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# Dorset Pension Fund

## Investment Strategy Review 2023

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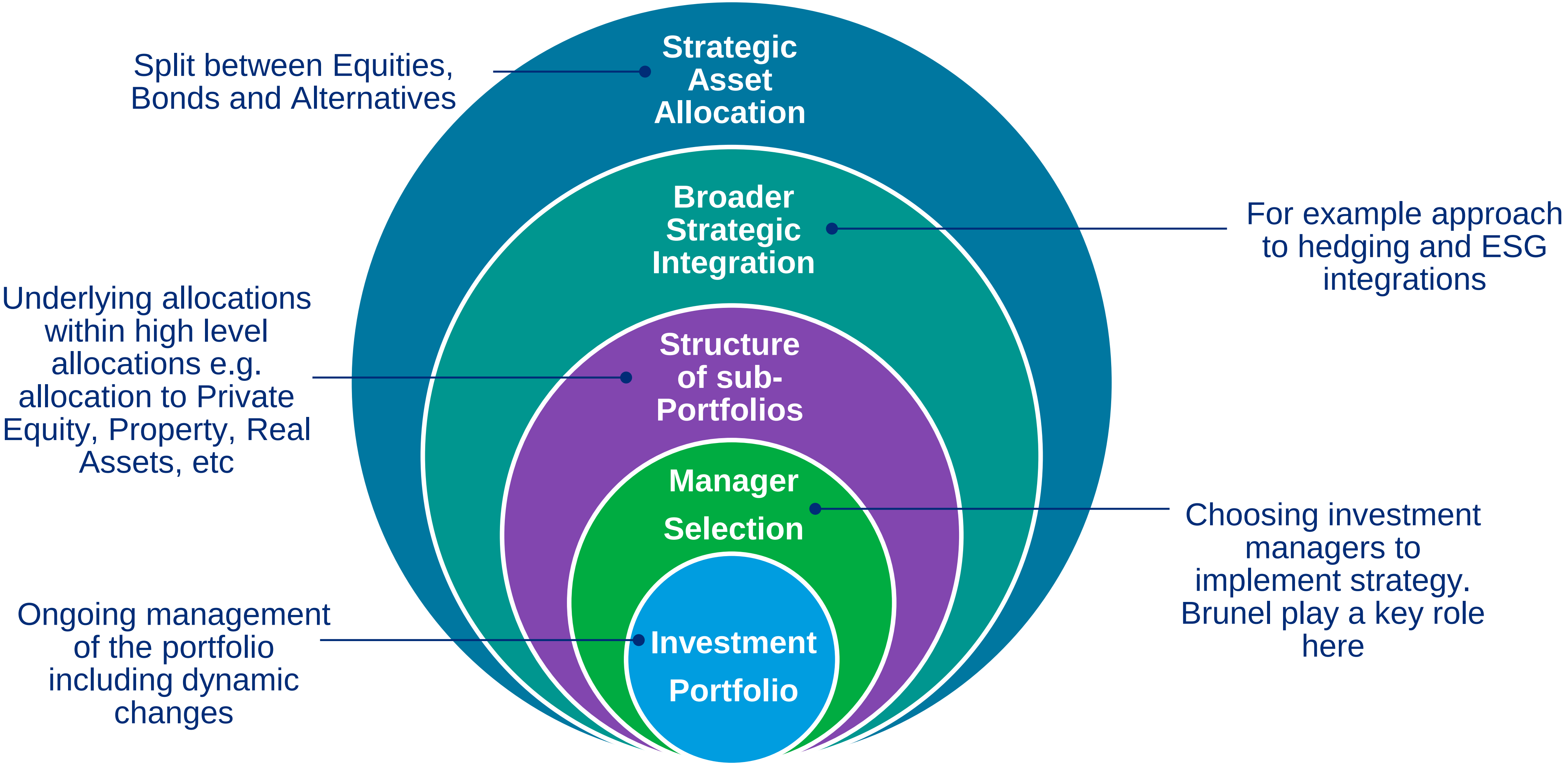
June 2023

A business of Marsh McLennan

# Investment Strategy

## Asset allocation is the key driver of performance




**Top level strategic decisions account for 80/90% of returns**

# Setting the scene

## What is the Fund looking to achieve?

**96%**

The funding level as at 31 March 2022 as formally calculated by the Fund's actuary.

**4.9%**

The 31 March 2022 actuarial discount rate

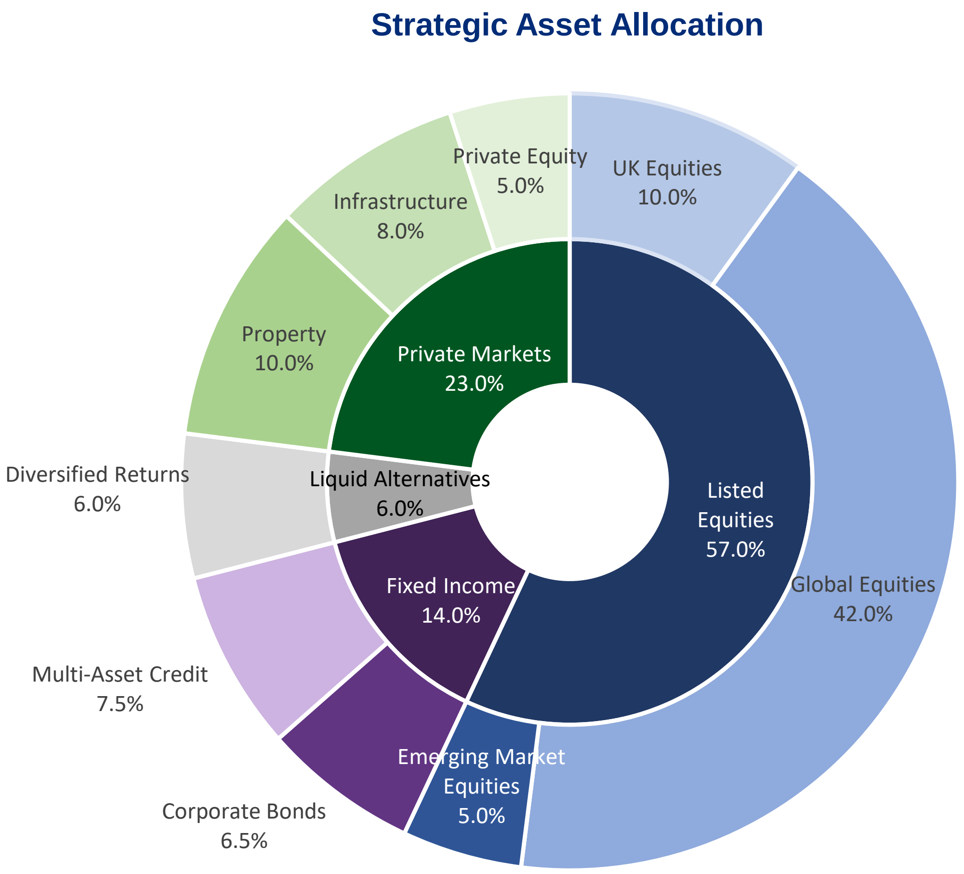
### What are we looking to achieve from an investment strategy perspective?

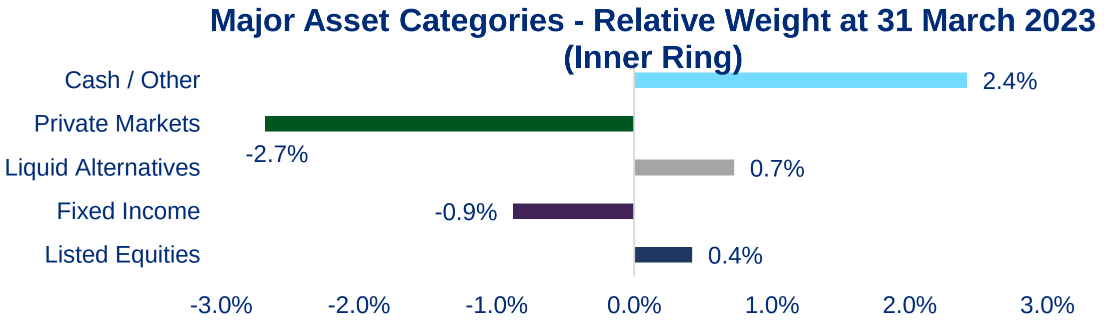
- Keeping contribution rates affordable but stable (need to achieve the discount rate)
- Continue improvement in funding level (need to outperform the discount rate)
- Mitigating impact of potential downside events (need to balance short/medium/long-term investment horizons)

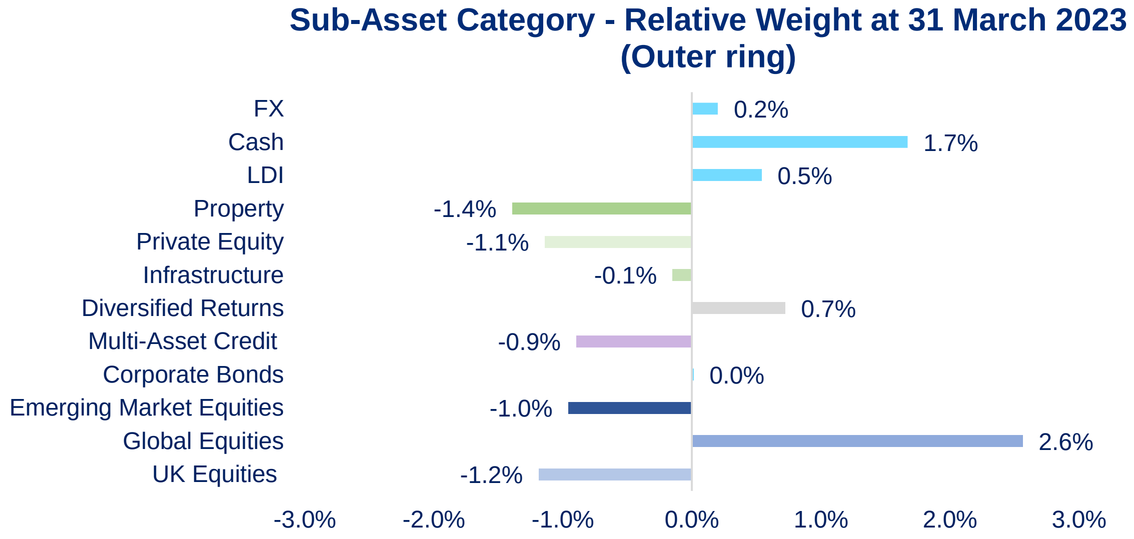
### Actuarial Valuation Movements

- **Funding level improved** from **92%** in 2019 to **96%** in 2022
- **Deficit improved** from **£255m** in 2019 to **£154m**
- **Discount rate fell** from **5.0%** in 2019 to **4.9%**
- Improvement has been driven by growth in asset valuations
- Small offsetting of funding gain driven by strengthening of the discount rate

# Strategic Asset Allocation




**As at 31 March 2023, the Fund was invested broadly in line with the Strategic Asset Allocation**

# Setting the scene

## Key Messages

**Background**

- In 2022, the Fund terminated its 12% allocation to LDI, reducing its weighting towards inflation hedging assets (by 12%). As a result, the strategic allocation to Global Equities was increased by 7.0% (35.0% to 42.0%). The allocations to Corporate Bonds and Multi Asset Credit were increased by 2.5% respectively (4.0% to 6.5%) and (5.0% to 7.5%).
- Mercer and Officers considered a number of investment strategies as part of this review, only some of which has been shown in this report.

**Results of the analysis**

- The **probability of achieving the discount rate** is 58% and leaves limited room for de-risking. However, this is **up materially from when we conducted the 2020 strategy review,** where there was a 40% probability of achieving the discount rate (5.0% p.a.).
- One of the key conclusions through the extensive modelling is that **the current investment strategy is relatively efficient,** making it hard to improve the risk/return characteristics given the Fund's return requirements.
- This shows the hard work that the Committee and Officers have put in into building a diversified investment strategy over a significant number of years, and **provides comfort in the Fund's current strategic asset allocation.**
- **While we are comfortable with the current Strategic Asset Allocation, we have highlighted a number of areas for the Committee to consider.**

**Potential Ideas**

1. The material rises in yields has made Fixed Income more attractive. **The Fund increased allocations to Fixed Income in 2022 and has captured some of this rise in yields.** However, its difficult to increase allocations materially without reducing expected return given where it could be funded from (equities / DGF).
2. Aligning the strategic allocation to property with the current allocation would **remove the need to consider rebalancing property with an investment**. The outlook for commercial property remains uncertain in the current macro environment.

The current investment strategy is relatively efficient - wholesale changes are not required

There is a 1 in 20 chance that assets could fall by c.40% over a 3 year period.

58% chance of meeting the discount rate – up from 40% at the 2020 review

Other potential ideas, but not likely to have large risk/return impacts. To have a material impact would require a large (c.10% increase in equities)

**Potential Ideas Continued**

3. The Fund has **scope to reduce the complexity of the ~~its~~ equity portfolio**. Further work would be required to review portfolio construction of the equity assets.
4. **We see Affordable Housing as an attractive asset class** from an investment and ESG/Sustainability perspective. It offers diversification versus commercial real estate sectors, is less sensitive to wider economic and financial market risk factors and fits well the government's Levelling-up agenda.
5. The Fund has previously reviewed whether to make an allocation to Private Debt. We continue to see merit in an allocation. Yield rises in public fixed income markets fed through to Private Debt and an allocation to **Private Debt could help meet this discount rate while delivering cashflows for the Fund,** which will become more important as the Fund matures.
6. Rebalancing is an important discipline. **Once the strategy has been agreed, we would suggest the rebalancing policy is reviewed.** Our initial thoughts are some of the tolerances look quite tight.

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