3	7.2%	219.4	7.3%	149.8	5.0%
Private Equity	98.1	3.6%	91.1	3.0%	149.8	5.0%
Property	301.0	11.2%	297.0	9.9%	359.6	12.0%
Cash	53.4	2.0%	31.0	1.0%	-	0.0%
F/X Hedging	-9.7	-0.4%	-3.0	-0.1%	-	0.0%
<b>Total Return Seeking Assets</b>	<b>2,389.5</b>	<b>88.6%</b>	<b>2,636.2</b>	<b>88.0%</b>	<b>2,577.3</b>	<b>86.0%</b>
Liability Matching Assets	306.8	11.4%	360.7	12.0%	419.6	14.0%
<b>Total Asset Valuation</b>	<b>2,696.3</b>	<b>100.0%</b>	<b>2,996.9</b>	<b>100.0%</b>	<b>2,996.9</b>	<b>100.0%</b>

## 10. Funding Update

10.1 The pension fund's actuary, Barnett Waddingham, undertakes a full assessment of the funding position every three years. This was last completed as at 31 March 2019 when the pension fund had a funding level of 92% i.e. assets were estimated to be 92% of the value that they would have needed to be to pay for the expected benefits accrued to that date, based on the assumptions used.

10.2 Barnett Waddingham also carry out an indicative update on the funding position at the end of each quarter. This is intended to give a better understanding of movements in the pension fund's overall funding position between triennial valuations. As at 30 June 2020 the estimated funding position was approximately 85%.

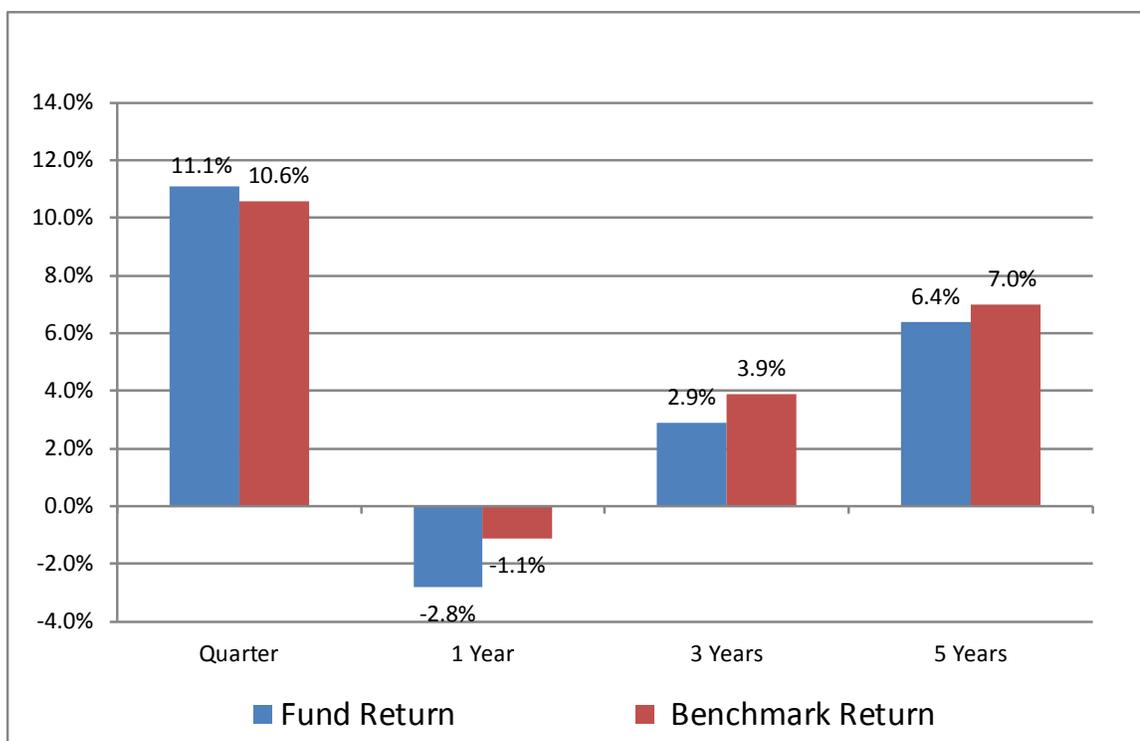
## 11. Implementation of changes to Strategic Asset Allocation

11.1 At its meeting on 13 September 2017, the Committee agreed a number of changes to the pension fund's strategic asset allocation. The following paragraphs summarise progress in implementing these changes.

- 11.2 The new 5% allocation to Multi Asset Credit manager CQS was achieved in full with an investment of £135M on 1 December 2017. It was funded from a partial disinvestment from the corporate bonds mandate with RLAM (£120M) and cash balances (£15M). This leaves the current allocation to Corporate Bonds as 7.9% against the target of 6%.
- 11.3 The increased allocation to Diversified Growth Funds (DGF) was met in part by investing a further £50M in the Baring Dynamic Asset Allocation Fund in February 2018 funded by partial disinvestment from the then internally managed UK equities portfolio. This leaves the current allocation to DGF as 5.7% against the revised target of 8%.
- 11.4 The total allocation to Listed Equities has reduced from 53% when the strategic allocation was agreed to approximately 49% as at 30 June 2020, compared to the target of 45%.
- 11.5 The increased allocations to private markets will be achieved if, and when, suitable opportunities arise with existing managers or through allocation to appropriate Brunel portfolios. A commitment of 2% has been made to the Brunel Private Equity portfolio and a further 2.0% commitment to the Brunel Secured Income portfolio. Drawdowns against commitments will be funded from cash balances and/or further disinvestment from equities and corporate bonds.
- 11.6 For all other asset classes, where the current allocation is different to the new target, it is expected that the target will be achieved through allocation to the appropriate Brunel portfolio as and when these become available.
- 11.7 Now that the results of the triennial valuation are known, there has been a review of the pension fund's strategic asset allocation, assisted by investment consultants, Mercer. The recommendations of this review are a separate item for discussion on the agenda of this meeting.

## **12. Investment Performance Summary**

- 12.1 The overall performance of the pension fund's investments to 30 June 2020 is summarised below (returns for three and five years are annualised figures).



12.2 The Brunel Pension Partnership’s performance report for the quarter ending 30 June 2020 is attached as Appendix 1. This report includes market summaries from Brunel’s investment officers and an overall performance summary for the Dorset County Pension Fund, together with more detailed information in relation to Dorset’s assets under Brunel’s management.

### 13. Performance by Asset Class and Investment Manager

#### UK Equities

13.1 In July 2018, the internally managed UK equity portfolio transferred to the Brunel UK Passive Equities portfolio managed by Legal & General Investment Management (LGIM). In November 2018, assets under the management of AXA Framlington transferred to the Brunel UK Equities Active portfolio. The performance of the pension fund’s external managers is summarised in the tables below.

#### **Brunel/LGIM Passive - £335.8m assets under management (AUM)**

	Performance	Benchmark	Relative
Quarter	10.2%	10.2%	0.0%
12 months	-13.0%	-13.0%	0.0%
Since inception p.a.	-6.9%	-6.9%	0.0%

**Brunel UK Active - £145.8m AUM**

	Performance	Benchmark	Relative
Quarter	11.7%	10.2%	1.5%
12 months	-13.3%	-13.0%	-0.3%
Since inception p.a.	-3.3%	-3.0%	-0.3%

**Schroders - £50.7m AUM**

	Performance	Benchmark	Relative
Quarter	21.1%	15.6%	5.5%
12 months	-6.9%	-13.4%	6.5%
3 years p.a.	-0.3%	-5.6%	5.3%
5 years p.a.	6.6%	0.8%	5.8%
Since inception p.a.	8.8%	4.7%	4.1%

**Global Developed Markets Equities**

- 13.2 In July 2018, the holdings under the management of Allianz transferred to the Brunel Smart Beta portfolio managed by LGIM. The performance of the pension fund's external global equities managers is summarised in the tables below.
- 13.3 In November 2019, the pension fund invested £125M in the Brunel High Alpha Developed Markets Equities. This was funded by partial disinvestment from assets under the management of the pension fund's two global equities' managers, Investec (£60M) and Wellington (£65M).
- 13.4 In January 2020, the mandate with Investec was terminated, with assets transferred to Brunel's passive global equities portfolio under the management of LGIM.

**Wellington - £210.0m AUM**

	Performance	Benchmark	Relative
Quarter	21.1%	19.8%	1.3%
12 months	8.5%	5.9%	2.6%
3 years p.a.	10.1%	8.5%	1.6%
Since inception p.a.	14.2%	12.7%	1.5%

**Brunel/LGIM Smart Beta - £140.3m AUM**

	Performance	Benchmark	Relative
Quarter	15.4%	15.5%	-0.1%
12 months	-2.4%	-2.1%	-0.3%
Since inception p.a.	3.2%	3.5%	-0.3%

**Brunel/LGIM Smart Beta (Hedged) - £137.2m AUM**

	Performance	Benchmark	Relative
Quarter	14.1%	14.1%	0.0%
12 months	-5.6%	-5.5%	-0.1%
Since inception p.a.	-0.5%	-0.1%	-0.4%

**Brunel Emerging Markets Equities - £99.5m AUM**

- 13.5 In November 2019, the pension fund's investment in the JP Morgan Emerging Markets Diversified Equity Fund transferred to the Brunel Emerging Markets Equity portfolio for a value £101.4M. The performance of the Brunel Emerging Markets Equity portfolio is summarised below.

	Performance	Benchmark	Relative
Quarter	18.8%	18.8%	0.0%
Since inception	-1.9%	0.6%	-2.5%

**Corporate Bonds - £237.8m AUM**

- 13.6 The performance of the pension fund's external Corporate Bonds manager, RLAM, is detailed in Appendix 2, and summarised below.

	Performance	Benchmark	Relative
Quarter	7.8%	9.1%	-1.3%
12 months	7.9%	8.6%	-0.7%
3 years p.a.	6.1%	5.5%	0.6%
5 years p.a.	7.3%	6.9%	0.4%
Since inception p.a.	8.7%	8.6%	0.1%

- 13.7 The manager underperformed their benchmark over 3 months and 12 months but outperformed over the longer periods of 3 and 5 years and since inception.

**Multi Asset Credit (MAC) - £135.3m AUM**

- 13.8 The performance of the Fund's external MAC manager, CQS, is detailed in Appendix 3 and summarised below.

	Performance	Benchmark	Relative
Quarter	12.4%	1.0%	11.4%
12 months	-4.6%	4.7%	-9.3%
Since inception p.a.	0.1%	4.7%	-4.6%

- 13.9 The target for the CQS fund is cash (1 month LIBOR) plus 4% over the longer term, and this is used as the benchmark for the investment.

**Property (CBRE) - £293.9m AUM**

- 13.10 The performance of the Fund's external property manager, CBRE, is detailed in Appendix 4, and summarised below.

	Performance	Benchmark	Relative
Quarter	-0.4%	-1.8%	1.4%
12 months	-1.5%	-2.7%	1.2%
3 years p.a.	3.7%	3.2%	0.5%
5 years p.a.	5.6%	4.8%	0.8%
Since inception p.a.	7.3%	7.3%	0.0%

- 13.11 In addition to assets under the management of CBRE, the pension fund also has some holdings in secured long income property funds under the management of Brunel.

**Diversified Growth Funds (DGF) - £171.5m AUM**

- 13.12 Diversified Growth Funds give fund managers total discretion over how and where they invest which means that the portfolio holds a wide range of investments against a diverse range of asset classes. The objective of the Barings fund is to deliver 'equity like' returns (over the long term) but with about 70% of the equity risk. The manager seeks to achieve out performance against a cash benchmark by focusing on asset allocation decisions.

- 13.13 The performance for Barings is summarised below.

	Performance	Benchmark	Relative
Quarter	12.3%	1.1%	11.2%
12 months	-5.0%	4.8%	-9.8%
3 years p.a.	0.1%	4.8%	-4.7%
5 years p.a.	1.8%	4.7%	-2.9%
Since inception p.a.	3.3%	4.6%	-1.3%

13.14 The target for the Barings fund is cash (3 month LIBOR) plus 4% over the longer term and this is used as the benchmark for the investment.

### **Private Equity**

13.15 Private Equity is an asset class that takes several years for commitments to be fully invested. The table below summarises the commitment the pension fund has made in total to each manager, the drawdowns that have taken place to date and the percentage of the total drawdown against commitments. It also shows the distributions that have been returned to the pension fund, the valuation as at 30 June 20 and the total gains or losses on investments.

#### **Private Equity Commitments, Drawdowns and Valuations**

<b><u>Manager</u></b>	<b><u>Commitment</u></b>		<b><u>Drawdown</u></b>		<b><u>Distribution</u></b>	<b><u>Valuation</u></b>		<b><u>Gain</u></b>
	<b><u>£m</u></b>	<b><u>£m</u></b>	<b><u>%</u></b>		<b><u>£m</u></b>	<b><u>£m</u></b>	<b><u>£m</u></b>	
HarbourVest	113.2	81.8	72%		79.9	52.5	50.6	
Aberdeen Standard	80.8	61.8	76%		65.9	28.9	33.0	
Brunel	60.0	9.3	16%		0.0	9.7	0.4	
<b>Total</b>	<b>254.0</b>	<b>152.8</b>	<b>60%</b>		<b>145.8</b>	<b>91.1</b>	<b>84.1</b>	

13.16 In order to meet the target allocation, there is a requirement to keep committing to Private Equity funds. Officers are in regular discussions with HarbourVest, Aberdeen Standard and the Brunel private markets team to identify further opportunities for investment.

13.17 Private Equity is a long-term investment and as such the performance should be considered over the longer term. Additionally, as the benchmark used for these investments is the FTSE All Share index and the investments are held in US dollars and Euros, currency movements can contribute to volatility in relative performance.

13.18 The tables below summarise performance to date for the pension fund's two legacy managers, HarbourVest and Aberdeen Standard.

**HarbourVest - £52.5m AUM**

	Performance	Benchmark	Relative
Quarter	-6.5%	10.2%	-16.7%
12 months	7.1%	-13.0%	20.1%
3 years p.a.	14.1%	-1.6%	15.7%
5 years p.a.	17.5%	2.9%	14.6%
Since inception p.a.	11.2%	4.4%	6.8%

**Aberdeen Standard - £28.9m AUM**

	Performance	Benchmark	Relative
Quarter	-13.7%	10.2%	-23.9%
12 months	-4.9%	-13.0%	8.1%
3 years p.a.	8.9%	-1.6%	10.5%
5 years p.a.	11.1%	2.9%	8.2%
Since inception p.a.	3.1%	4.8%	-1.7%

**Infrastructure**

13.19 As with Private Equity, Infrastructure is a long-term investment that takes several years for commitments to be fully invested. The pension fund has two external infrastructure managers, Hermes and IFM. The target for each manager is a 10% absolute annual return and this is used at the benchmark for these investments. Performance is summarised in the tables below:

**Hermes - £96.5m AUM**

	Performance	Benchmark	Relative
Quarter	1.5%	2.3%	-0.8%
12 months	10.9%	10.1%	0.8%
3 years p.a.	8.1%	10.0%	-1.9%
Since inception p.a.	8.6%	10.0%	-1.4%

**IFM - £106.7m AUM**

	Performance	Benchmark	Relative
Quarter	2.2%	2.3%	-0.1%
12 months	4.0%	10.1%	-6.1%
3 years p.a.	12.1%	10.0%	2.1%
Since inception p.a.	14.1%	10.0%	4.1%

13.20 The investments with IFM are denominated in US dollars but performance is measured in sterling, therefore currency movements can contribute to volatility in performance.

**Liability Driven Investment (LDI) - £360.7m AUM**

13.21 A proportion of the pension fund’s assets are held in an inflation hedging strategy, managed by Insight Investments which are not held to add growth, but to match the movements in the pension fund’s liabilities.

13.22 LDI strategies allow pension schemes to continue investing in return-seeking assets while hedging out their liability risks through the use of leverage. As at 30 June 2020, 12.0% of the pension fund’s assets were invested in the mandate but 34% of the pension fund’s liabilities were hedged against inflation sensitivity i.e. if liabilities increased by £100M (purely as a result of changes to inflation expectations), the value of the assets under management would be expected to increase by approximately £34M.

13.23 The liability matching strategy is intended to hedge against the impact of increasing pensions liabilities which are linked to the Consumer Prices Index (CPI). CPI cannot currently be hedged as there is not a sufficiently developed futures market, so the Fund’s strategy targets the Retail Prices Index (RPI) swaps market to act as a proxy for CPI which tends to be lower than RPI.

13.24 The performance of the manager is detailed in Appendix 5 and summarised below.

	Performance	Benchmark	Relative
Quarter	17.6%	17.3%	0.3%
12 months	-10.9%	-10.4%	-0.5%
3 years p.a.	-1.3%	-1.4%	0.1%
5 years p.a.	2.1%	2.0%	0.1%
Since inception p.a.	5.6%	4.9%	0.7%

**14. Brunel Pension Partnership**

14.1 Mark Mansley resigned as Brunel’s Chief Investment Officer in May 2020 and has left the company. Interviews for a replacement have now taken place and an appointment is expected to be announced shortly.

- 14.2 Until a replacement is appointed and in post, the heads of Listed Markets, Private Markets and Responsible Investing (David Cox, Richard Fanshawe and Faith Ward respectively) will report directly to Laura Chappell, Brunel's Chief Executive Officer.
- 14.3 James Russell-Stracey has been appointed by Brunel as Chief Stakeholder Officer. This is a board level appointment with management responsibility for Brunel's client relationship team and is intended to provide an improved 'conduit' between the shareholders/clients and the company. James is leading the review of the partnership governance arrangements that had begun before his appointment.

**15. Pension Fund Accounts 2019-20 (Appendix 6)**

- 15.1 The draft unaudited pension fund accounts for 2019-20 have been completed and are now subject to review by Dorset Council's auditors, Deloitte LLP. It is expected that the auditors will conclude their review shortly and their findings will be reported to the Committee as soon as they are known.

**Footnote:**

Issues relating to financial, legal, environmental, economic and equalities implications have been considered and any information relevant to the decision is included within the report.