East Sussex County Council

# PENSION COMMITTEE

MONDAY, 12 JULY 2021

10.00 AM COUNCIL CHAMBER, COUNTY HALL, LEWES

**++ Please note that this meeting will be held in person++**

MEMBERSHIP - Councillor Gerard Fox (Chair)
Councillors Sam Adeniji, Julia Hilton, Paul Redstone and David Tutt

## A G E N D A

1 Minutes *(Pages 3 - 14)*

2 Apologies for absence

3 Disclosure of Interests

Disclosures by all Members present of personal interests in matters on the agenda, the nature of any interest and whether the Members regard the interest as prejudicial under the terms of the Code of Conduct.

4 Urgent items

Notification of items which the Chair considers to be urgent and proposes to take at the appropriate part of the agenda.

5 Investment Strategy Review *(Pages 15 - 68)*

6 Work programme *(Pages 69 - 82)*

7 Any other non-exempt items previously notified under agenda item 4

8 Exclusion of the public and press
To consider excluding the public and press from the meeting for the remaining agenda item on the grounds that if the public and press were present there would be disclosure to them of exempt information as specified in paragraph 3 of Part 1 of the Local Government Act 1972 (as amended), namely information relating to the financial or business affairs of any particular person (including the authority holding that information).

9 Environmental Social and Governance Impact Assessment *(Pages 83 - 192)*

10 Investment Report *(Pages 193 - 230)*

11 Any other exempt items previously notified under agenda item 4

PHILIP BAKER
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2 July 2021

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NOTE: *As part of the County Council's drive to increase accessibility to its public meetings, this meeting will be broadcast live on its website and the record archived. The live broadcast is accessible at: www.eastsussex.gov.uk/yourcouncil/webcasts/default.htm*

PENSION COMMITTEE

MINUTES of a meeting of the Pension Committee held at Council Chamber, County Hall, Lewes on 22 June 2021.

| | |
|---|---|
| PRESENT | Councillors Gerard Fox (Chair) Councillors Sam Adeniji, Julia Hilton, Paul Redstone and David Tutt |
| ALSO PRESENT | Ray Martin, Chair of the Pension Board<br>Ian Gutsell, Chief Finance Officer<br>Sian Kunert, Head of Pensions<br>Russell Wood, Pensions Manager: Investment and Accounting<br>Paul Punter, Head of Pensions Administration<br>Nigel Chilcott, Audit Manager<br>Danny Simpson, Principal Auditor<br>William Bourne, Independent Adviser<br>Andrew Singh, Isio<br>Darrell Tovey, Vigeo Eiris<br>Ornella Dilorio, Vigeo Eiris<br>Guillaume Checri, Vigeo Eiris<br>Martin Jenks, Senior Democratic Services Adviser<br>Harvey Winder, Democratic Services Officer |

1 MINUTES

1.1 The minutes of the previous meeting held on 1 March 2021 were agreed as a correct record subject to the following amendments:

- Amend 67.2 para 6 to read "The PRI discussed a number of signatory member approaches including active engagement incorporating escalation which involved asset managers( as shareholders of the company) voting against a company's accounts or board of directors where they are not taking sufficient action on carbon emissions and with, in some cases, divestment as the final step. For passive mandates this is difficult as divestment from individual companies and or sectors is not possible, however, passive managers can still vote against a company's accounts or board of directors each year. Over time, this should still send a strong message as it gathers momentum and more investors sign up to PRI."
- Add the following clarification to 67.2 para 5: *(it was clarified after the meeting that the date was 2050 and that it was not binding).*

2 APOLOGIES FOR ABSENCE

2.1 There were no apologies for absence.

3 DISCLOSURE OF INTERESTS

3.1 Cllr David Tutt declared a personal, non-prejudicial interest in item 21 as the Leader of Eastbourne Borough Council, which is involved in an ongoing admission agreement with a sub-contractor.

4 URGENT ITEMS

4.1 There were no urgent items.

5 PENSION BOARD MINUTES

5.1 The Committee considered the minutes of the Pension Board meeting held on 1st June 2021.

5.2 The Committee RESOLVED to note the minutes.

6 INVESTMENT REPORT

6.1 The Committee considered a report providing an update on the investment activities undertaken by the East Sussex Pension Fund (ESPF or the Fund).

6.2 The Committee's discussion included the following key issues:

- Despite the impact of COVID-19, Isio, the Fund's investment advisor, advised that it is important to retain a diversified portfolio containing exposure to various property types, particularly as businesses begin to pay back rent arrears accrued during the pandemic lockdowns, which commercial property managers agreed to at the time. It is not always easy to change the weighting of the holdings from one property type to the other, however, Schroders, the asset manager for the Fund's property portfolio, is a fund of fund managers, which enables it to be somewhat flexible in how it balances its property portfolio to where it sees maximum returns. Retail is currently the most volatile property type, but Schroders has only around 20% exposure to retail, which Isio is not concerned about.
- Whilst it is a valid concern that the cost of refitting buildings to meet climate emission goals could be a risk to the Fund's property assets in the coming years, the majority of returns achieved by Schroder are through rental income rather than through capital appreciation, which is less exposed to the effect of building costs. Schroders, however, could be asked its views on the matter. In addition, Schroders is outside the ACCESS pool and ACCESS is currently looking at illiquid assets, however, it will be 2-3 years before any illiquid pool will be established and the exit costs for property are high. It would therefore be unadvisable to divest from property until it is clear what, if any, alternative ACCESS was offering. ACCESS is in the process of tendering a consultant to do this work.
- There were considerable discrepancies between the two sources of performance for the ATLAS Infrastructure Fund – those from the fund managers themselves and those produced by the Fund's custodian, Northern Trust – Isio has asked Northern Trust to investigate further, as their figures appeared accurate. This is not uncommon occurrence as performance figures are always a snapshot in time and can change daily due to events like cash flow movements.

- The Fund's equity portfolio has a slight bias towards growth stocks against value stocks, however, growth stocks have outperformed value stocks over the past few years due to the low interest rates, which encourage investment in assets that will give higher future returns compared to dividend payments. This is likely to continue until interest rates change. The Fund has value stock exposure through Longview, which tilts towards value stocks over growth stocks.
- The snapshot of the Fund's exposure to fossil fuels seen in the quarter 1 report is backwards looking and includes the UBS funds that the Committee agreed to divest from at the last meeting. These funds will fall out in future reporting and fossil fuel exposure will be reduced considerably as a consequence. Isio will present a report on the investment managers' approach to Environmental, Social and Governance (ESG) issues, including fossil fuel exposure, at the next Committee meeting.

6.3 The Committee RESOLVED to:

1) note the Action Log and Investment Workplan (appendix 1);

2) note the Quarterly Investment Report from the Investment Advisor, Isio (appendix2);

3) receive Fixed Income training (appendix 3);

4) note the Fixed Income Review of Current Holdings (appendix 4);

5) note the ACCESS Pool update;

6) note the high level carbon foot printing and energy transition scores for the Fund's managers.

7 GOVERNANCE REPORT

7.1 The Committee considered a report providing an update on various governance workstreams completed and changes effecting Local Government Pension Schemes (LGPS) and the ESPF specifically.

7.2 The Committee's discussion included the following key issues:

- The Pensions Administration Team (PAT) will meet again with Prudential at the end of June about the performance of their Additional Voluntary Contribution (AVC) service. The Fund will also be conducting a review of AVC providers in the near future and will come back to the Committee with any recommendations for action.
- As part of the new Risk Management Policy, the Committee should receive more timely updates of emerging risks including via email if the Committee is not due to meet when a risk emerges.

7.3 The Committee RESOLVED to:

1) Approve the change in the wording of the Internal Dispute Resolution (Appendix1);

2) Approve the new Risk Management policy (Appendix 2);

3) Note the potential change in The Pension Regulator (TPR) expectations;

4) Approve the new approach to manage requests for fees to be waived due to financial hardship (Appendix 4);

5) Approve the revised Governance and Compliance Statement (Appendix 6);

6) Note the planned production of an annual report of the Pension Board to the Pension Committee;

7) Note the update on the McCloud Working Group;

8) Note developments on the Scheme Advisory Board Good Governance project;

9) Note the update on Additional Voluntary Contributions (AVC's) and approve a review of the AVC provider later in the year; and

10) request more timely risk register proposed strategy management updates via email where appropriate.

## 8 ABATEMENT POLICY REVIEW

8.1 The Committee considered a report seeking approval for changes to the Administering Authority's policy on abatement.

8.2 The Committee asked what would happen to employees who will have returned to work under the old abatement policy between 2014 and 1 April 2021 and who may be entitled to move onto the new policy (back dated to 1 April 2021) but who may not be aware they are entitled to do so. The administration system does not flag whether someone has returned to work under an abated policy, so it is not known how many may be affected. Furthermore, not all members returning to work in the period 2014-2021 will have necessarily been subject to an abated pension, as it depends on the salary of the role they are returning to as to whether abatement was applied fully or in part, or not at all. This means only those with a suspended pension could be easily spotted. The only way to identify all those who are affected, and the costs involved in moving them all on to the new scheme, is to ask all members receiving a pension whether it has been abated, which the PAT intends to do but which may take some time. Once identified, these employees will have their pension put to the full monetary value as of 1 April 2021.

8.3 The Committee RESOLVED to:

1) approve the removal of the abatement with effect from 1 April 2021; and

2) delegate authority to the Chief Finance Officer, in consultation with the Chair, to take all necessary actions to give effect to the implementation of the above recommendation

## 9 PENSIONS ADMINISTRATION REPORT

9.1 The Committee considered a report providing an update on matters relating to Pensions Administration activities.

9.2 The Committee RESOLVED to note the report.

## 10 INTERNAL AUDIT REPORTS AND INTERNAL AUDIT STRATEGY FOR THE PENSION FUND (ESPF)

10.1 The Committee considered a report containing a number of internal audit reports and seeking approval of the draft Internal Audit Strategy for Pensions 2021/22.

10.2 The Committee's discussion included the following key issues:

- Internal Audit will test the migration of all data from the instance of Altair held on Surrey County Council servers to East Sussex County Council to see if all data has transferred over successfully, or if there are any discrepancies. This will take place in July, once the project is complete.
- The Committee asked report authors to minimise jargon when describing internal audits. Definitions of terms like Altair and i-Connect should also be included for the benefit of new members.
- The two red rated actions in the Information Governance review are well underway to be resolved.

10.3 The Committee RESOLVED to:

1. note the internal audit reports attached as appendices 1-4; and

2. approve the 2021/22 Internal Audit Strategy for Pensions (Appendix 5).

## 11 EXTERNAL AUDIT PLAN FOR EAST SUSSEX PENSION FUND 2020/21

11.1 The Committee considered a report on the Fund's external audit plan for 2020/21.

11.2 The Committee resolved to note the report.

## 12 EMPLOYER ENGAGEMENT AND CONTRIBUTIONS REPORT

12.1 The Committee considered a report providing an update on Employer Engagement activities including communications; and the collection of Employer contributions up to March 2021 which were due on 19 April 2021.

12.2 The Committee resolved to note the report.

## 13 EAST SUSSEX PENSION FUND (ESPF) QUARTERLY BUDGET REPORT

13.1 The Committee considered a report on the latest quarterly Financial Outturn report for 2020/21.

13.2 The Committee RESOLVED to note the report.

## 14 RISK REGISTER

14.1 The Committee Considered the Fund's Risk Register.

14.2 The Committee discussed how the register at Appendix 1 is the overall strategic risk register covering high level administration, governance and investment risks. The investment risks are high-level macro-economic risks and the Committee has previously requested a more detailed investment risk register that sits beneath this strategic risk register. This will be produced following discussions at the strategy review day in July, where statement of investment principles will also be considered.

14.3 The Committee RESOLVED to agree the risk rating of new risks as set out in Appendix 1.

## 15 WORK PROGRAMME

15.1 The Committee considered its work programme.

15.2 The Committee's discussion included the following key issues:

- Consideration should be given to providing the Committee with some reports earlier than the statutory publication date of five clear working days before the meeting.
- Bite-sized training sessions are preferable to half-day sessions.

15.3 The Committee RESOLVED to agree its work programme.

## 16 EXCLUSION OF THE PUBLIC AND PRESS

16.1 The Committee RESOLVED to exclude the public and press from the meeting for the remaining agenda item on the grounds that if the public and press were present there would be disclosure to them of exempt information as specified in paragraph 3 of Part 1 of the Local Government Act 1972 (as amended), namely information relating to the financial or business affairs of any particular person (including the authority holding that information).

## 17 CARBON FOOTPRINT REPORT

17.1 The Committee considered a report providing an update on the carbon footprint of the Fund's liquid investments as at 31 March 2021.

17.2 A summary of the discussion is set out in an exempt minute.

17.3 The Committee RESOLVED to note the report.

## 18 INVESTMENT REPORT

18.1 The Committee considered a report providing an update on the investment activities undertaken by the Fund that are confidential exempt under the Local Government Act 1972.

18.2 A summary of the discussion is set out in an exempt minute.

18.3 The Committee RESOLVED to agree actions which are set out in an exempt minute.

## 19 PENSION FUND BREACHES LOG AND INTERNAL DISPUTE RESOLUTION PROCEDURE CASE REPORT

19.1 The Committee considered the ESPF breaches Log.

19.2 A summary of the discussion is set out in an exempt minute.

19.3 The Committee RESOLVED to agree the recommendations as set out in the report.

## 20 EMPLOYER ADMISSIONS AND CESSATIONS

20.1 The Committee considered an update on the latest admissions and cessations of employers within the Fund.

20.2 The Committee RESOLVED to agree the recommendations as set out in the report.

The meeting ended at 1.40 pm.

Councillor Gerard Fox (Chair)

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By virtue of paragraph(s) 3 of Part 1 of Schedule 12A
of the Local Government Act 1972.

Appendix 1

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**Report to:** **Pension Committee**

**Date of meeting:** **12 July 2021**

**By:** **Chief Financial Officer**

**Title of report:** **Investment Strategy Review**

**Purpose:** **This report provides Pension Committee with an overview of the investment strategy and direction of travel for the East Sussex Pension Fund.**

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**RECOMMENDATION**

**The Pension Committee is recommended to:**

1) **note the Investment Strategy report (Appendix 1);**
2) **Agree the following proposed strategic asset allocation (as set out paragraph 4.1-4.7):**

| Asset Class | % |
|---|---|
| Global Equity | 40.0 |
| Diversified Growth | 17.0 |
| Private Equity | 5.5 |
| Balanced Property | 7.0 |
| Inflation-Linked Property | 4.0 |
| Infrastructure Equity | 11.0 |
| Private Credit | 5.0 |
| Diversified Credit | 10.5 |
| Corporate Bonds | - |
| Index-Linked Gilts | - |
| Cash | - |

**3) delegate authority to the Chief Finance Officer, in consultation with the Chair, to take all necessary actions to give effect to the implementation of the above recommendation.**

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## 1. Background

1.1 Under the Local Government Pension Scheme (LGPS) Regulations, the Council is required to maintain a Pension Fund for its employees and other ‘scheduled bodies’ as defined in the Regulations. The Pension Committee is required to maintain an Investment Strategy Statement (ISS) to govern the East Sussex Pension Fund’s (ESPF or the Fund) investments and needs to review this periodically to ensure it is still fit for purpose.

1.2 To assist the Committee Isio has undertaken a detailed review of the Fund’s overall investment strategy in order to quantify the inherent risks and to consider options for the evolution of the asset allocation. As well as high level asset allocation, Isio has focus on certain key specific areas of the portfolio, to provide recommendations on how the committee might evolve the strategy going forward.

**2. Investment Strategy Review**

2.1 The Committee requested a review of the current investment strategy, Isio has prepared some training on the salient points on the function of the investment strategy and areas for consideration by the Committee which is planned in advance of this meeting. The training will be recorded and sent to Committee Members unable to attend at the scheduled time slot.

2.2 The objectives of the Investment Strategy is to deliver a return that improves the funding level over time (to achieve future lower employer contribution rates), with as little volatility in the funding level as possible (to maintain stability of contributions as far as possible), and maintain sufficient assets to meet liabilities i.e. an overall funding level of 100% or more. The assumptions underlying the Actuary's funding basis are important factors in determining the return requirement. As the Fund grows, it will also be important to ensure that stability, relative to sponsor budgets, is maintained. The Fund's current strategy is shown below:

| Asset Class | % |
|---|---|
| Global Equity | 40.0 |
| Diversified Growth | 20.0 |
| Private Equity | 5.5 |
| Balanced Property | 10.0 |
| Infrastructure Equity | 8.0 |
| Private Credit | 3.0 |
| Diversified Credit | 7.0 |
| Corporate Bonds | 3.5 |
| Index-Linked Gilts | 3.0 |
| Cash | - |

2.3 The current Investment Strategy is positioned so that it can achieve an expected return of 5.3% per annum. This level of return has been factored into the valuation calculations in the 2019 valuations. To move the expected return of the strategy down i.e. to remove some of the investment risk in the portfolio would also require the Actuary to adjust the valuation calculations which could result in increased contributions from employers. The next triennial valuation will take place based on the data as at 31 March 2022, with new contribution rates for employers coming into effect from April 2023.

2.4 The Committee should consider the strategic direction of the Fund in relation to its clear principles in relation to Environmental, Social and Governance (ESG) issues which are summarised in the Statement of Responsible Investment (RI) Principles. These are as follows:

1. Apply long-term thinking to deliver long-term sustainable returns.
2. Seek sustainable returns from well-governed assets.
3. Use an evidence-based long term investment appraisal to inform decision-making in the implementation of RI principles and consider the costs of RI decisions consistent with our fiduciary duties.

4. Evaluate and manage carbon exposure in order to mitigate risks to the Fund from climate change.

It is important to ensure the strategy is aligned with these principles.

2.5 Based on the estimated 31 March 2021 position and median predicted outcome going forward, the expectation is the Fund will be in a surplus of c. £540m in 3 years' time (up from c. £280m at the end of March 2021). Ultimately any surplus could be used to bring down the future service cost of the Fund to the employers.

2.6 Given the current investment risk in the strategy, there is a 1 in 20 chance that a deficit of c.£1,072m or more could arise in 3 years' time –this would trigger a need for the deficit contribution rate to be paid in addition to the cost of future accrual.

2.7 Given the current strong funding position, there is scope to reduce investment risk and lessen the impact of any potential downside scenarios, essentially narrowing the range of potential outcomes. Reducing investment risk, and narrowing the range of potential return outcomes, would reduce the potential variability of contribution rates at future valuations. This could be done with minimal impact to expected returns.

2.8 The Fund's key risks are equity exposure and the interest rates / inflation risk inherent within the value placed on the liabilities. The 40% strategic allocation to equities means that a fall in equity valuations would result in a material decrease in the Fund's assets (similar to that experienced over Q1 2020, although this was quickly reversed). The significant risk from inflation is due to the majority of the pension benefits in the Fund being directly linked to inflation. While the Fund's discount rate is not explicitly linked to interest rates, it is assumed that a change in long term interest rates will be reflected to some degree in a change in the expected future returns from the investment strategy, and consequently also in the Actuary's discount rate.

## 3. Proposed direction of travel

3.1 The Committee should look to **increase exposure to assets with direct inflation-linkage.** Rising inflation is a key risk to the Fund given the liability structure; and increasing the allocation to assets with direct inflation linkage would help address this risk. e.g. infrastructure and long lease property.

3.2 **Increase exposure to less liquid assets**. Given the Fund's long term horizon, and the overall level of liquidity in the current portfolio, there is scope to target less liquid opportunities e.g. private market debt, equity and infrastructure to a greater degree and earn an excess return for doing so.

3.3 **Increase alignment to Responsible Investment Policy**. The Fund has made strong progress incorporating ESG considerations into its investment strategy and this is expected to remain a key focus going forward.

3.4 **Pooling of assets**. The regulatory environment directs the pooling of assets going forward. This will need to be considered in conjunction with setting the investment strategy and implementation of decisions.

3.5 Strategy changes should be considered as a direction of travel rather than an instant change in investment. All investment changes will require comprehensive due diligence in advance of a specific subscription. In addition, it takes time to find new investments that suitably align to the risk and reward parameters that the strategic changes are looking to achieve. Illiquid assets often have queue of commitments, meaning that the money is not paid to the new investment manager until they have found a new assets to purchase with the committed investment, so the actual asset allocation can look different to the strategic allocation even where a new manager has been selected and the investment subscription is complete, it can take years for the commitment to be drawn down (meaning the cash is paid over). In addition, some asset classes also have exit costs associated with them while others are very volatile, so timing of moving any asset would be considered carefully by the Investment consultant, officers and a transition management team where appropriate. Multiple strategy changes could play out over a couple of years and could take longer if the Fund is reliant of the ACCESS Pool to offer a new asset class.

## 4. Proposed Portfolio

4.1 Isio has provided a proposed new structure to the Fund's Strategic Asset Allocation which is anticipated to slightly increase the expected return from 5.3% to 5.5% and subsequently raise the expected surplus of the Fund. This would also provide a better 3 year 1 in 20 downside position. The suggested changes would also increase the assets with a direct linkage to inflation to circa 15% from the current linkage circa 11%. The alternate Strategic asset allocation is provided below showing the movement between asset classes:

| | Current | Proposed | Movement |
|---|---|---|---|
| Asset Class | % | % | % |
| Global Equity | 40.0 | 40.0 | - |
| Diversified Growth | 20.0 | 17.0 | (3.0) |
| Private Equity | 5.5 | 5.5 | - |
| Balanced Property | 10.0 | 7.0 | (3.0) |
| Inflation-Linked Property | - | 4.0 | 4.0 |
| Infrastructure Equity | 8.0 | 11.0 | 3.0 |
| Private Credit | 3.0 | 5.0 | 2.0 |
| Diversified Credit | 7.0 | 10.5 | 3.5 |
| Corporate Bonds | 3.5 | - | (3.5) |
| Index-Linked Gilts | 3.0 | - | (3.0) |
| Cash | - | - | - |

4.2 Isio will talk through the planned strategic changes, reasoning and impact as they present their report in **Appendix 1**.

4.3 The Fund has delivered strong investment returns in recent years during a period in which most asset markets have trended upwards, with the equity exposure being particularly beneficial, however, liabilities have also increased since the last valuation, meaning the funding position has remained neutral, as at 31 March 2021, at 106% funded. The proposed strategy changes have been recommended to address the current investment risks that the Fund is facing. The latest Funding Position report from the Actuary is included in **Appendix 2** for information on how the funding position has moved since the last valuation and the importance of maintaining sufficient return on investments

4.4 Whilst equity risk remains one of the Fund's biggest risks, the Fund should maintain its existing strategic allocation to equities as a long term driver of overall return, and focus on increasing allocations to assets with direct inflation exposure, to help address the risk of rising inflation. In addition investing more into less liquid assets allow the fund to target a premium for being able to tie up its capital, as a long term investor.

4.5 Isio recommend that the Fund should seek to continue building out the real assets portfolio, with a particular focus on opportunities within infrastructure. This would serve not only to increase the portion of Fund assets with direct inflation exposure, helping to address a significant risk facing the Fund, but could also be implemented to further demonstrate the Fund's commitment to sustainable investments. Alongside this, the Fund could consider introducing exposure to property assets with a direct inflation linked income stream to further increase the inflation protection.

4.6 Isio recommend the Fund's allocation to corporate bonds should be switched into diversified credit, which exhibits a more attractive risk/return profile (as a result of its wider opportunity set and active management). This strategy change would also help to improve the ESG positioning of the Fund and reduce climate risks, as this portfolio has relatively high investment in fossil fuel companies compared to its other holdings – although this is more through utilities companies than energy extraction, such as, oil and gas majors.

4.7 Further commitments to commercial real estate debt and private debt more broadly should be considered, in order to harvest the premium available and to broaden the Funds private debt exposure.

## 5. Implementation

5.1 To consider the implementation of the proposed changes, officers would first look to which assets classes are available through the ACCESS pool and where these are not currently in place the anticipated timeline to be on the pool. Officers will also take into consideration any developments in the issuance of further pooling statutory guidance from the Ministry and Housing Communities and Local Government (MHCLG).

5.2 Where strategic changes cannot be implemented within the ACCESS pool, the Fund would need to consider whether it could access the asset class temporarily until such time as the Pool can bring the asset class on line and work with the pool to implement the required changes to access via the pool. A temporary investment would be more possible in liquid asset classes, or though open-ended investments of more illiquid asset classes. There can be significant costs exiting certain assets and the Fund would never want to be a forced seller of assets during a position of a market failure.

5.3 The Fund currently has 13 managers and 19 individual mandates, any restructuring of the Funds assets should be done with a view to minimise any increase to the number and complexity of the Fund arrangements to avoid further governance requirements.

5.4 ACCESS has a pipeline for work to bring Private Equity, Infrastructure and Real Estate available within the pool, these are not anticipated to be in place until 2022/2023 with a prioritisation for Private Equity in importance. Officers have reached out to other ACCESS funds and are aware a number of them have existing exposure to the same open ended infrastructure Fund that would be worth officers and advisers looking at as part of an implementation stage associated with this investment class,

5.5 ACCESS is currently working to launch 4 Multi Asset Credit sub funds (Diversified Credit) in October 2021, these are currently going through final implementation stages. One of the four is M&G Alpha Opportunities which the Fund currently invests. It is hoped that the proposed increased allocation to this asset class would be investable within the ACCESS pool when the new sub funds are launched.

5.6 After speaking with other ACCESS members, it does not appear that Long Dated Inflation linked property is a priority or existing investment of our counterparts, so may not be on the radar for the ACCESS Pool for a number of years.

## 6. Conclusion and reasons for recommendation

6.1 The Funds investment strategy is the primary driver for the return and investment risk of the Fund's assets. This needs to be regularly monitored to ensure that the Fund's strategic asset allocation balances the need to generate sufficient return against the investment risks the Fund is challenged with. The proposed new structure is an evolution of the current strategy to address the increased risk that inflation is believed to pose to the Fund's liabilities. Whilst also maintaining an acceptable level of return.

6.2 The Pension Committee is recommended to note the Investment Strategy report (**Appendix 1**) and agree the proposed strategic asset allocation:

| Asset Class | % |
|---|---|
| Global Equity | 40.0 |
| Diversified Growth | 17.0 |
| Private Equity | 5.5 |
| Balanced Property | 7.0 |
| Inflation-Linked Property | 4.0 |
| Infrastructure Equity | 11.0 |
| Private Credit | 5.0 |
| Diversified Credit | 10.5 |
| Corporate Bonds | - |
| Index-Linked Gilts | - |
| Cash | - |

**IAN GUTSELL**
**Chief Finance Officer**

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# East Sussex Pension Fund

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## Investment Strategy Review

July 2021

isio.

Appendix 1

Document Classification: Confidential

# Contents

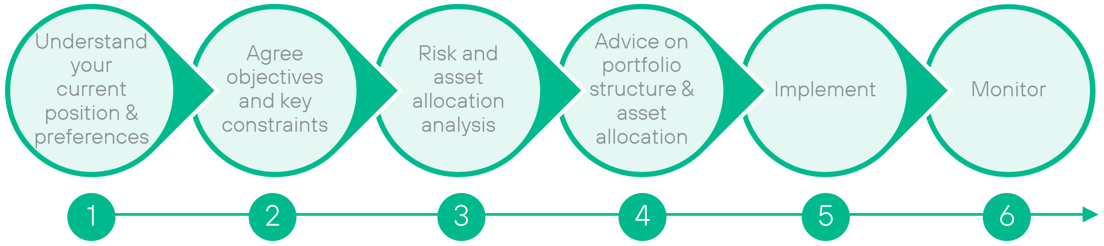
# Introduction

## Addressee

- This report is addressed to the East Sussex County Council ("the Council") as Administering Authority of the East Sussex Pension Fund ("the Fund").

## Background

- The Council has engaged Isio to undertake a detailed review of the Fund's overall investment strategy in order to quantify the inherent risks and to consider options for the evolution of the asset allocation. As well as high level asset allocation, Isio has been asked to focus on certain key specific areas of the portfolio, and to provide recommendations on how these should evolve going forward.
- The diagram below highlights the key stages in our approach for assessing overall investment strategy, with this paper focussing on stages 1-4.




## Scope of Report

- This paper provides a detailed review of the Fund's current investment strategy, asset allocation and investment structure, including:
  - Portfolio risk/return characteristics
  - The projected evolution of the funding position
  - An overview of the suitability of the Fund's equity, fixed income and diversified growth and real assets portfolios
  - An overview of the Fund's cash flow requirements, asset income and liquidity profile; and how these are expected to evolve going forward
  - An overview of any potential attractive asset class opportunities which could be suitable for the Fund
  - A range of alternative portfolios which we believe may be better aligned to the Fund's objectives.
- We have integrated environmental, social and governance ('ESG') considerations throughout the review, including in our assessment of how the portfolio could evolve going forwards. Such considerations have been evaluated with the Fund's ESG principles in mind.

# Objectives

## Financial Objectives

- We understand that the Fund's objectives, as outlined in the March 2020 Funding Strategy Statement, are:
    - To ensure the long-term solvency of the Fund, using a prudent long term view, to ensure that sufficient resources are available to meet all liabilities as they fall due.
    - To minimise the long-term cash contributions which employers need to pay to the Fund, by recognising the link between assets and liabilities and adopting an investment strategy which balances risk and return.
    - To reflect the different characteristics of different employers in determining contribution rates.
- Thus the objective is to deliver a return that improves the funding level over time (to achieve future lower employer contribution rates), with as little volatility in the funding level as possible (to maintain stability of contributions as far as possible), and maintain sufficient assets to meet liabilities i.e. an overall funding level of 100% or more. The assumptions underlying the Actuary's funding basis are important factors in determining the return requirement. As the Fund grows, it will also be important to ensure that stability, relative to sponsor budgets, is maintained.

## Evolution

- The Fund remains open to new members and future accrual. It is therefore growing due both due to interest accruing on past service liabilities, and due to new liability accrual. The liabilities are also maturing (the proportion of pensioner members is growing) and this will change the cash flow profile of the Fund over time. Ultimately more cash will be paid out than is received in cash contributions, making asset income an increasingly important consideration going forward.

## ESG

- In addition to the funding objectives, the Fund has clear principles in relation to ESG issues which are summarised in the Statement of Responsible Investment Principles. These are as follows:
    1. Apply long-term thinking to deliver long-term sustainable returns
    2. Seek sustainable returns from well-governed assets.
    3. Use an evidence-based long term investment appraisal to inform decision-making in the implementation of RI principles and consider the costs of RI decisions consistent with our fiduciary duties.
    4. Evaluate and manage carbon exposure in order to mitigate risks to the Fund from climate change.
- It is important to ensure the strategy is aligned with these principles.

# Objectives (continued)

## What Return is Required?

- At the March 2019 Actuarial Valuation, the discount rate used to value the liabilities was 4.0% p.a. The Actuary therefore requires the assets to deliver at least 4.0% p.a. to achieve full-funding based on the agreed contributions (all else being equal).
- The discount rate assumption is based upon the absolute level of returns that the asset portfolio is expected to achieve. As at 31 March 2019 the Actuary estimated that the Fund's assets had a 75% likelihood of achieving this return.
- As at the date of the modelling in this report, 31 March 2021, we estimated the expected return of the Fund's investment strategy to be 5.3% p.a. This is on a best estimate basis.
- The difference between the expected return of 5.3% p.a. and required return of 4.0% reflects an element of prudence in the Actuarial funding assumptions, which is to be expected.
- Given the significant surplus achieved and margin between the expected and required return, we believe there may be some scope to reduce overall risk and return if desired. However any change in expected return should be discussed with the Actuary prior to implementation to ensure this does not impact the funding methodology.

# Current strategy

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# Investment strategy overview

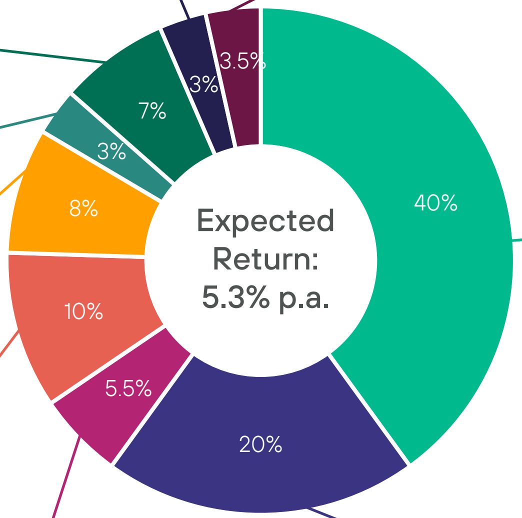
Key:
Strategic Weights in Chart
(Actual Allocations) in brackets

**Index-Linked Gilts (3%)**
UBS Over 5 Year IL Gilt Fund: £129m (3%)

**Fixed Interest Bonds (2%)**
M&G Corporate Bonds: £158m (4%)

**Diversified Credit (7%)**
M&G Alpha Opportunities: £285m (7%)

**Private Debt (1%)**
M&G Private Debt: £42m (1%)




**Equity (42%)**
UBS Global Equities: £362m (9%)
USB UK Equity: £67m (2%)
Longview Global Equity: £459m (11%)
WHEB Sustainability Fund: £223m (5%)
Wellington Global Impact Fund: £223m (5%)
Storebrand Global ESG Plus Fund: £455m (11%)

**Infrastructure (4%)**
UBS Infrastructure: £38m (1%)
Pantheon Infrastructure: £38m (1%)
M&G Infrastructure: £33m (1%)
ATLAS Global Infrastructure: £77m (2%)

**Property (8%)**
Schroders Property: £348m (8%)

**Private Equity (6%)**
HarbourVest Private Equity: £111m (3%)
Adams Street Private Equity: £155m (4%)

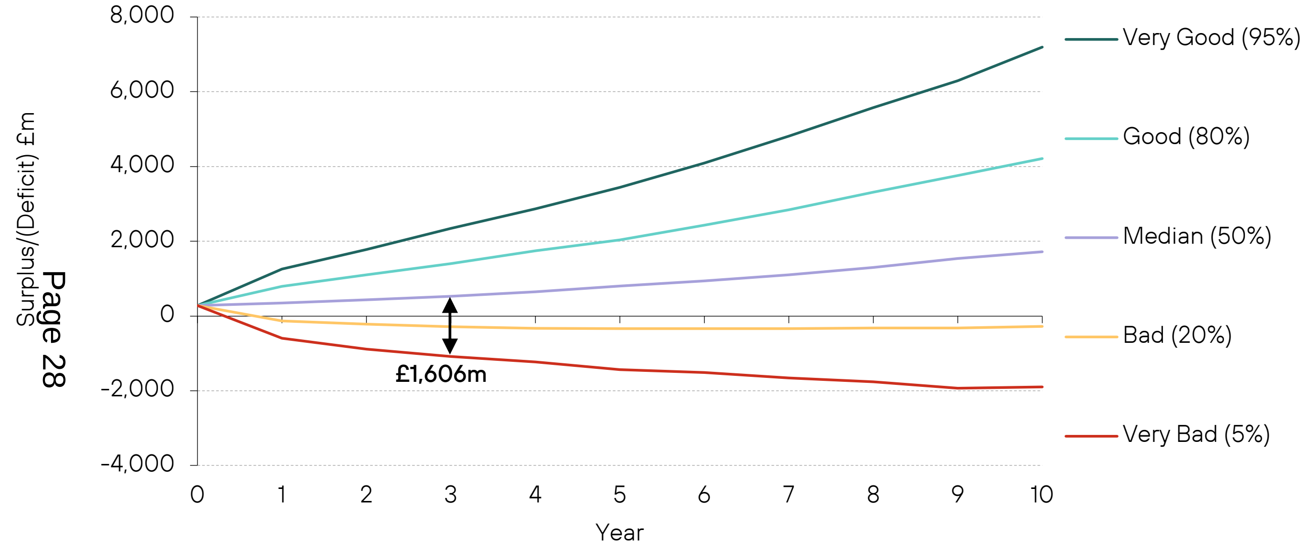
**Diversified Growth (24%)**
Newton Absolute Return: £492m (12%)
Ruffer Absolute Return Fund: £510m (12%)



Source: Investment managers at 31 March 2021.

# Funding trajectory

## Current Funding Trajectory




| Funding Position – 31 March 2021 | |
|---|---|
| Discount rate | 4.0% |
| Current surplus (deficit) | £277m |
| Current funding level | c.107% |

| Forecast Funding Position – 3 Years' Time | |
|---|---|
| Expected deficit / surplus | £524m |
| Expected funding level | c. 114% |
| Estimated Funding Deficit 1 in 20 chance (5%) | (£1,082m) |

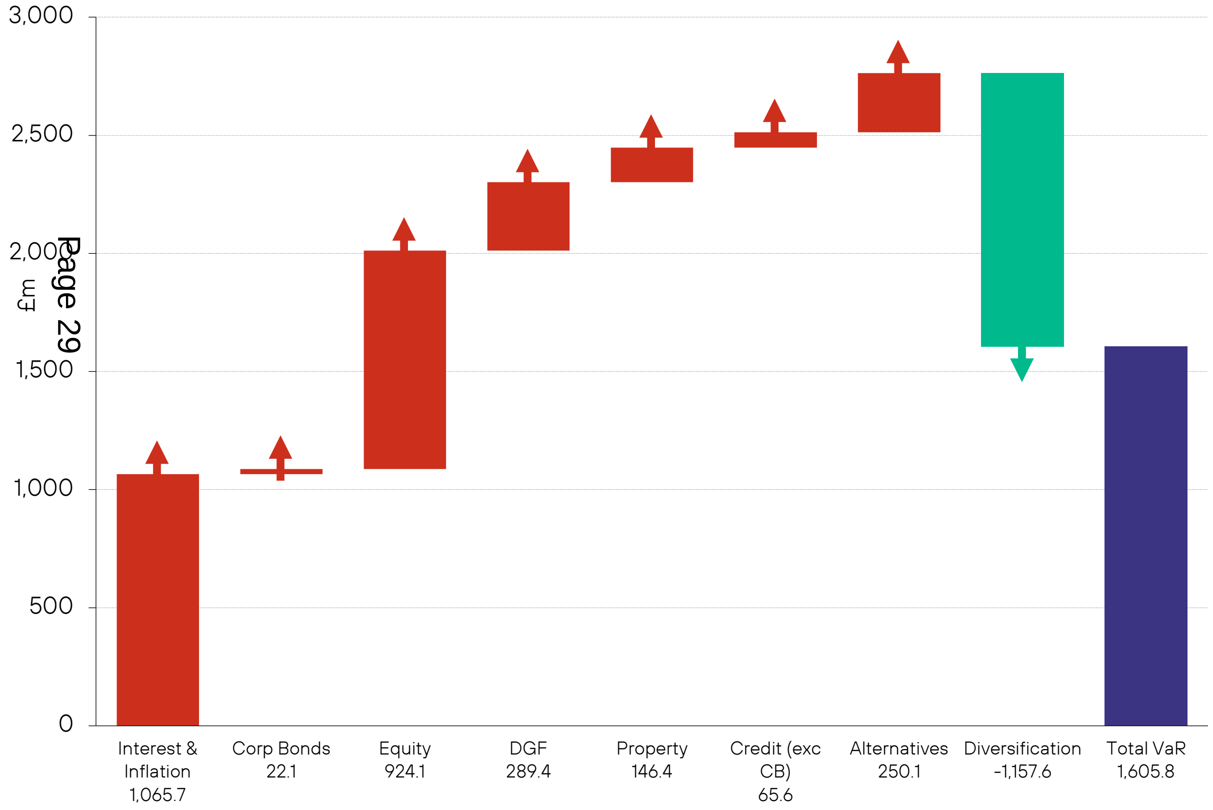
Source: Barnett Waddingham Robertson, Isio calculations. Notes: Start funding position has been assumed to be 107% as at 31 March 2021. This analysis assumes that there is no future funding strain for the Fund (i.e. the cost of future service accrual is broadly equal to future service contributions). This point has been confirmed by the Fund Actuary.

## Comments

- The central expectation is for the funding position to continue to improve and increase gradually over time due to investment returns along with employer and employee contributions.
- Based on the estimated 31 March 2021 position and median predicted outcome going forward, we expect the Fund to be in a surplus of c. £520m in 3 years' time (up from c. £280m at the end of March 2021).
- Ultimately any surplus could be used to bring down the future service cost of the Fund to the employers.
- The chart highlights the degree of variation (both upside and downside) that the Fund is exposed to by the current investment strategy. This volatility could have a material impact on the funding position and the future cash funding requirements.
- Given the current investment risk in the strategy, there is a 1 in 20 chance that a deficit of c.£1,082m or more could arise in 3 years' time – this would trigger a need for the deficit contribution rate to be paid in addition to the cost of future accrual.
- Given the current strong funding position, we believe there is scope to reduce investment risk and lessen the impact of any potential downside scenarios, essentially narrowing the range of potential outcomes.
- Reducing investment risk, and narrowing the range of potential return outcomes, would reduce the potential variability of contribution rates at future valuations. We believe this could be done with minimal impact to expected returns.

# Risk analysis

## Value at Risk (3 year, 95%) Breakdown - Strategic allocation



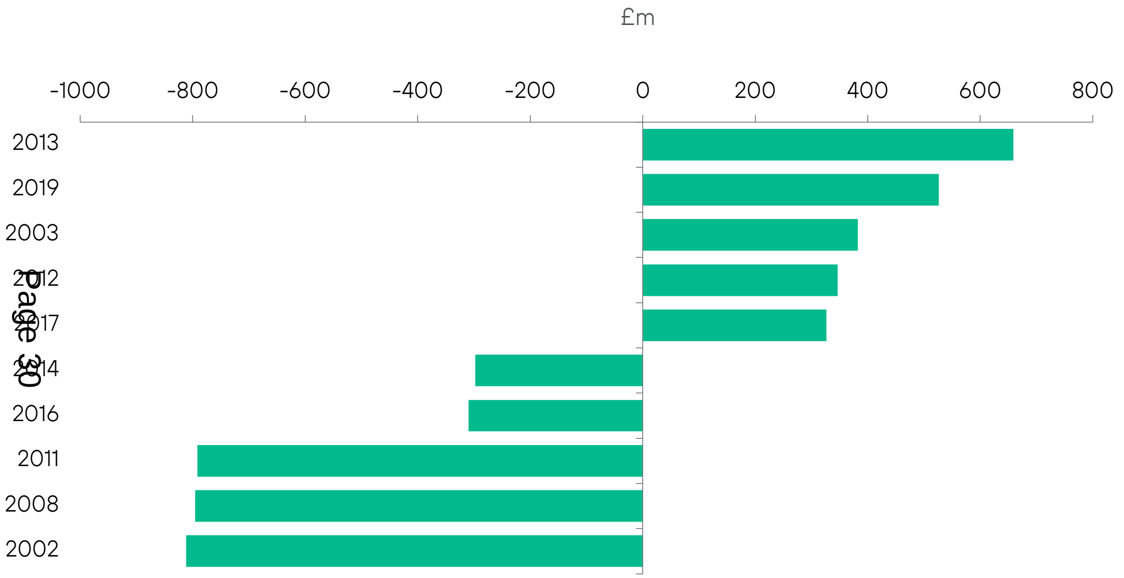

Source: Barnett Waddingham Robertson, Isio calculations. Notes: Start funding position has been assumed to be 107% as at 31 March 2021. This analysis assumes that there is no future funding strain for the Fund (i.e. the cost of future service accrual is broadly equal to future service contributions). This point has been confirmed by the Fund Actuary.

## Equity and Inflation are the Most Significant Risks

- The chart to the left illustrates the overall level, and composition of investment risk in the strategic asset allocation, as measured by the 1 in 20, 3 year Value at Risk ("VaR"). The VaR represents the difference in the funding in three years' time between the expected outcome and a 1 in 20 outcome.
- The total risk (3 year, 1 in 20 VaR) is c.£1.6bn, i.e. that there is a 1 in 20 chance that the Fund could be £1.6bn behind (or ahead) of the expected position in 3 years time.
- The Fund's key risks are equity exposure and the interest rates / inflation risk inherent within the value placed on the liabilities. The 40% strategic allocation to equities means that a fall in equity valuations would result in a material decrease in the Fund's assets (similar to that experienced over Q1 2020, although this was quickly reversed).
- The significant risk from inflation is due to the majority of the pension benefits in the Fund being directly linked to inflation. While the Fund's discount rate is not explicitly linked to interest rates, we assume that a change in long term interest rates will be reflected to some degree in a change in the expected future returns from the investment strategy, and consequently also in the Actuary's discount rate.
- We believe the Fund should be aware of these risks and consider how these are managed as part of any strategic changes. In particular, we believe it will be beneficial for the Fund to
  - Continue to increase the Fund's exposure to assets which provide a direct link to inflation;
  - Continue to focus on building exposure to assets with a more contractual payoff profile which offer diversification from listed equity within the growth portfolio. The Fund can also harvest an illiquidity premium for long term investment.

# Scenario analysis

### How Would the Strategy have Performed (Approximate) – 5 best and 5 worst years (2000-2020)



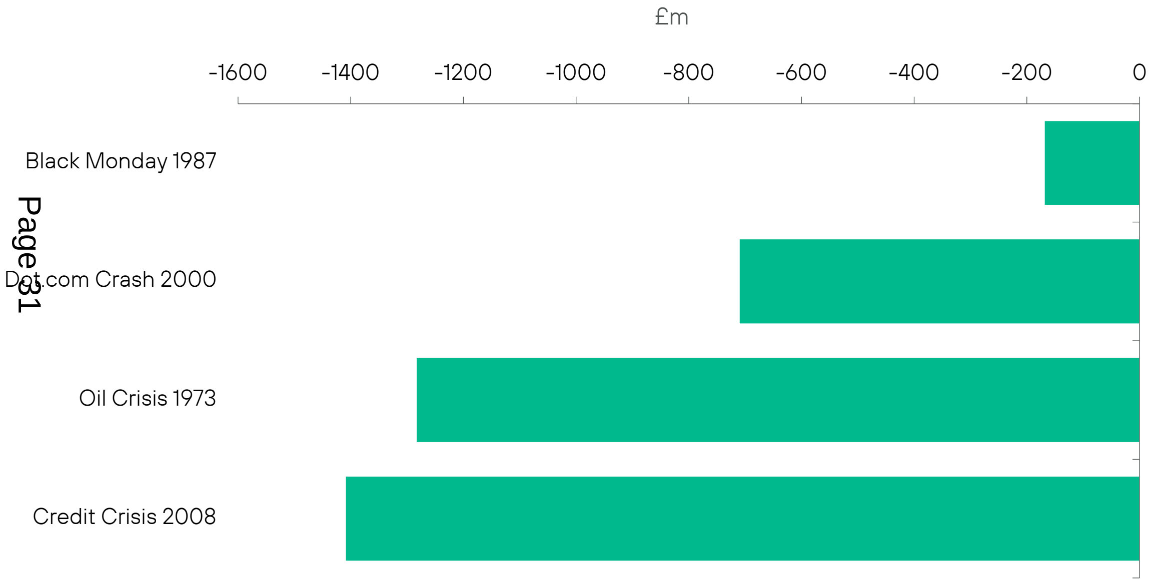

### Comments

- Based on the current strategic allocation and asset value, we illustrate the funding level of the Fund would have changed under the best and worst calendar years since 2000.
- The Fund's 1 year Value at Risk figure is around £950m (over 3 years this is £1.6bn, as illustrated on page 9) . This means we would expect a worsening of funding position relative to expectations of c. £950m roughly 1 in 20 years. The chart opposite illustrates how frequently such events have occurred in practice over recent history.
- There have been three calendar years during the last 20 in which the Fund's funding position would have worsened by around £800m.

Source: Barnett Waddingham Robertson, Isio calculations. Notes: Start funding position has been assumed to be 107% as at 31 March 2021.

# Scenario analysis

## How Would the Strategy have Performed (Approximate) – 4 crises

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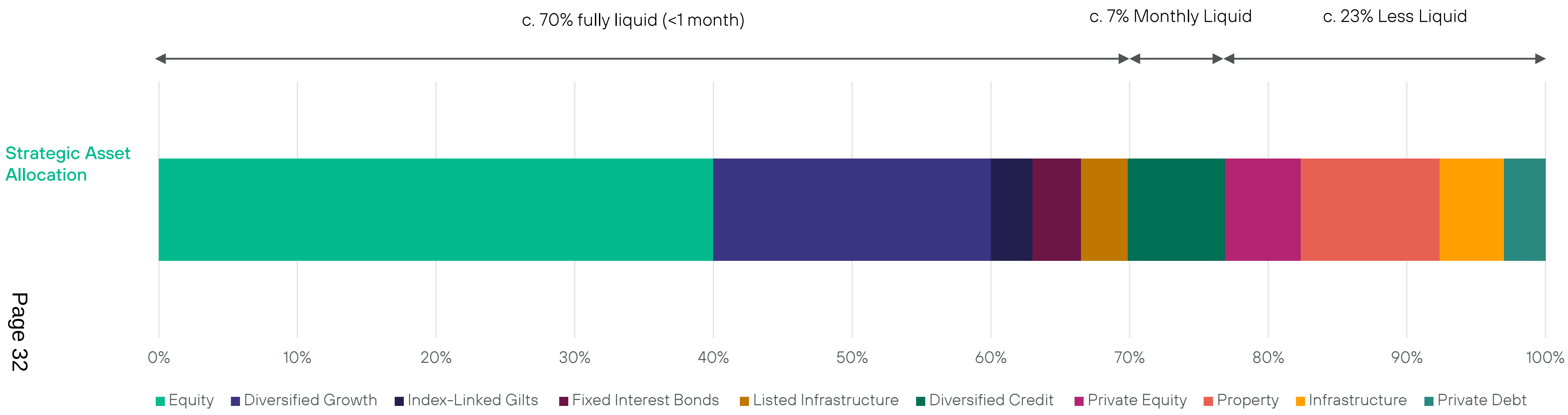
Source: Barnett Waddingham Robertson, Isio calculations. Notes: Start funding position has been assumed to be 107% as at 31 March 2021.

## Comments

- Based on the current strategic allocation and asset value, we illustrate the funding level of the Fund would have changed under four historical market stress scenarios. These measure the impact across each specific event:
  - During the 2008 credit crisis, equity markets fell c. 50%, credit spreads widened materially, and long dated interest rates fell. Such moves would materially impact the Fund, given its equity exposure, and relatively low interest rate protection. The impact of these moves would have been partially offset by a c.0.5% fall in long dated inflation expectations, which would push down the value placed on liabilities.
  - The Fund would have suffered a significant drawdown during the 1973 Oil Crisis, with a c. 42% fall in equity markets, and a drop in long dated interest rates damaging the overall funding level.
  - The 2000 Dot.com crash saw a c. 35% fall in equity markets, but limited other negative market impacts for pension funds. However, we would expect such an event to still have a material impact on the Fund, given the 40% equity allocation.
  - A repeat of 'Black Monday' would have a negative impact on funding level, albeit not to the same extent as the other scenarios considered. In this scenario, equity markets fell c. 10%, however long dated interest rates increased – pushing down the value placed on pension fund liabilities.
  - The scenarios suggest that the 1 in 20 risk illustrated previously (occurring over a three year period) is not unrealistic given the quantum that was observed during past market crises.

# Liquidity profile

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## Observations

- Based on the target strategic allocation, the asset strategy remains relatively liquid, with around 65% - 70% of assets able to be liquidated within a month and a significant proportion of these in a matter of days. The remaining assets are well diversified across a range of less liquid asset classes.
- Whilst the Fund is large, much of the portfolio could be liquidated relatively quickly with limited market impact. We cannot currently envisage any circumstances where the Fund would need this level of liquidity or flexibility.
- As a long-term investor, the Fund has the ability to tie-up capital in opportunities with lower liquidity where there are good risk adjusted returns available for doing so. We believe there is scope for the Fund to further increase the allocation to less liquid markets and to harvest a premium for longer term investment.
- We consider the shorter term cashflow requirements in more detail overleaf.

Source: Investment managers

# Cashflow profile

- The Fund is expected to have a number of cash outflows over the coming years. There are three core capital outflows:
  - Monthly pension payroll (which is fairly predictable);
  - Lump sum / death grant member payments (there is a degree of uncertainty over such benefits as they are more variable in nature);
  - Expenses such as manager fees, transaction costs and other miscellaneous charges.
- The Fund Actuary has shared details of the expected pension payments from the Fund. We note that these incorporate anticipated lump sum payments, but do not make any allowance for any transfers out of the Fund –we expect the overall magnitude of these to be negligible.
- The analysis in the table shows that the expected employer and employee contributions will largely offset the Fund's outgoings, though there is likely to be a small shortfall each year.
- This shortfall can be met using investment income form existing mandates
- Based on the current asset allocation, we expect that the Fund's illiquid mandates will produce enough income over the next 5 years to cover the small net negative cashflow. Further income can be drawn from the wider investment strategy if needed.
- The Fund also has more than sufficient liquidity to deal with any deviations in these amounts.
- We do not believe that there is a strong requirement to significantly increase the level of investment income within the strategy at this stage. However, we note that this may be a natural consequence of reducing the overall level of risk by focusing on mandates which deliver more of their returns via a more contractual payoff.

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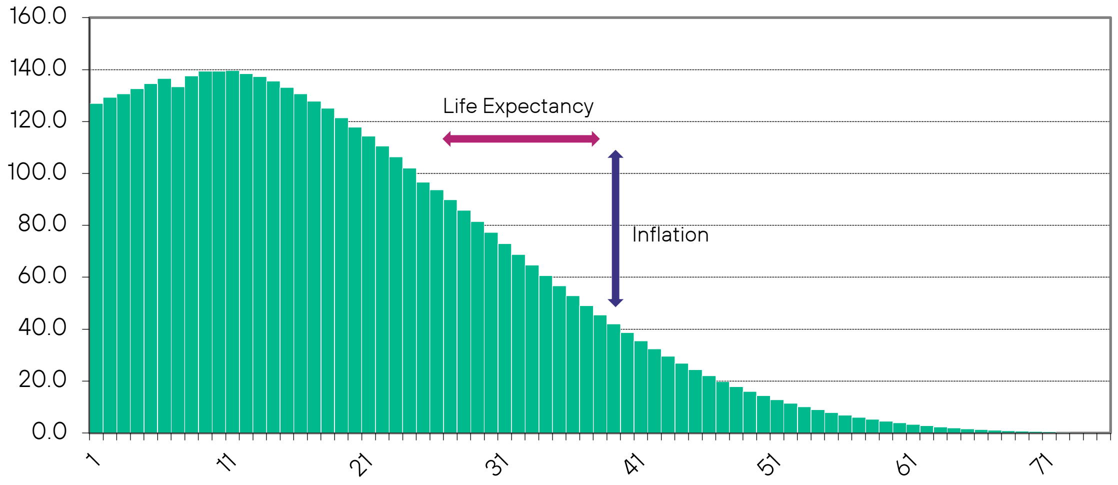
**Liability Profile**




| Cashflows (£m) | Year 1 | Year 2 | Year 3 | Year 4 | Year 5 |
|---|---|---|---|---|---|
| **Income** | **£120m** | **£124m** | **£127m** | **£131m** | **£135m** |
| Employer contributions | £92m | £95m | £98m | £101m | £104m |
| Employee contributions | £28m | £29m | £29m | £30m | £31m |
| **Outgo** | **(£129m)** | **(£136m)** | **(£141m)** | **(£148m)** | **(£155m)** |
| Pension Payments | (£129m) | (£136m) | (£141m) | (£148m) | (£155m) |
| **Net Cashflow** | **(£9m)** | **(£12m)** | **(£14m)** | **(£17m)** | **(£20m)** |

Source: Barnett Waddingham, Isio calculations, Investment managers.
For these purposes, contributions have been assumed to rise at 3% p.a.

# Direction of travel

# Proposed direction of travel

## Increase exposure to assets with direct inflation-linkage

Rising inflation is a key risk to the Fund given the liability structure, and increasing the allocation to assets with direct inflation linkage would help address this risk. e.g. infrastructure and long lease property.

## Increase exposure to less liquid assets

Given the Fund's long term horizon, and the overall level of liquidity in the current portfolio, there is scope to target less liquid opportunities e.g. private market debt, equity and infrastructure to a greater degree and earn an excess return for doing so.



## Increase alignment to Responsible Investment Policy

The Fund has made strong progress incorporating ESG considerations into its investment strategy and this is expected to remain a key focus going forward

## Pooling of assets

The regulatory environment directs the pooling of assets going forward. This will need to be considered in conjunction with setting investment strategy and implementation of decisions.

# Asset classes for consideration – inflation linked assets

## Infrastructure Equity

Investments into large scale public or private facilities that are essential for economic activity (e.g. energy, utilities, transport and more recently renewables) or provide societal benefits (hospitals, prisons, schools) that deliver long term contractual income and inflation protection.

There are two primary asset types: 'Brownfield' assets which are already in operation provide a reliable cashflow stream and are considered lower risk; 'Greenfield' assets are projects still in the development stage, and which are considered higher risk due to the exposure to construction risk.



| | |
|---|---|
| **Expected net return p.a.** | Gilts + 4.5% |
| **Volatility p.a.** | 12% |
| **Liquidity** | Varies – low for 8-10 year close ended funds; medium for open ended private asset funds; high for open ended public infrastructure funds |
| **Inflation linkage** | High |
| **ESG** | ESG impact possible at fund and asset level, with products available which target positive ESG outcomes (through investments in renewable energy, energy efficient projects etc). |

## Inflation-linked Property

Inflation-linked property encapsulates a range of types of property investment, all of which have the similar characteristic of the majority of returns expected to be delivered through rental income which is linked to inflation in some manner, rather than the capital appreciation of the underlying properties.

Certain funds invest in a diversified blend of UK commercial properties which are leased out to high quality tenants. In contrast to balanced property, these funds target very long-dated rental agreements typically including a regular uplift between cashflows and prevailing inflation.

Other funds focus on the residential property market in various guises, with stakes taken in the development and management of private residential accommodation, which in turn is used to generate rental income.

| | |
|---|---|
| **Expected net return p.a.** | Gilts + 2.5% - 3.0% |
| **Volatility p.a.** | 8% - 13% |
| **Liquidity** | Medium – typically quarterly following a lock in period |
| **Inflation linkage** | High |
| **ESG** | ESG impact of commercial property assessed on fund-by-fund basis, typically focussed on deal-specific due diligence. Residential funds can offer attractive ESG footprint. |

# Asset classes for consideration – private credit

## Private Corporate Debt

Private corporate debt involves providing finance (loans) in private markets, mainly to small to medium sized businesses. Investments are drawn down over a 3 year investment period.

Returns from the funds are generated from coupon payments, origination fees, as well as the principal repayment at the end of the loan, and provide pension schemes with a stream of contractual cashflows.



| | Unitranche | |
|---|---|---|
| | Senior | Junior |
| **Expected net return p.a.** | Gilts + 3% | Gilts + 5% |
| **Volatility p.a.** | 6-8% | 8-10%. |
| **Liquidity** | 5-8 year closed-end structure | |
| **Inflation linkage** | Low, floating rate | |
| **ESG** | ESG impact assessed on fund-by-fund basis, typically focussed on deal-specific due diligence. | |

## Commercial Real Estate Debt ('CRED')

CRED funds are comprised of a concentrated portfolio of loans, backed by commercial real estate (e.g. offices, hotels, shopping centres) which rank below other (senior) investors in the event of bankruptcy.

Historically, financing of CRED purchases was done almost entirely via commercial banks; however, they have increasingly withdrawn from this space since the financial crisis. As a result, institutional investors that can afford to lock up their capital for 8 10 years have the opportunity to fill in this gap and reduce their reliance on non contractual asset classes (e.g. equity) as primary return drivers. Unlike traditional property investments, the returns on CRE loans come in the form of coupon payments and origination and prepayment fees.

| | Unitranche | |
|---|---|---|
| | Senior | Junior |
| **Expected net return p.a.** | Gilts + 1.8% | Gilts +5% |
| **Volatility p.a.** | 6% | 14% |
| **Liquidity** | Low – typically 8-10 year close ended funds | |
| **Inflation linkage** | Low | |
| **ESG** | ESG impact assessed on fund-by-fund basis, typically focussed on tenant engagement. | |

# Alternative portfolios

Reduced

Increased

| | Current Strategic | Current Actual | Alt 1 *Evolution* |
|---|---|---|---|
| Global Equity | 40.0% | 42.2% | 40.0% |
| Diversified Growth | 20.0% | 23.7% | 17.0% |
| Private Equity | 5.5% | 6.3% | 5.5% |
| Balanced Property | 10.0% | 8.2% | 7.0% |
| Inflation-Linked Property | – | – | 4.0% |
| Infrastructure Equity | 8.0% | 4.4% | 11.0% |
| Private Credit | 3.0% | 1.0% | 5.0% |
| Diversified Credit | 7.0% | 6.7% | 10.5% |
| Corporate Bonds | 3.5% | 1.9% | – |
| Index-Linked Gilts | 3.0% | 3.0% | – |
| Cash | – | 0.8% | – |
| Expected return (% p.a.) | **5.3%** | **5.3%** | **5.5%** |
| VaR (3 yr, 1 in 20 chance) | **£1,606m** | **£1,673m** | **£1,608m** |
| Expected 3yr position (Surplus) | **£524m** | **£518m** | **£560m** |
| 3yr 1 in 20 downside position (Deficit) | **(£1,082m)** | **(£1,155m)** | **(£1,048m)** |
| % of assets with direct inflation linkage | **c. 11%** | **c. 7%** | **c. 15%** |

Source: Barnett Waddingham, Isio Calculations. Notes: Direct inflation linkage assumed to be 100% of inflation-linked property, 100% of infrastructure equity, 100% of infrastructure debt, and 100% of index-linked gilts. Start funding position has been assumed to be 107% as at 31 March 2021. This analysis assumes that there is no future funding strain for the Fund (i.e. the cost of future service accrual is broadly equal to future service contributions). This point has been confirmed by the Fund Actuary. Inflation-linked property has been modelled as 50% long lease property, 50% residential property. Private Credit is expected to be made up of a diversified portfolio of underlying risks. Alt 1 Private Credit is split: 3% CRED, 2% Private Corporate Debt.

# ESG considerations

| Consideration | Description | Comments |
|---|---|---|
| ESG impact and alignment with RI policy | • The Fund has a defined Responsible Investment Policy containing explicit ESG objectives. This statement outlines how the Fund's Pension Committee consider ESG factors through the investment decision making process and how these are implemented in the Fund's portfolio. | • The Fund has already made significant strides in improving the ESG profile of the investment strategy. The primary asset class when considering ESG sustainable or impact investing is equity, and the Fund's holdings reflect this, with 75% of the public equity exposure (30% of Fund assets) to be invested in sustainable or impact-focussed funds. The steps taken to evolve the Fund's equity portfolio have placed it at the forefront of the shift towards ESG investing, relative to many of its peers.<br>• In order to further the alignment with the Responsible Investment Policy, any new mandates under consideration should be reviewed fully from an ESG perspective prior to implementation – at both the asset class and manager level. We have outlined below how ESG considerations should be viewed in relation to the proposed strategic changes for the Fund:<br>1. Corporate Bonds switched to Diversified Credit – while current diversified credit funds are unlikely to have an explicit impact or sustainable focus (although M&G are due to launch one in late 2021), the greater flexibility within their investment process allows more scope for integration of ESG criteria, and therefore provides greater potential for managers to be able to differentiate themselves within the asset class through their ESG credentials. We note that the M&G corporate bond fund holds a consistently high fossil fuel allocation than the M&G Diversified Credit Fund.<br>2. Reductions in Index-Linked Gilts & Diversified Growth – both asset classes offer very limited scope to implement ESG beliefs at fund level; however DGF managers do have some flexibility to integrate ESG considerations at asset level.<br>3. Increase in Private Credit – there is limited scope to apply ESG considerations at fund level; however we believe the Committee should evaluate how well any potential new managers integrate ESG analysis into their 'bottom-up' deal level due diligence process e.g. some managers have begun to negotiate ESG specific covenants in their deals.<br>4. Increase in infrastructure Equity – infrastructure equity provides the Committee with significant scope to implement ESG considerations. There are infrastructure funds available which focus solely on renewable/sustainable projects; while all infrastructure funds have significant influence over the ESG footprint of projects at deal level.<br>5. Introduction of Inflation-Linked Property – this mandate is relatively flexible in terms of specific implementation method, covering multiple asset classes. If the Committee was to implement via long lease property, there is relatively little scope for fund level ESG integration; however we believe the Committee should evaluate how well any potential new managers integrate ESG analysis into their 'bottom-up' deal level due diligence process. Alternatively, the Committee could implement some form of residential/social housing mandate, which is likely to have explicit goals and targets around positive ESG impact. |

# Implementation considerations

| Consideration | Description | Comments |
|---|---|---|
| 1. Fund range currently available on the ACCESS Pool | • The Fund is required to move assets to the ACCESS Pool over time. As such the range of funds currently available on the ACCESS Pool should be considered in conjunction with setting investment strategy. | • The proposed alternative investment strategy outlined requires an increase in the Fund's allocations to Private Credit, Infrastructure Equity, Inflation-Linked Property and Diversified Credit.<br>• The ACCESS pool currently offers a range of funds for investment in Diversified Credit and we propose these should be considered as a route of implementing the increased holding in this asset class, with a view to finding a mandate which compliments the Fund's current exposure with M&G.<br>• The ACCESS pool does not currently offer funds in Private Credit, Infrastructure Equity or Inflation-Linked Property. As such, alongside a discussion with ACCESS in relation to their intentions in this area, we propose alternative methods of implementation for these allocations are considered. |
| 2. Anticipated timescales for future fund launches | • The Fund is required to move assets to the ACCESS Pool over time. As such future fund launches from the ACCESS Pool and the timescales associated with these should considered in conjunction with setting investment strategy. | • The ACCESS pool does not currently offer funds in Private Credit, Infrastructure Equity or Inflation-Linked Property.<br>• ACCESS have communicated that they intend to make offerings available for investment by pool members in each of these areas in due course, and this will be done in priority order. The order and time scales for the fund launches remains uncertain and this continues to be discussed with ACCESS.<br>• ACCESS are currently in the process of appointing an implementation advisor whose mandate will be to advise on these fund launches. |

# Additional considerations (1)

| Consideration | Description | Comments |
|---|---|---|
| **1. Realigning the illiquid mandates with the strategic benchmark** | • The Fund's allocations to property, infrastructure and private credit are underweight relative to their respective strategic targets. | • The Fund's infrastructure holdings vary in terms of their stage in the lifecycle, with some fully drawn and distributing, and others still to draw the majority of their commitments. In our recent paper, we recommended that the Fund consider making an allocation to an open-ended infrastructure fund, as well as consider allocating £30m to a renewables-specific fund (which would look to develop new infrastructure assets) whilst maintaining an exposure to liquid infrastructure via Atlas, recognising the diversification benefit and the time taken to deploy the new mandates. The proposed increase in the allocation would mean that the Atlas allocation can be maintained and other opportunities could be explored.<br>• The majority of the Fund's commitment to the M&G commercial real estate debt fund has already been called. We previously rated M&G highly (green on a traffic light scale), but in the light of recent significant departures from the team, we have downgraded this proposition to amber. We believe the Council should make additional commitments to the asset class in order to increase the allocation towards benchmark, even if the strategic allocation is not increased as proposed in this report. Should the Fund's allocation be topped up, we would be happy to provide guidance around suitable managers.<br>• Consideration should also be given to the balanced property mandate. This is currently 8% of total Fund assets, and is underweight relative to the 10% target. We believe other sub asset classes, including long lease property and residential, are more attractive strategically due to their inflation protection and the strong match for the Fund's liability profile this provides. |
| **2. Restructuring the private and diversified credit holdings** | • The proposed new strategy incorporates new allocations to private credit and diversified credit. | • Should the Committee decide to increase the strategic allocation to private credit, we believe the Committee could consider diversifying the private credit exposure by introducing private corporate debt to the existing real estate debt exposure.<br>• Should the diversified credit allocation be increased, we believe there is scope to diversify the manager-specific risk by adding another provider. The Committee could also consider introducing a daily traded fund, if concerned about liquidity. |
| **3. Stress scenario liquidity availability** | • The Officers have previously undertaken analysis to estimate the level of immediate liquidity which could be required by the Fund in a worst case scenario | • Historical analysis indicates that in a worst case scenario the Fund may be cashflow negative of the order of £10-£20mln over an annual period.<br>• In this circumstance there may be a requirement to source this amount via disinvestment from the asset portfolio. The scenario outlined will likely result in stressed asset prices and as such the Fund has expressed an preference to hold a small allocation to liquid assets which they would expect to perform in a stable manner in this environment and facilitate efficient disinvestment. Historically the Fund has looked to the holding in Index-linked Gilts for this.<br>• We believe considering a daily liquid Diversified Credit Fund (considering the range of Funds available on the ACCESS Pool) would be appropriate for this allocation under the newly proposed strategy. |

# Additional considerations (2)

| Consideration | Description | Comments |
| --- | --- | --- |
| 4. Overall Fund Governance | • The Fund currently has investments with 13 different managers. | • Across the 13 managers, the Fund has investments in 19 individual mandates.<br>• Any restructuring of the Fund's assets should be done with a view to minimising any increase to the number or complexity of existing investment arrangements, to avoid further increasing the overall governance burden. Any decisions around new mandates should give consideration to the availability of funds on the ACCESS pool and the regulatory directive to transfer assets on pool. |
| 5. Transaction Costs | • There are often explicit transition costs associated with the movement of assets. | • The round trip transaction costs of any movement in assets should be considered ahead of implementation. While we do not anticipate that the majority of the asset class changes proposed would incur transition costs, we do note that the sale of public credit assets is likely to incur a spread cost of up to 0.5%, while the purchase of property assets will incur trade costs of up to 5%. |

# Summary and Next Steps

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# Summary and next steps

## Summary

- The Fund has delivered strong investment returns in recent years during a period in which most asset markets have trended upwards, with the equity exposure being particularly beneficial. This performance has led to a surplus, of c. £280m as at 31 March 2021.
- Whilst equity risk remains one of the Fund's biggest risks, we believe that the Fund should maintain its existing strategic allocation to equities as a long term driver of overall return, and focus on increasing allocations to assets with direct inflation exposure, to help address the risk of rising inflation, and also less liquid assets to allow the fund to target a premium for being able to tie up its capital.
- We recommend the Fund seeks to continue building out the real assets portfolio, with a particular focus on opportunities within infrastructure. This would serve not only to increase the portion of Fund assets' with direct inflation exposure, helping to address a significant risk facing the Fund, but could also be implemented to further demonstrate the Fund's commitment to sustainable investments. Alongside this, we believe the Fund could consider introducing exposure to property assets with a direct inflation linked income stream to further increase the inflation protection.
- We recommend that the Fund's allocation to corporate bonds is switched into diversified credit, which exhibits a more attractive risk/return profile (as a result of its wider opportunity set and active management).
- We believe that further commitments to commercial real estate debt and private debt more broadly should be considered, in order to harvest the premium available and to broaden the Funds private debt exposure.

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## Next Steps

- The Committee should consider its views on:
  - addressing the strategically underweight allocations to commercial real estate debt and infrastructure.
  - the strategic proposal put forward for the infrastructure, commercial real estate debt, and diversified credit holdings.
  - whether there is appetite to adopt the alternative portfolio outlined in this paper.
- We look forward to discussing this report at the upcoming meeting.

# Appendices



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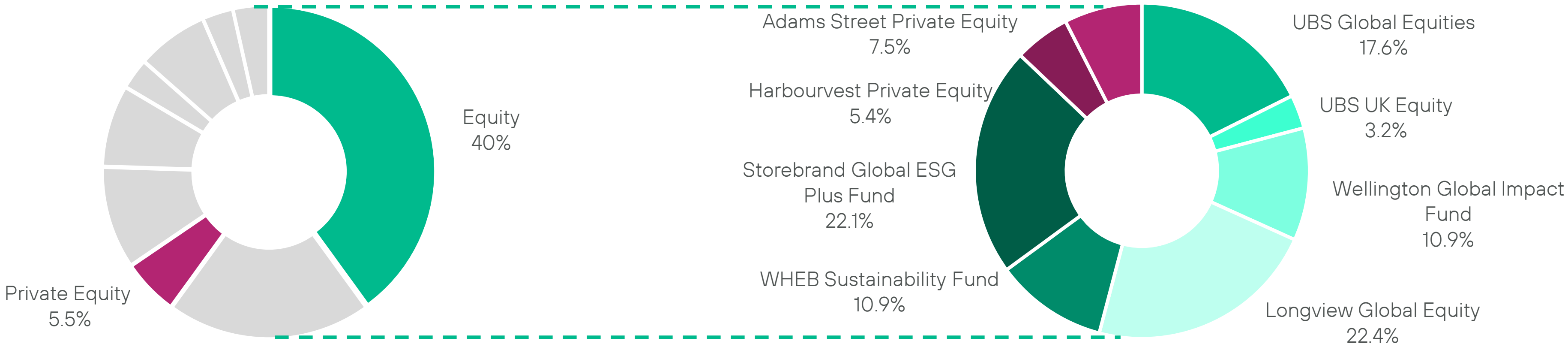
# A1: Equity portfolio

Strategic Equity Weight

Equity Portfolio As At 31 March 2021

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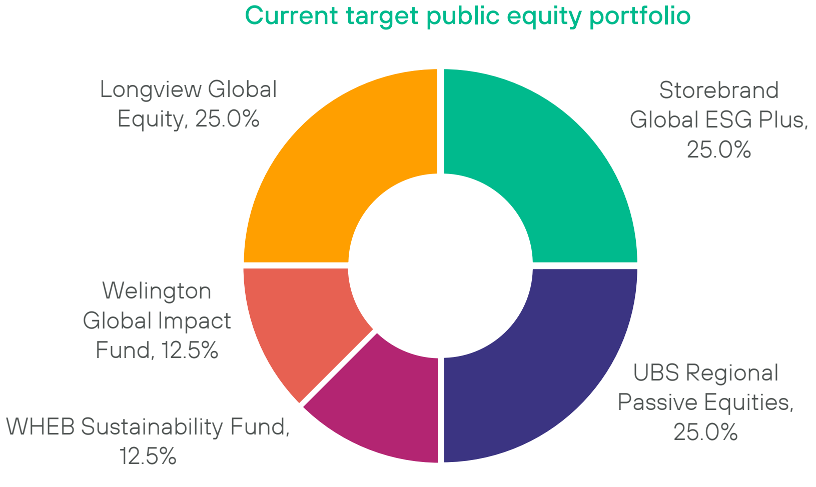
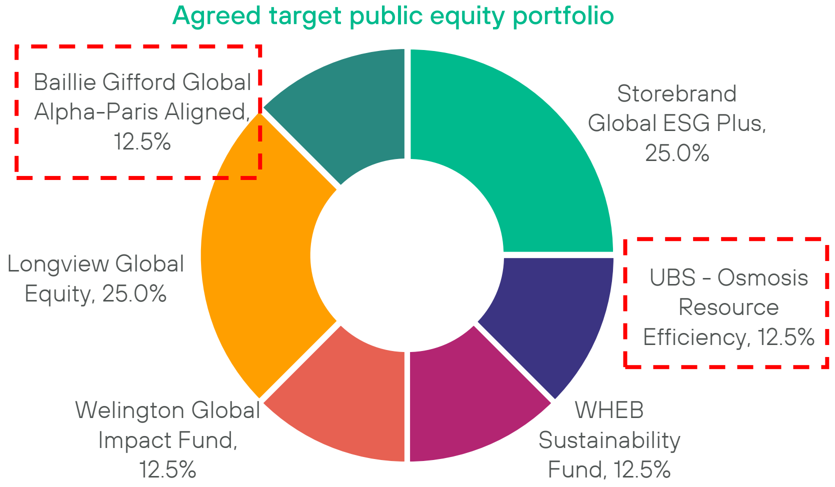
| Manager | Mandate | Geography | Management Style | Description |
|---|---|---|---|---|
| UBS | Public Equity | Global | Passively managed | The UBS regional passive equity portfolio tracks the relevant index for each underlying fund and has a tilt towards companies with a large market capitalisation. The UBS portfolio currently comprises regional allocations to global markets, but has an underweight to the US and an overweight to Europe (including the UK) compared to the market cap index. Overall the allocation is low-cost. |
| Wellington | Public Equity | Global | Active: Impact / Growth | The Wellington Global Impact Fund looks to generate long term returns while addressing major social & environmental challenges. The Fund has a bias towards mid-cap companies within the UK and Europe and a slight inherent growth tilt given the way the manager constructs the portfolio. The Fund has the highest annual management charge of the equity funds. |
| Longview | Public Equity | Global | Active Growth at reasonable price | The LF ACCESS Global Equity Fund (Longview)objective is to outperform the MSCI benchmark by 3.0% gross of fees over 3 year rolling periods. The Fund is comprised of predominately large cap firms (greater than £5bn) and has a strong bias to US stocks. |
| WHEB | Public Equity | Global | Active: Sustainable / Growth at reasonable price | The WHEB Sustainability Fund looks to generate long term returns while advancing sustainability and prosperity. The Fund is comprised of mid cap stocks and exhibits some bias to the UK and Europe compared to the benchmark, as well as a slight growth style tilt. |
| Storebrand | Public Equity | Global | Passive: Sustainable Smart Beta | The Storebrand Global ESG Plus Fund tracks a benchmark with significantly reduced climate risk, excluding fossil fuels and climate negative stocks. The Fund is comprised of 95% large cap stocks and exhibits some bias to the UK and Europe. |
| HarbourVest | Private Equity | Global | Diversified by Style & Access Method | The HarbourVest private equity portfolio is comprised of a range of exposures, with the majority being primary and secondary fund-of-funds and a bias towards buyout relative to venture capital holdings. The portfolio is currently c. 75% drawn down. |
| Adams Street | Private Equity | Global | Diversified by Style & Access Method | The Adams Street private equity portfolio is comprised of a range of exposures, with the majority being primary and secondary fund-of-funds and a bias towards buyout relative to venture capital holdings. The portfolio is largely invested in the US and Western Europe. The portfolio is currently c. 75% drawn down. |



Source: Investment managers

# A1: Equity portfolio - evolution

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| Agreed Change | Comments |
|---|---|
| Public Equity: UBS passive equity exposure to be switched into a combination of the Osmosis Resource Efficient (Ex Fossil Fuel) Core Fund, and the Baillie Gifford Global Alpha Paris Aligned Fund. | The Fund currently holds c. 25% of its public equity portfolio in passive UBS funds. It has been agreed that this will be fully divested, with the proceeds to be split between a segregated mandate run by UBS which tracks the Osmosis Resource Efficient Core Equity (ex Fossil Fuels Index, and the LF ACCESS Global Alpha–Paris Aligned Fund.<br><br>The first of the two new mandates, run by UBS using portfolio constructions rules provided by Osmosis, will provide the Fund with a portfolio which has a significantly lower water and energy usage, as well as waste production, relative to the global passive benchmark. Osmosis' philosophy is that by holding a portfolio of 'resource efficient' companies, constructed in a risk-controlled manner, the Fund can achieve both excess risk-adjusted returns, and a more attractive ESG footprint relative to passive global equities. The Fund has opted for the variant of the Fund which excludes fossil fuels.<br><br>The second new mandate is comprised of an allocation to one of the ACCESS pool's active core equity funds (expected to be available on the platform in June or July). The underlying fund is managed by Baillie Gifford, an active growth equity manager with an extremely strong track record of outperformance. The fund itself will be based on one of the manager's flagship products, the Global Alpha Fund, with several quantitative and qualitative screens applies within the process to improve the ESG footprint of the portfolio.<br><br>Alongside the existing exposure to ESG-focussed funds operated by Wellington, Storebrand and WHEB, these new allocations will serve to increase the magnitude of the positive ESG tilts within the Fund's portfolio. These moves are in line with the Fund's ESG principles. |
| Private Equity: Further allocations to be made to the existing managers, to maintain the Fund's allocation around the strategic target. | The Fund has made new allocations to the Fund's two existing private equity managers, Adams Street and HarbourVest, with the intention of maintaining the allocation as close to the strategic target of 5.5% as possible over the medium term. |

Source: Investment managers

# A1: Diversified growth portfolio

**Strategic Diversified Growth Weight** | **Diversified Growth Portfolio As At 31 March 2021**


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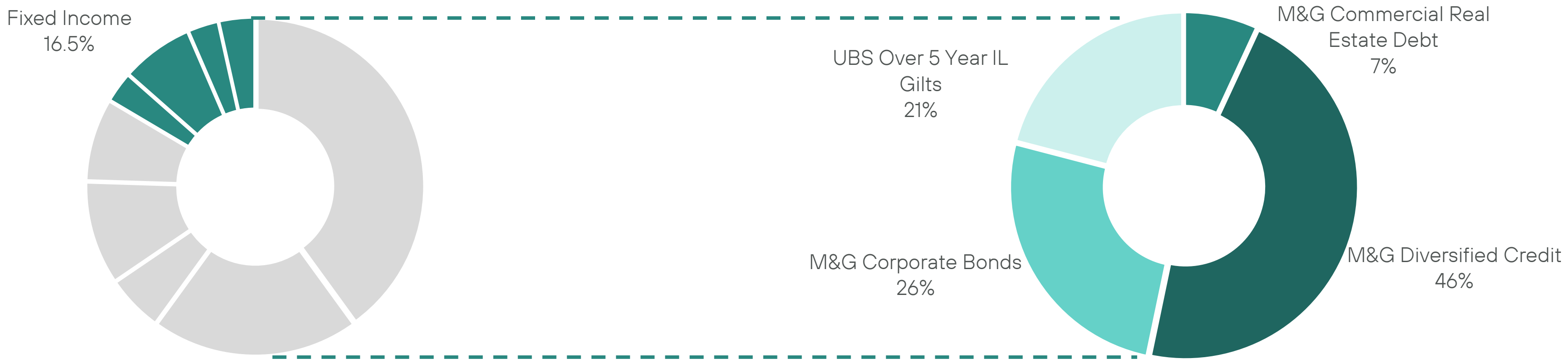
| Manager | Mandate | Geography | Management Style | Description |
|---|---|---|---|---|
| Newton | Diversified Growth | Global | Active | The Newton diversified growth fund has a relatively simple investment style, with an investment universe of largely equities and bonds (and limited alternatives exposure). The tilts of the equity holdings are largely determined by the wider Newton views (the organisation is a strong active equity manager). |
| Ruffer | Diversified Growth | Global | Active | The Ruffer diversified growth fund has a much clearer focus on capital preservation than the majority of its peers. Similar to Newton, the fund has a relatively traditional investment universe, with a significant focus on equities and bonds (both fixed interest and inflation linked). The fund is heavily reliant on active manager skill, with the investment process incorporating relatively high conviction, concentrated positions relative to other managers. The approach is quite unique and has enabled the fund to successfully navigate a wide range of different market environments. |

Source: Investment managers

# A1: Fixed income portfolio

**Strategic Fixed Income Weight** | **Fixed Income Portfolio As At 31 March 2021**

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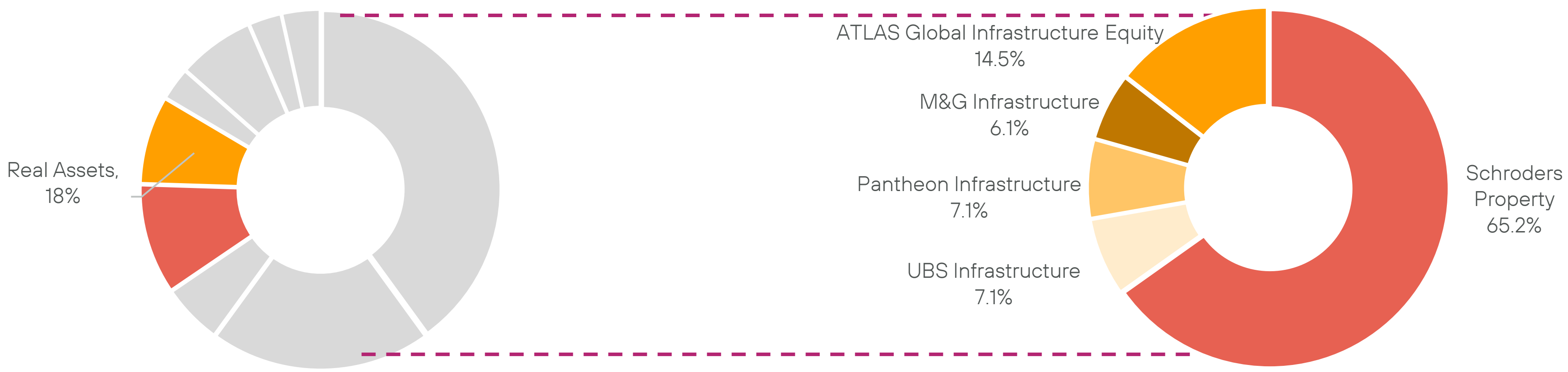
| Manager | Mandate | Geography | Management Style | Description |
|---|---|---|---|---|
| UBS | Index-Linked Gilts | UK | Passive | The UBS Over 5 Year Index-Linked Gilts Fund is comprised of UK government bonds with 100% of the portfolio linked to inflation. The UK Government is currently rated AA in terms of its credit rating. The Fund looks to match the FTSE Index Linked Gilts Over 5 Years index and is the cheapest mandate in the fixed income portfolio. |
| M&G | Corporate Bonds | Global: UK focus (63%), USA (12%), Europe (18%) & Other (7%) | Active | The M&G LF Access Sterling Corporate Bond Fund is a 'fund of one' with the East Sussex Pension Fund as the only investor. The Fund aims to outperform the composite investment grade corporate bond benchmark by 0.5% p.a.. The portfolio is comprised of mostly investment grade credit with a maximum of 10% of assets permitted in sub-investment grade. |
| | Diversified Credit | Global: Predominately Europe (65%), USA (11%), UK (23%) & Other (1%) | Active | The M&G Alpha Opportunities Fund invests in a range of credit assets, allocating across sub asset classes where the manager sees value, and targets a return of Libor plus 2.6% to 4.6% p.a. The Fund retains an average credit rating of investment grade quality. The Fund deals monthly and is therefore has slightly lower liquidity. |
| | Commercial Real Estate Debt ('CRED') | Global: UK focus (64%), Europe (28%), USA (8%) | Active | The M&G Real Estate Debt Fund VI is a closed-ended mandate with a net projected IRR of 4.5%, The scheduled maturity date is 20 December 2027 and the current investments are split between investment grade and sub-investment grade credit and focus solely on private market real estate debt lending. The M&G mandate is the least liquid in the fixed income portfolio and provides the opportunity for the manager to harvest a premium for longer term investment. |

Source: Investment managers

# A1: Real assets portfolio

**Strategic Real Assets Weight** | **Real Assets Portfolio As At 31 March 2021**




| Manager | Mandate | Geography | Strategy | Description |
|---|---|---|---|---|
| UBS | Infrastructure | Developed Europe, North America & Australia | Core/Core Plus | The UBS infrastructure portfolio consists of two funds (AIIF I and AIIF III), the AIIF III Fund is the most recent vintage and is due to hold a final close in Q1 2022. The AIIF I Fund is fully deployed and expects to distribute capital and wind down by 2025. Both funds focus on similar geographical regions and sectors, including energy, utilities, transport and telecoms. AIIF III has a greater sustainability focus than AIIF I. |
| Pantheon | Infrastructure | Predominately Europe, North America & APAC | Core/Core Plus | The Pantheon infrastructure portfolio is currently drawing down capital and is due to be fully deployed in 1 - 2 years. The portfolio is split broadly 50/50 between secondaries and co-investments. Secondaries investments are the purchase of existing stakes in infrastructure funds, typically at a discount to NAV, from other limited partners. Co-investments are the taking direct stakes in companies or projects, alongside other large investors. The investments are comprised of broad sector exposure including digital infrastructure, renewables and energy efficiency, transport, power and utilities, and energy infrastructure. |
| M&G | Infrastructure | Europe | Greenfield & Brownfield Core/Core Plus | The M&G portfolio is comprised of two funds (M&G Greenfield II and M&G Brownfield III) both of which are currently drawing down capital. The Greenfield II Fund has a longer timeframe to full deployment (3-4 years) compared to the Brownfield III Fund (1 year). Both Funds target similar sector e.g. fibre, transport and energy sectors. |
| ATLAS | Listed Infrastructure | Global (Developed Markets only) | Core/Core Plus | In contrast to the other infrastructure allocations, the Atlas Global Infrastructure Equity Fund is open-ended (i.e. investors can buy in and out at any time, and the Fund's structure is evergreen) and invests in publicly listed infrastructure companies. This differs from the other infrastructure exposure, which is largely private companies/projects, accessed via closed –ended fund structures (i.e. investors' capital is locked up for a 6-10 year fund lifecycle, and paid back as investments are realised). The Fund is fully invested in sectors such as transport infrastructure, utilities and renewables.. |
| Schroders | Balanced Property | UK | Core/Value Add | The Schroders fund utilises a 'fund-of'-funds' structure to access property markets, with c. 25% of the fund invested in closed-ended exposure, and the remainder in open ended funds. The Fund is overweight to the industrials sector and underweight to retail and London offices relative to benchmark, however it retains relatively significant Retail and Office exposure on an absolute basis. The fund-of-funds structure is a relatively expensive way to access property markets, given it introduces a second layer of fees (management fee in addition to underlying manager fees); albeit it does provide additional diversification versus a standalone property fund. Although the focus of the mandate is investing in commercial real estate equity the manager has requested flexibility for debt investment. |

Source: Investment managers

# A2: Value at Risk – an explanation

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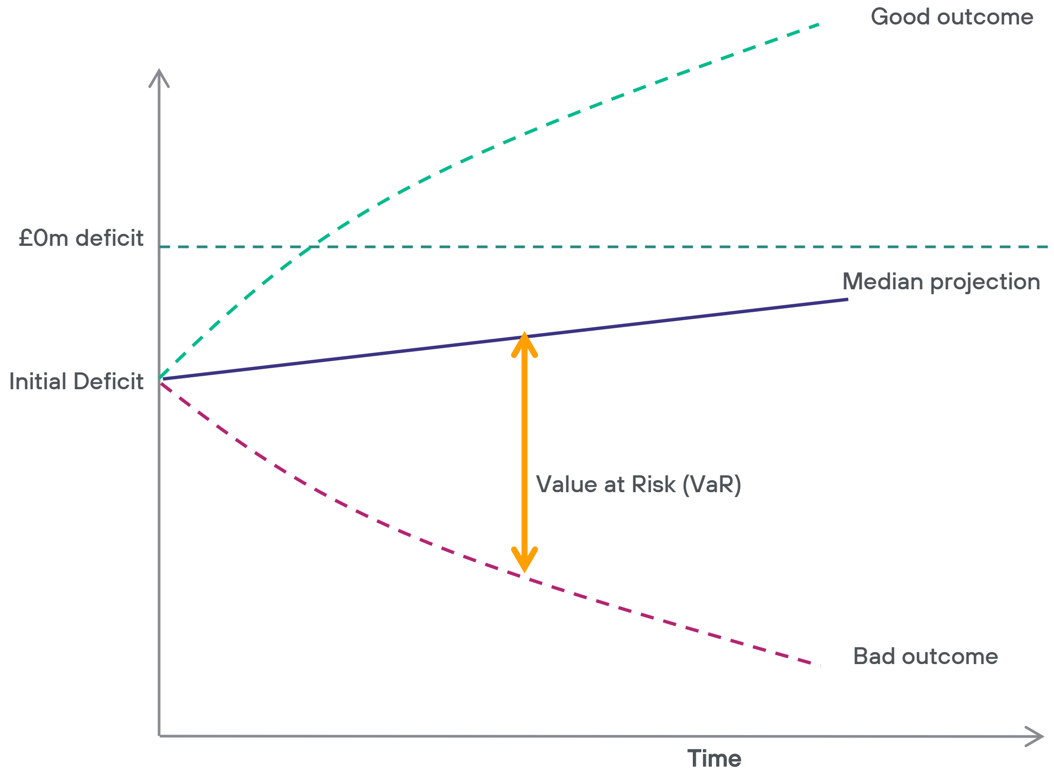
### Value at Risk ("VaR")

- The 1 in 20 value at risk is the difference between the 5th percentile outcome and the expected (median) outcome. The VaR measure gives a sense of how much better or worse the funding position could be relative to the central expectation for different market conditions. This is important when comparing investment strategies and setting contribution rates.




Note: the above chart is for illustrative purposes only.

# A3: Return and volatility assumptions (1)

## Introduction to the Assumptions

- These are our "best estimate" asset class return, volatility and correlation assumptions. We believe there is a 50:50 chance that the actual outcome will be above/below our assumptions.
- The assumptions are long-term, for a 10-year period, expressed in Sterling terms.
- Return assumptions are:
  - Annualised (i.e. geometric averages), rounded to the nearest 0.1%.
  - Expressed relative to the yield on fixed interest gilts (the annual yield at the 10-year tenor on the Bank of England spot curve). This yield was 0.2% at 31 December 2020.
  - Net of management fees.
  - Before tax. UK pension schemes are exempt from tax on investments. The impact of taxation may reduce returns for other investors.
- Volatility assumptions are based on the standard deviation of annual returns over a 10-year period, rounded to the nearest 0.5%.
- Bond volatilities are sensitive to the duration of the index. Our Fixed Interest Gilts (FIG) and Index-Linked Gilts (ILG) assumptions both relate to Over 15 Year indices, but the cashflow profile of the ILG index is considerably longer than the FIG index. Hence the difference in volatilities does not necessarily mean that real yields are assumed to be more volatile than fixed yields.
- Correlation assumptions are based on the correlation of annual returns over a 10-year period, rounded to the nearest 5%.

## Limitations and Risk Warnings

- There can be no guarantee that any particular asset class or investment manager will behave in accordance with the assumptions.
- The assumption setting process is subjective and based on qualitative assessments rather than a wholly quantitative process. Newer asset classes can be harder to calibrate due to the lack of a long-term history. Some asset classes may rely on active management to help deliver the assumed return. The returns on illiquid assets may vary by vintage; in these cases the quoted return expectation is necessarily an estimate encompassing multiple vintages.
- Where these assumptions are used within asset-liability modelling, please note that the model's projections are sensitive to the econometric assumptions. Changes to the assumptions can have a material impact upon the modelling output

# A3: Return and volatility assumptions (2)



| Asset Class | Sector [1] | Return [2] | Volatility [3] |
|---|---|---|---|
| Equity | Developed Markets – Passive | 4.0% | 20.0% |
| | Developed Markets – Core Active | 4.5% | 20.5% |
| | Global Unconstrained | 5.0% | 21.0% |
| | Developed – SmallCap Passive | 4.6% | 24.0% |
| | Emerging Markets – Passive | 5.0% | 28.0% |
| Property | UK Balanced Property | 2.3% | 13.0% |
| | Long Lease Property | 2.5% | 8.0% |
| | Private Rented Sector | 3.0% | 13.0% |
| | Global Property Secondaries | 6.0% | 30.0% |
| Hedge Funds | Multi-Strategy Fund of Funds | 2.5% | 10.0% |
| | Global Macro | 3.0% | 13.0% |
| DGF | DGF (lower risk) [5] | 2.8% | 10.0% |
| | DGF (higher risk) [5] | 3.5% | 12.5% |
| Alternatives | Private Equity | 6.5% | 30.0% |
| | Diversified Alternatives | 6.0% | 22.0% |
| | Infrastructure Equity | 4.6% | 12.0% |

Notes:
Please refer to full explanations and caveats on previous pages.
[1] Includes active management except where specified as passive.
[2] Expected return per annum, net of fees, relative to the yield on fixed-interest gilts.
[3] Expected standard deviation of absolute annual returns.
[4] Includes allowances for downgrades and defaults.
[5] "Lower risk" and "higher risk" are relative descriptions within the asset category only, with no wider meaning.
Source: Isio

| Asset Class | Sector [1] | Return [2] | Volatility [3] |
|---|---|---|---|
| Credit [4] | Corp. Bonds (IG All-Stk) – Passive | 0.6% | 7.0% |
| | Corp. Bonds (IG All-Stk) – Active | 0.9% | 7.0% |
| | Corp. Bonds (IG >15y) – Passive | 0.6% | 9.0% |
| | Corp. Bonds (IG >15y) – Active | 0.9% | 9.0% |
| | Absolute Return Bonds | 1.3% | 4.0% |
| | Asset-Backed Securities (IG) | 1.7% | 5.0% |
| | CLO | 2.5% | 9.0% |
| | Direct Lending | 4.2% | 10.5% |
| | Distressed Debt | 7.0% | 16.0% |
| | Diversified Private Credit | 4.2% | 10.0% |
| | Infrastructure Debt – Senior | 2.0% | 6.0% |
| | Infrastructure Debt – Junior | 3.3% | 9.5% |
| | Multi-Asset Credit (higher risk) [5] | 3.3% | 9.5% |
| | Multi-Asset Credit (lower risk) [5] | 2.6% | 6.5% |
| | Real Estate Debt – Senior | 1.8% | 6.0% |
| | Real Estate Debt – Junior | 5.0% | 14.0% |
| | Real Estate Debt – Whole Loan | 3.5% | 9.0% |
| | Secured Finance | 3.0% | 8.0% |
| | Semi-Liquid Credit | 3.5% | 9.0% |
| Gilts | Fixed Int. Gilts (>15y) – Passive | 0.0% | 8.0% |
| | Index-Linked Gilts (>15y) – Passive | 0.0% | 11.5% |
| Cash | Cash | 0.0% | 1.0% |

# A4: Modelling methodology (1)

## Data and Sources

- Information on characteristics of the Fund's liability profile, including the split between membership types, was taken from information provided by Hymans Robertson in relation to the 31 March 2020 actuarial valuation initial results.

## Modelling Principles

- SOFIA is a stochastic model that simulates a large number of possible future economic outcomes, in which financial conditions develop in a number of different ways, defined by assumptions for average outcomes, range of variability, and inter-dependency between different markets.
- The high-level market scenarios are generated by a third-party Economic Scenario Generator (ESG) provided by Moody's Analytics. The ESG is an industry-standard tool that is widely used by financial institutions (e.g. insurers, asset managers, and investment banks).
- Based on the scenarios generated by the ESG, SOFIA simulates asset-class returns calibrated to Isio's asset-class assumptions.
- SOFIA takes the initial starting position of the assets and the liabilities, and projects these values forward under the simulated scenarios, taking into account any relevant inflows and outflows.
- Different investment strategies are modelled in order to illustrate the effects of different allocations. In each case, SOFIA assumes that the strategy remains constant over the full projection period. Assets are annually rebalanced back to the original allocations.

## Modelling Results

- The results of the projections are shown by ranking the calculated results from best to worst in each year, and presenting the following outcomes:
- Median: this is the middle outcome and can be thought of as the "expected result". Half of the modelled outcomes are better than this and half are worse.
- Bad: this splits the results so that there is a one in five (20%) chance of having a worse outcome. This is a measure of risk.
- Very Bad: this splits the results at a one in twenty (5%) chance of having a worse result. This is a more extreme measure of downside risk.
- Good and Very Good (where shown): these illustrate possible positive outcomes at the 20% and 5% levels respectively.
- The "Value at Risk", where shown, is defined as the difference between the Median outcome and the Very Bad outcome, i.e. it represents the variability of funding outcomes and shows the magnitude of the possible downside from the expected result. Please note that this is not the same as the possible downside loss from the starting position.

# A4: Modelling methodology (2)

### Compliance Statement

- This report, and the work relating to it, complies with "Technical Actuarial Standard 100: Principles for Technical Actuarial Work" ("TAS 100").
- This report has been prepared for the purpose of assisting the addressee in their review of the investment strategy. If you intend to use it for any other purpose or make any other decisions after considering this report, please inform Isio and we will consider what further information or work is needed to assist you in making those decisions.

### Material Assumptions

- Isio's central asset-class assumptions are assessed and revised at each calendar quarter-end. The assumptions used within this modelling exercise are set out in the Appendix.
- Certain assumptions are sourced directly from the Moody's Analytics ESG and available market data, or set via adjustments to these sources. Where required or deemed to be more appropriate, assumptions are entirely determined by Isio. The assumption setting process is subjective and based on qualitative assessments rather than a wholly quantitative process. Where judgement is required, input is received from Isio's internal asset-class research teams.



### Limitations and Risk Warnings

- The only risk factors considered in our modelling are those that affect the values of pension schemes' assets and the financial assumptions used to value schemes' liabilities. Some of the risks that are not reflected include demographic risks (e.g. uncertainty of life expectancy), future changes to members' benefits, and legislative risks. The modelling results should therefore be viewed alongside those risks, as well as other qualitative considerations including portfolio complexity, governance burden, and liquidity risk.
- The model's projections are sensitive to the starting position and the econometric assumptions. Changes to the assumptions can have a material impact upon the output. There can be no guarantee that any particular asset class or investment manager will behave in accordance with the assumptions. Newer asset classes can be harder to calibrate due to the lack of a long-term history.
- The modelling analysis is based on portfolios containing a range of asset classes and different approaches to fund management. Clients should not make decisions to invest in these asset classes or approaches to fund management based solely on the modelling analysis.
- Portfolios that make use of derivatives are exposed to additional forms of risk and can experience losses greater than the amount of invested capital.
- No guarantee can be offered that actual outcomes will fall within the range of simulated results. Actual outcomes may be better than the simulated 95th percentile or worse than the simulated 5th percentile.

# A4: Modelling methodology (3)

### Liability Basis

- Where the model illustrates a scheme-specific funding basis (e.g. Technical Provisions), the funding basis is calculated in the same way across all the investment portfolios modelled. We therefore focus on the effect of investment strategies on asset values and hence surplus/deficits, without the distorting effect of differing discount rates. However, in cases where the discount rate allows for a risk premium, the magnitude of the risk premium may depend on the proportion of return-generating assets in the portfolio, and therefore in practice the funding basis may be different under different investment strategies.

### Contribution Basis



- The model's projections may be based on either fixed or variable contributions:
- "Fixed contributions" means that the current schedule of deficit contributions is assumed to remain in place for the full projection period. The purpose of this is to illustrate pure investment risk, showing the effect of differing investment strategies without the distorting impact of different amounts of money being contributed. In practice, however, the long-term downside outcomes would be less likely to be reached, as poor intermediate outcomes would lead to a requirement for additional contributions after future valuations.
- "Variable contributions" means that the model simulates future actuarial valuations every three years, and calculates the future deficit contributions that might be required under the particular situations being projected. This illustrates the range of possible future contribution requirements.
- In addition to the deficit contributions, the model also calculates contributions required to fund future service accrual, if there are active members accruing additional pension entitlements. In this case a small amount of variability arises from the range of possible future inflation projections. Therefore the "fixed contribution" projections may still show minor differences in contributions between, for example, Median and Bad outcomes.

# A5: Disclaimers

- This report has been prepared for the sole benefit of East Sussex County Council as Administering Authority of the East Sussex Pension Fund and based on their specific facts and circumstances and pursuant to the terms of Isio Group/ Isio Services Ltd's Services Contract. It should not be relied upon by any other person. Any person who chooses to rely on this report does so at their own risk. To the fullest extent permitted by law, Isio Group/ Isio Services Ltd accepts no responsibility or liability to that party in connection with the Services.

- The information contained within the report is available only to relevant persons, and any invitation, offer or agreement to purchase or otherwise acquire investments referred to within the report will be engaged in only with relevant persons. Any other person to whom this communication is directed, must not act upon it.

- In the United Kingdom, this Report is intended solely for distribution to Professional Clients as defined by the Financial Conduct Authority's Conduct of Business Sourcebook.

- This report has not therefore been approved as a financial promotion under Section 21 of the Financial Services and Markets Act 2000 by an authorized person.

- Isio Service Limited is authorised and regulated by the Financial Conduct Authority FRN 922376.

- The output from our modelling is based on a large number of underlying assumptions. Changes to these assumptions can have a material impact on the results of the modelling.

- The outcomes shown above are not intended to be the best possible, or worst possible outcomes. The actual outcome could be worse than the 5th percentile, or better than the 95th percentile.

- The modelling analysis is based on portfolios containing a wide range of asset classes and different approaches to fund management.  Clients should not make decisions to invest in these asset classes or approaches to fund management based solely on the modelling analysis.

- The only risk factors we have considered in our modelling are those that affect the values of pension schemes' assets and the financial assumptions used to value schemes' liabilities.  Some of the risks we have not considered include demographic risks such as the life expectancy of pension schemes' members and future changes to members' benefits.

# Thank you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# East Sussex County Council

# Pension Fund

## Funding update report as at 31 March 2021

**Barnett Waddingham LLP**

10 June 2021

# Contents

# Introduction

East Sussex County Council, as administering authority for the East Sussex County Council Pension Fund (the Fund), has asked that we carry out monitoring assessment of the Fund as at 31 March 2021. The purpose of this assessment is to provide an update on the funding position.

The Fund participates in the Local Government Pension Scheme (LGPS). The LGPS is a defined benefit statutory scheme administered in accordance with Local Government Pension Scheme Regulations 2013 (the Regulations).

We have taken account of current LGPS Regulations (as amended) as at the date of this report.

On 16 July 2020, the Government published a consultation on the proposed remedy to be applied to LGPS benefits in response to the McCloud and Sargeant cases in relation to age discrimination. The consultation closed on 8 October 2020 and a ministerial statement on 13 May 2021 confirmed that revised regulations would be issued, likely later this year. The Government also announced the unpausing of the 2016 cost cap process and that it would take into consideration the McCloud remedy. At the time of producing this report the outcome of these matters is still to be agreed so the exact impact they will have on LGPS benefits is unknown. An allowance has been made within the discount rate for the current uncertainties in LGPS benefits, details of which can be found in the Changes in market conditions – market yields and discount rates section.

The information in this report is addressed to and is provided for use by East Sussex County Council as the administering authority to the Fund. This report may be shared with other interested parties but it does not constitute advice to them.

This report complies with Technical Actuarial Standard 100: Principles for Technical Actuarial Work (TAS 100) and Technical Actuarial Standard 300: Pensions (TAS 300) as issued by the Financial Reporting Council (FRC).

We assess the funding position on a smoothed basis which is an estimate of the average position over a six month period spanning the reporting date. As the smoothing adjustment reflects average market conditions spanning a six month period straddling the reporting date, the smoothed figures are projected numbers and likely to change up until three months after the reporting date. The smoothed results are indicative of the underlying trend.

# Assets

The estimated (unsmoothed) asset allocation of the East Sussex County Council Pension Fund as at 31 March 2021, based on data received from East Sussex County Council, is as follows:

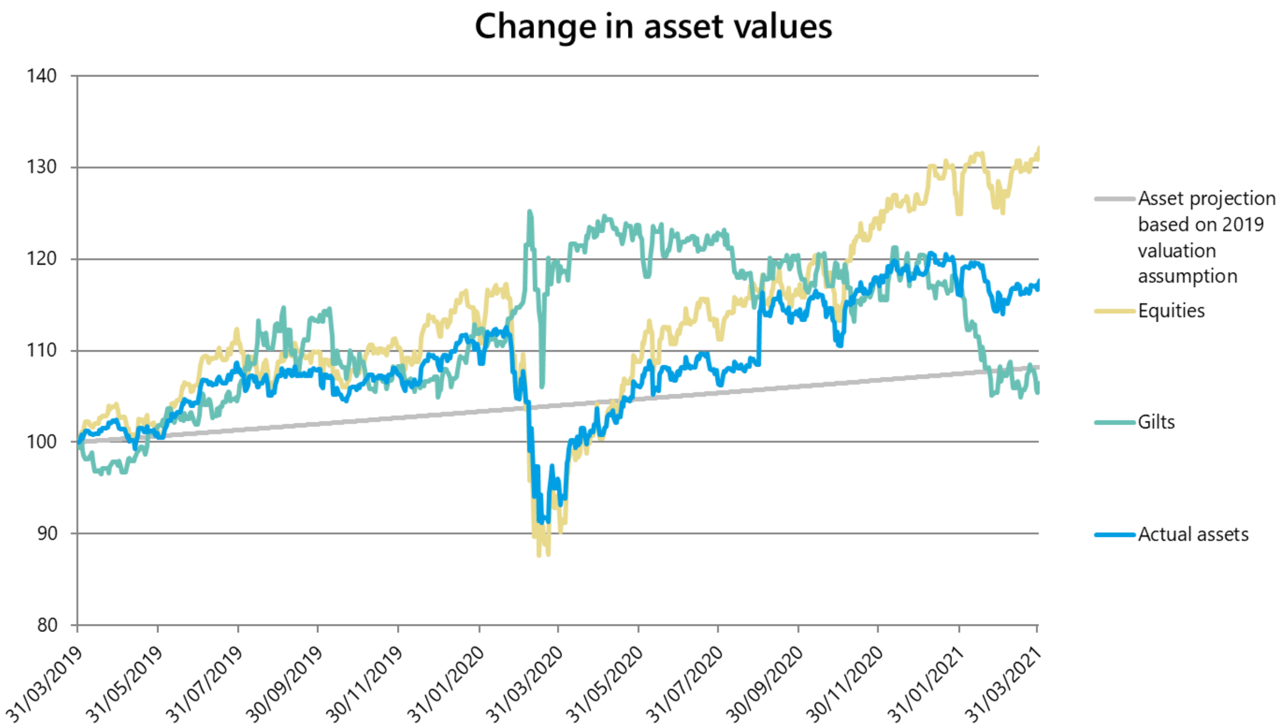
| Assets (market value) | 31 March 2021 | | 31 March 2019 | |
|---|---|---|---|---|
| | £000s | % | £000s | % |
| Equities | 3,227,118 | 76% | 2,392,487 | 66% |
| Bonds | 627,339 | 15% | 755,359 | 21% |
| Property | 319,533 | 8% | 340,346 | 9% |
| Cash | 70,882 | 2% | 144,670 | 4% |
| **Total assets** | **4,244,872** | **100%** | **3,632,863** | **100%** |

The assets in each class are an approximation, and are not a detailed indication of the breakdown of assets in any pooled investment funds

The asset value of £3,633m at 31 March 2019 is consistent with the value disclosed in the 2019 actuarial valuation report. The asset value of £4,245m was provided by the administering authority on 2 June 2021 and is subject to final audit and revision.

The investment return achieved by the Fund's assets in market value terms for the year to 31 March 2021 is estimated to be 22.0%. The return achieved since the previous valuation (31 March 2019) is estimated to be 16.7% (which is equivalent to 8.0% p.a.). This estimated return is based on Fund cashflows and total asset values rather than investment manager reports.

The following chart shows the changes in equity and bond markets since the previous actuarial valuation and compares them with the estimated actual fund returns and the expected fund returns assumed at the previous valuation:




As we can see the asset value as at 31 March 2021 in market value terms is more than where it was projected to be at the previous valuation.

For funding purposes, we now use a "smoothed" value of the assets rather than the market value. The financial assumptions that we use in valuing the liabilities are also smoothed around the valuation date so that the market conditions used are the average of the daily observations over the six month period around 31 March 2021. Therefore, we value the assets in a consistent way and apply the same smoothing adjustment to the market value of the assets.

# Changes in market conditions – market yields and discount rates

The actual investment returns earned by the Fund will affect the value of the Fund's assets. The value of the Fund's liabilities, however, is dependent on the assumptions used to value the future benefits payable.

For the purpose of this exercise it is appropriate to use the method and assumptions set by Barnett Waddingham as the new Fund actuary from 1 January 2021. Details of the derivation of the demographic assumptions can be found in the 2019 actuarial valuation report, and details of the financial assumptions can be found in the Funding Strategy Statement.

The following table shows how the main financial assumptions have changed since the last triennial valuation:

| | 31 March 2021 | | 31 March 2019 | |
|---|---|---|---|---|
| Assumptions (smoothed) | Nominal | Real | Nominal | Real |
| | % p.a. | | % p.a. | |
| Pension increases (CPI) | 2.7% | - | 2.3% | - |
| Salary increases | 3.7% | 1.0% | 2.3% | 0.0% |
| Discount rate | 4.0% | 1.3% | 4.0% | 1.7% |

The discount rate assumption is set with reference to the Fund's long term investment strategy and therefore reflects the long term expected return on assets for the Fund. We have included in the discount rate assumption an explicit prudence allowance of 1.1%. This incorporates an allowance for current uncertainties in LGPS benefits (relating to the effects of the McCloud/Sargeant judgement and the cost cap).

The previous Fund actuary, Hymans Roberston LLP, carried out the actuarial valuation as at 31 March 2019 and adopted a long-term salary increase assumption of CPI only i.e. no above inflation, or "real", salary increases. We have instead adopted a long-term salary increase assumption for funding purposes of 1.0% above CPI.

The key assumption which has the greatest impact on the valuation of liabilities is the real discount rate (the discount rate relative to CPI inflation) – the higher the real discount rate the lower the value of liabilities. As we see, the real discount rate is the same at the 31 March 2019 valuation, but the expected future increases to pensions in payment and salaries increases the value of liabilities used for funding purposes.

# Results

The funding position for each month has been rolled forward from the formal valuation and is shown in Appendix 1. It should be borne in mind that the nature of the calculations is approximate and so the results are only indicative of the underlying position.

The results of our assessment indicate that:

- The current projection of the smoothed funding level as at 31 March 2021 is 106% and the average required primary rate of employer contribution would be 21% of payroll.
- This compares with the reported (smoothed) funding level of 107% and average required primary rate of employer contribution of 18% of payroll at the 31 March 2019 funding valuation.

The Fund remains in surplus although the funding level has decreased slightly, the surplus has reduced, and the cost of benefits has increased due to higher assumed pension increases.

# Final comments

There are many factors that affect the Fund's funding position and could lead to the Fund's funding objectives not being met within the timescales expected.  Some of the key risks that could have a material impact on the Fund include longevity risk, financial risks (including inflation and investment risk) and regulatory risks. There is more detail on this contained within the Fund's Funding Strategy Statement and the 31 March 2019 actuarial valuation report.

Note that the funding position at a future date will be dependent on the investment performance of the Fund as well as future market conditions which determine the financial assumptions.

We would be pleased to answer any questions arising from this report.

Barry McKay

**Barry McKay FFA**
**Partner**
**Barnett Waddingham LLP**

# Appendix 1 Financial position since previous valuation

Below we show the financial position on a smoothed basis for each month since the previous full valuation. As the smoothing adjustment reflects average market conditions spanning a six month period straddling the reporting date, the smoothed figures for the previous three months are projected numbers and likely to change up until three months after the reporting date.

Please note that the results shown below are sensitive to the underlying assumptions. For example, increasing the discount rate assumption by 0.5% will increase the funding level by about 10%, and increasing the CPI inflation assumption by 0.5% will reduce the funding level by about 10%.

| Smoothed results | Assets | Liabilities | Surplus / (Deficit) | Funding level | CARE ongoing cost | Discount rate | Return required to restore funding level |
|---|---|---|---|---|---|---|---|
| Valuation date | £000s | £000s | £000s | % | % of pay | % p.a. | % p.a. |
| 31 Mar 2019 | 3,619,950 | 3,386,000 | 233,950 | 107% | 18.0% | 4.0% | 3.6% |
| 30 Apr 2019 | 3,680,222 | 3,357,576 | 322,646 | 110% | 17.3% | 4.7% | 4.2% |
| 31 May 2019 | 3,739,574 | 3,376,051 | 363,523 | 111% | 17.3% | 4.7% | 4.1% |
| 30 Jun 2019 | 3,787,535 | 3,393,752 | 393,783 | 112% | 17.4% | 4.6% | 4.1% |
| 31 Jul 2019 | 3,818,506 | 3,404,131 | 414,375 | 112% | 17.4% | 4.6% | 4.0% |
| 31 Aug 2019 | 3,871,770 | 3,421,444 | 450,326 | 113% | 17.4% | 4.5% | 3.9% |
| 30 Sep 2019 | 3,893,034 | 3,438,836 | 454,198 | 113% | 17.4% | 4.5% | 3.8% |
| 31 Oct 2019 | 3,913,765 | 3,457,069 | 456,696 | 113% | 17.5% | 4.4% | 3.8% |
| 30 Nov 2019 | 3,928,206 | 3,479,781 | 448,425 | 113% | 17.6% | 4.4% | 3.7% |
| 31 Dec 2019 | 3,863,138 | 3,452,356 | 410,782 | 112% | 17.3% | 4.4% | 3.8% |
| 31 Jan 2020 | 3,848,930 | 3,437,593 | 411,337 | 112% | 17.0% | 4.3% | 3.7% |
| 29 Feb 2020 | 3,831,831 | 3,432,081 | 399,750 | 112% | 16.9% | 4.3% | 3.7% |
| 31 Mar 2020 | 3,821,363 | 3,440,740 | 380,623 | 111% | 16.9% | 4.3% | 3.8% |
| 30 Apr 2020 | 3,825,354 | 3,451,966 | 373,388 | 111% | 16.9% | 4.3% | 3.7% |
| 31 May 2020 | 3,802,753 | 3,476,615 | 326,138 | 109% | 17.0% | 4.3% | 3.8% |
| 30 Jun 2020 | 3,857,687 | 3,551,106 | 306,581 | 109% | 17.5% | 4.2% | 3.8% |
| 31 Jul 2020 | 3,907,691 | 3,627,372 | 280,319 | 108% | 18.1% | 4.2% | 3.8% |
| 31 Aug 2020 | 4,170,954 | 3,693,384 | 477,570 | 113% | 18.6% | 4.1% | 3.5% |
| 30 Sep 2020 | 4,196,618 | 3,754,877 | 441,741 | 112% | 19.0% | 4.1% | 3.5% |
| 31 Oct 2020 | 4,216,633 | 3,812,396 | 404,237 | 111% | 19.4% | 4.0% | 3.5% |
| 30 Nov 2020 | 4,251,642 | 3,856,086 | 395,556 | 110% | 19.6% | 4.0% | 3.5% |
| 31 Dec 2020 | 4,271,375 | 3,904,257 | 367,118 | 109% | 19.9% | 4.0% | 3.5% |
| 31 Jan 2021 | 4,293,110 | 3,956,437 | 336,673 | 109% | 20.3% | 4.0% | 3.6% |
| 28 Feb 2021 | 4,283,270 | 3,994,927 | 288,343 | 107% | 20.5% | 4.0% | 3.6% |
| 31 Mar 2021 | 4,261,915 | 4,021,529 | 240,386 | 106% | 20.6% | 4.0% | 3.7% |

# Appendix 2 Data, method and assumptions

## Data

In completing our calculations we have used the following items of data, which we received from East Sussex County Council:

- The results of the valuation as at 31 March 2019 which was carried out for funding purposes;
- Actual whole Fund income and expenditure items for the period to 31 March 2021; and
- Estimated Fund returns based on Fund asset statements provided to 31 March 2021, and Fund income and expenditure as noted above.

The data has been checked for reasonableness and we are happy that the data is sufficient for the purpose of this report.

Full details of the benefits being valued are as set out in the Regulations as amended and summarised on the LGPS website and the Fund's membership booklet. We have made no allowance for discretionary benefits.

## Method

To assess the value of the Fund's liabilities as at 31 March 2021, we have rolled forward the value of the liabilities calculated for the funding valuation as at 31 March 2019 using the financial assumptions below and actual cashflows paid to and from the Fund.

It is not possible to assess the accuracy of the estimated value of the liabilities as at 31 March 2021 without completing a full valuation. However, we are satisifed that the approach of rolling forward the previous valuation data to 31 March 2021 should not introduce any material assumptions in the results provided that the actual experience of the Fund is broadly in line with the underlying assumptions and that the structure of the liabilities is substantially the same as at the latest formal valuation. From the information we have received there appears to be no evidence that this approach is inappropriate.

We have been provided with the Fund assets at various dates but for dates that these are not available, we calculate the Fund assets by rolling forward the previous assets provided allowing for investment returns (estimated where necessary), and actual cashflows paid to and from the Fund. The latest date that we have been provided with the Fund assets is 31 March 2021.

## Assumptions

For the purpose of this exercise it is appropriate to use the method and assumptions consistent with those set by the Fund actuary for the purpose of the 31 March 2019 actuarial valuation, updated where necessary to reflect market conditions and the funding approach of Barnett Waddingham as the new Fund actuary from 1 January 2021.

A summary of the main financial assumptions adopted is set out in the main body of this report.

As noted in the Introduction, an allowance has been made for current uncertainties in LGPS benefits (relating to the effects of the McCloud/Sargeant judgement and the cost cap). This is allowed for

At the time of producing this report the outcome of the effects relating to the McCloud/Sargeant judgement are still to be agreed upon. The final remedy in response to the judgement will only be known once a final set of remedial Regulations are published. Furthermore, it is also not known yet what benefit changes in addition to the McCloud remedy (if any) may be made in light of the results of the cost cap process.

The main demographic assumptions are:

- The post retirement mortality assumption adopted for all calculations is based on Club Vita mortality analysis.;
- The dependant post retirement mortality assumption adopted for all calculations is based on Club Vita mortality analysis.

These base tables are then projected using the CMI 2018 Model, allowing for a long-term rate of improvement of 1.25% p.a, a smoothing parameter of 7 and an initial addition parameter of 0.5% p.a. for males and 0.25% p.a. for females.

The other key demographic assumptions are:

- We have adopted the retirement age pattern assumption as used for the purpose of the 2016 LGPS cost cap valuation. Further details are available on request.; and
- It is assumed that 50% of future retirements elect to exchange pension for additional tax free cash up to HMRC limits for service to 1 April 2008 (equivalent 75% for service from 1 April 2008).

Further details of the derivation of the financial and demographic assumptions can be found in the relevant actuarial valuation report and Funding Strategy Statement.

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**Report to:** **Pension Committee**

**Date of meeting:** **12 July 2021**

**By:** **Chief Finance Officer**

**Title:** **Work Programme**

**Purpose:** **To agree the Committee's work programme**

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**RECOMMENDATION**

**The Committee is recommended to agree its work programme.**

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## 1 Background & Supporting information

1.1 The work programme contains the proposed agenda items for future Pension Board and Pension Committee meetings over the next year and beyond. It is included on the agenda for each Committee meeting.

1.2 The work programme also provides an update on other work going on outside the Board and Committee's main meetings, including working groups, upcoming training and a list of any information requested by the Board or Committee that is circulated via email.

1.3 The inclusion of the Board's work programme allows the Committee to see what work the Board will be undertaking, which will help it in its role to assist the Committee.

1.4 This item also provides an opportunity for Committee Members to reflect on any training they have attended since the last meeting.

## 2 Conclusion and reasons for recommendations

2.1 The work programme sets out the Committee's work both during formal meetings and outside of them. The Committee is recommended to consider and agree the updated work programme including consideration the regularity of agenda items to ensure effective governance of the Fund at the scheduled Committee meetings.

**IAN GUTSELL**
**Chief Finance Officer**

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Email: Sian.Kunert@EastSussex.gov.uk

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## Pension Board and Committee – Work Programme

| **Future Pension Board Agenda** | | |
|---|---|---|
| **Item** | **Description** | **Author** |
| **Standing items (items that appear on each agenda)** | | |
| Pension Board Updates | Verbal updates on training events or conferences attended by Members of the Board | N/A |
| Pension Committee Agenda | A consideration of the draft agenda of the Pension Committee. | Head of Pensions |
| Governance Report | A report on governance issues effecting the fund, developments in the LGPS, policy amendments and McCloud working group update | Head of Pensions |
| Employer Engagement and Contributions Report | A report on Employer Engagement matters to note, Employer Contributions update, Communications from the Fund and Communications working group update | Head of Pensions |
| Pensions Administration report | An update on the performance of the Pensions Administration Team. | Head of Pensions Administration |

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|---|---|---|
| Internal Audit reports | All internal audit reports on the ESPF are reported to the Board | Head of Internal Audit |
| East Sussex Pension Fund (ESPF) Quarterly budget report | An update on the ESPF's budget. | Head of Pensions |
| East Sussex Pension Fund (ESPF) Risk Register | A report on the ESPF's Risk Register | Head of Pensions |
| Work programme | A report on the Board and Committee's work programme | Head of Pensions |
| East Sussex Pension Fund (ESPF) Breaches Log | A report on the ESPF breaches log | Head of Pensions |
| Employer Admissions and Cessations | A report on the admission and cessation of employers to the ESPF. | Head of Pensions |
| **14 September 2021** | | |
| Covenant Review Report | Report from PWC on the covenant review project | Head of Pensions |
| Annual Report of the Pension Board | Annual report of the Pension Board to the Scheme manager outlining the work throughout the year | Head of Pensions with the Chair of the Board |
| Independent Auditors Report on the Pension Fund Account and Annual Report and | A report on the External Audit findings of the Pension Fund financial Statements and the complete 2020/21 Annual Report and Accounts. | Head of Pensions |

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|---|---|---|
| Accounts 2020/21 | | |
| Communications Policy | Revision to the Communications Policy | Head of Pensions |
| GDPR | Refresh of the GDPR policies including the Privacy notice including the communications of these documents | Governance and Compliance Pensions Manager |
| Representation of Pension Committee | Report requested by Cllr Druitt as employer representative for Brighton and Hove City Council on the representation on the Pension Committee as decision maker for the Fund | Cllr Druitt (Employer representative) |
| **5 November 2021** | | |
| Employer Forum Agenda | Discussion on Pension Fund Employer Forum Agenda topics | Head of Pensions |
| Annual Training Plan | Report on Training completed in the year and training recommendations for the up-coming year | Head of Pensions |
| Good Governance Decision making matrix | Report to outline the revise the decision-making matrix for the Pension Fund, delegations and representations in line with SAB Good Governance project | Head of Pensions |
| **10 February 2022** | | |
| Business Plan and Budget 2022/23 | Report to set the Budget for the Pension Fund for the Financial Year 2022/23 including the Business Plan with key deliverables for the year. | Head of Pensions |

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|---|---|---|
| External Audit Plan for the East Sussex Pension Fund 2021/22 | Draft External Audit Plan for 2021/22 Pension Fund Financial Statements | Head of Pensions |
| **June 2022** | | |
| Internal Audit Strategy and Plan | Draft internal audit Pension Fund Strategy and Audit Plan 2022/23 | Internal Audit |
| Governance and Compliance Statement | Annual Review of Governance and Compliance Statement | Governance and Compliance Pensions Manager |
| Annual Report of the Pension Board | Annual report of the Pension Board to the Scheme manager outlining the work throughout the year | Head of Pensions with the Chair of the Board |
| Training Policy | Biannual review of the training Strategy | Governance and Compliance Pensions Manager |

| Actions requested by the Pensions Board | | |
|---|---|---|
| **Subject Area** | **Detail** | **Status** |
| Internal Audit reports | The Board requested that internal audit consider an audit of the common data sets provided to the Pensions Regulator | TBC |
| Scheme administration | The Board requested a report on potential recommendations from the Scheme Advisory Board (SAB) that the Scheme Manager role is removed from local authority control. | Ongoing discussions |
| Scheme administration | The Board requested a future report on how the ESPF KPIs for pension administration compare with those of other local government pension schemes. | To be considered at September 2021 meeting |
| Decision making | To revise the decision-making matrix (including a RACI model) and to circulate it for information. | To be provided November 2021 |

| Future Pension Committee Agenda | | |
|---|---|---|
| **Item** | **Description** | **Author** |
| **Standing items (items that appear on each agenda)** | | |
| Investment Report | A Quarterly performance report of the investment managers | Head of Pensions and Investment Consultant |
| Governance Report | A report on governance issues effecting the fund, developments in the LGPS, policy amendments and McCloud working group update | Head of Pensions |
| Employer Engagement and Contributions Report | A report on Employer Engagement matters to note, Employer Contributions update, Communications from the Fund and Communications working group update | Head of Pensions |
| Pensions Administration report | An update on the performance of the Pensions Administration Team. | Head of Pensions Administration |
| Internal Audit reports | All internal audit reports on the ESPF are reported to the Board | Head of Internal Audit |
| East Sussex Pension Fund (ESPF) Quarterly budget report | An update on the ESPF's budget. | Head of Pensions |
| East Sussex Pension Fund (ESPF) Risk Register | A report on the ESPF's Risk Register | Head of Pensions |

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|---|---|---|
| Work programme | A report on the Board and Committee's work programme | Head of Pensions |
| East Sussex Pension Fund (ESPF) Breaches Log | A report on the ESPF breaches log | Head of Pensions |
| Employer Admissions and Cessations | A report on the admission and cessation of employers to the ESPF. | Head of Pensions |
| **28 September 2021** | | |
| Statement on Responsible Investment Principles | Annual report on the review of the Statement on Responsible Investment Principles | Head of Pensions |
| Responsible Investment implementation Statement | Report outlining the implementation of Responsible investment within the Fund | Head of Pensions |
| 2020 Stewardship Code | Report outlining the Funds compliance with the 2020 Stewardship Code | Head of Pensions |
| Independent Auditors Report on the Pension Fund Account and Annual Report and Accounts 2020/21 | A report on the External Audit findings of the Pension Fund financial Statements and the complete 2020/21 Annual Report and Accounts for review. | Head of Pensions |
| Covenant Review Report | Report from PWC on the covenant review project | Head of Pensions |
| Communications Policy | Revision to the Communications Policy | Head of Pensions |

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|---|---|---|
| GDPR | Refresh of the GDPR policies including the Privacy notice including the communications of these documents | Governance and Compliance Pensions Manager |
| Contracts and Tenders | Appointment of Independent Advisor | Head of Pensions |
| **25 November 2021** | | |
| Annual Training Plan | Report on Training completed in the year and training recommendations for the up-coming year | Head of Pensions |
| **24 February 2022** | | |
| External Audit Plan for the East Sussex Pension Fund 2021/22 | Draft External Audit Plan for 2021/22 Pension Fund Financial Statements | Head of Pensions |
| Business Plan and Budget 2022/23 | Report to set the Budget for the Pension Fund for the Financial Year 2022/23 including the Business Plan with key deliverables for the year. | Head of Pensions |
| **June 2022** | | |
| Internal Audit Strategy and Plan | Draft internal audit Pension Fund Strategy and Audit Plan 2022/23 | Internal Audit |
| Governance and Compliance Statement | Annual Review of Governance and Compliance Statement | Governance and Compliance Pensions Manager |
| Annual Report of the Pension Board | Annual report of the Pension Board to the Scheme manager outlining the work throughout the year | Head of Pensions with the Chair of the Board |

| | | |
|---|---|---|
| Carbon Footprinting | A report on the carbon footprint of the portfolio of ESPF including whether investments are in line with transition pathways. | Head of Pensions |
| Training Policy | Biannual review of the training Strategy | Governance and Compliance Pensions Manager |
| **July 2022 (no standing items)** | | |
| Independent Auditors Report on the Pension Fund Account and Annual Report and Accounts 2021/22 | A report on the External Audit findings of the Pension Fund financial Statements and the complete 2021/22Annual Report and Accounts for review. | Head of Pensions |
| Training / Focus of choice | Time for specific training or to focus on a specific topic | Head of Pensions |



| **Actions requested by the Committee** | | |
|---|---|---|
| **Subject Area** | **Detail** | **Date completed** |
| | | |

| **Current working groups** | | |
|---|---|---|
| **Title of working group** | **Detail and meetings since last Pensions Board and Committee meetings** | **Membership** |

| | | |
|---|---|---|
| Investment Implementation Working Group (IIWG) | The Investment Working Group and ESG working group have been amalgamated, as agreed at Pensions Committee 21 September 2020.<br><br>The IIWG has an advisory role to over oversee the implementation of decisions by the Pension Committee in relation to investment decisions and carry out detailed research and analysis for Pensions Committee.<br><br>Recent meetings<br><br>• 27 April 2021<br>• 2 June 2021<br>• 18 June 2021 | William Bourne, Russell Wood, Sian Kunert, Representative from Investment Consultant<br><br>Cllr Fox or substitute committee member is invited to attend |
| Data Improvement and ABS Working Group | Recent meetings<br><br>• 29 March 2021<br>• 14 April 2021<br>• 27 May 2021<br><br>Scheduled<br><br>• 29 July 2021<br>• 23 August 2021 | Cllr Fox, Ray Martin, Diana Pogson, Stephen Osborne, Paul Punter, Sian Kunert, Ian Gutsell |
| McCloud Working Group | The McCloud Working Group has been established to oversee the implementation of the McCloud ruling within a prescribed timeframe and addressing any gaps and barriers preventing progress and ultimately delivery of the project.<br><br>A high-level impact assessment has been completed to identify those members of the scheme that will be affected by this ruling.<br><br>The Group have acknowledged there are many data requests of employers and this project needs to be managed carefully with other demands on employers time.<br><br>Recent meetings<br><br>• 22 April – supported by Hymans | Cllr Fox, Stephen Osborn, Lynda Walker, Paul Punter, Sian Kunert, Dave Kellond |

| | | |
|---|---|---|
| Communications Working Group | The Communications Working Group was established by the Pensions Board in February 2021 to drive forward improvements in communications with stakeholders with support from employee and employer representatives.<br><br>Recent meetings<br>• 2 June<br><br>Scheduled<br>• 20 July<br>• 18 August | Ray Martin, Lynda Walker, Diana Pogson, Sian Kunert, Tim Hillman<br><br>Any other Board member is invited to join sessions |

| **Training and Development - recent and future events** | | | |
|---|---|---|---|
| **Title of Training/Briefing** | **Detail** | **Date** | **Attended** |
| PLSA ESG conference | 3 Day ESG focused investment conference run by the PLSA focusing on Climate, Fossil Fuels, policies and practice, Data Governance for climate and ESG risks | 30 June – 2 July 2021 | Cllr Fox, Cllr Hilton, Cllr Redstone, Cllr Adeniji |
| **Title of Training/Briefing** | **Detail** | **Proposed Date** | **Invited** |
| Infrastructure Training | In house session with guest presentations from Pantheon and GLIL | 8 July | Committee Members |
| Fixed Income Training and Investment Strategy Training | In house session run by Isio to support the investment strategy discussions at the upcoming committee | 9 July | Committee Members |
| Personal Cyber Resilience | AON Webinar on Cyber Resilience | 8 & 22 July | Committee Members and Board members |

| | | | |
|---|---|---|---|
| Overview of the Local Government Pension Scheme | Overview of the Local Government Pension Scheme for new Committee o Board members or as a refresher. | 15 July & 28 October | Committee Members and Board members |
| Cryptocurrency | Training on Cryptocurrency investment provided by Ruffer, as requested by Committee on 1 March 2021 | TBC | Committee Members |
| An introduction to covenant | PWC training session for officers, Committee and Board members to understand Employer covenants and their importance. Part of the Covenant review project. | 3 August | Committee Members and Board members |
| Employers in distress | PWC training session for officers, Committee and Board members to understand how to manage Employers in distress following the employer covenants analysis. Part of the Covenant review project. | 10 August | Committee Members and Board members |

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# Agenda Item 10

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Appendix 1

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