



FOR PUBLICATION

DERBYSHIRE COUNTY COUNCIL

PENSIONS AND INVESTMENTS COMMITTEE

WEDNESDAY, 6 DECEMBER 2023

Report of the Director - Finance and ICT

**STRATEGIC ASSET ALLOCATION BENCHMARK AND INVESTMENT
STRATEGY STATEMENT**

1. Purpose

- 1.1 To seek approval for a new Strategic Asset Allocation Benchmark for Derbyshire Pension Fund (the Fund/Pension Fund) and a revised Investment Strategy Statement for consultation with the Fund's stakeholders.

2. Information and Analysis

2.1 Strategic Asset Allocation Benchmark

At the last formal actuarial valuation at the end of March 2022, the funding level of the Pension Fund was 100%. This was an improvement on the funding level of 97% at the formal valuation at the end of March 2019. This improvement was consistent with the gradual improvement in the Fund's funding level over the last decade, which has improved from 82.5% at the end of March 2013 to 100% at the end of March 2022.

The funding level of the Pension Fund is the ratio of assets to liabilities at the valuation date. The funding level provides a high-level snapshot of the funding position at a particular date.

On 31 March 2022, the assets of the Fund were valued at £6,132m and the past service liabilities were estimated to be £6,131m. The investment and membership experience of the Fund from March 2019

to March 2022 had a positive impact on the funding level, partly offset by higher inflation increasing the cost of past service liabilities.

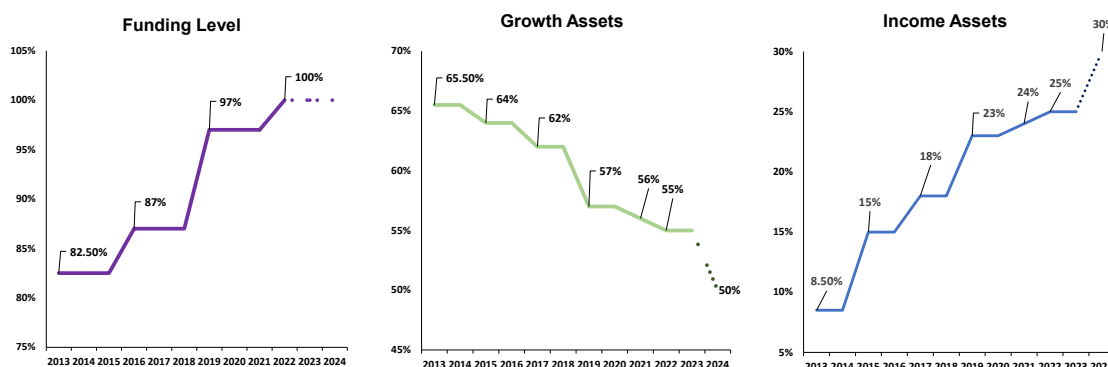
Following the receipt of the formal March 2022 actuarial valuation, the Fund's Strategic Asset Allocation Benchmark (SAAB) has been reviewed, taking into consideration the further improvement in the funding level. The following changes are proposed:

Asset Class	Current SAAB	Intermediate SAAB	Final SAAB	Final Change
UK Equities	12.0%	10.0%	8.0%	(4.0%)
Japanese Equities	5.0%	2.5%	-	(5.0%)
Emerging Market Equities	5.0%	2.5%	-	(5.0%)
Global Sustainable Equities	29.0%	31.5%	36.0%	7.0%
Private Equity	4.0%	6.0%	6.0%	2.0%
Growth Assets	55.0%	52.5%	50.0%	(5.0%)
Infrastructure	10.0%	11.5%	13.0%	3.0%
Multi-Asset Credit	6.0%	6.5%	7.0%	1.0%
Direct Property	6.0%	9.5%	10.0%	1.0%
Indirect Property	3.0%			
Income Assets	25.0%	27.5%	30.0%	5.0%
Conventional Bonds	6.0%	6.0%	6.0%	-
Index-Linked Bonds	6.0%	6.0%	6.0%	-
Corporate Bonds	6.0%	6.0%	6.0%	-
Cash	2.0%	2.0%	2.0%	-
Protection Assets	20.0%	20.0%	20.0%	-
Total	100.0%	100.0%	100.0%	-

The proposed final SAAB includes a 5% switch from Growth Assets to Income Assets, reflecting the improvement in the Fund's funding position noted above, whilst acknowledging that the Fund remains open to new members and continues to accrue additional future pension liabilities. The proposed final SAAB also includes a change in the composition of the Fund's equity exposure.

The proposed 5% switch from Growth Assets to Income Assets reflects the continuation of a gradual change in the Fund's exposure to both Growth Assets and Income Assets over the last decade as the Fund's funding position has improved. As shown in the charts below, the Fund's exposure to Growth Assets has been reduced from 65.5% of total assets on 31 March 2013 to 55.0% on 31 March 2023. Over this

same period, the Fund's share of Income Assets has increased from 8.5% to 25.0%.



The Fund's In-House Investment Management Team notes that Growth Assets can be extremely volatile, whereas Income Assets are generally more defensive and less correlated to the business cycle and economic conditions. As a result, Income Assets tend to be less volatile than Growth Assets, with lower levels of drawdowns at times of market stress and uncertainty. The Fund's Income Assets, which relate to Infrastructure, Property and Multi-Asset Credit, are also return seeking assets and are supported by predictable and recurring cash yields.

In November 2020, the Fund's regional equity allocations were streamlined, when the Fund's North America, Europe and Asia Pacific Ex-Japan Equity allocations were consolidated and switched into Global Sustainable Equities. This allocation targets investment in global companies that are sustainable in financial, environmental, social and governance terms, and where appropriate, that provide solutions to sustainability challenges.

The IIMT recommends that this streamlining is now extended to cover the Fund's Japanese and Emerging Market Equity allocations. It should be noted that all these regions are represented within a global sustainable equity allocation, and as result, the Fund's equity investments will continue to be geographically diversified and exposed to global and regional GDP drivers. The IIMT continues to recommend a standalone allocation to UK Equities because the UK equity market offers portfolio diversification.

The IIMT notes that the transition from regional equities, with a heavy UK home bias, towards a more global approach over the last 10 to 20 years has been a common trend across LGPS & UK corporate pension funds. The IIMT believes that a global approach should provide the

Fund's underlying investment managers with the opportunity to out-perform through regional tactical asset allocation.

It is proposed that the majority of the recommended 5% increase in Income Assets is allocated to Infrastructure, taking the asset class weighting from 10% to 13%. Infrastructure is an attractive asset class for the Pension Fund, offering equity like returns, predictable long-term cash flows which are often linked to inflation, and returns with a low correlation to other major asset classes. The balance reflects a 1% increased allocation to both Multi-Asset Credit and Property.

It is also recommended that the current direct and indirect property allocations are merged into one property allocation, to simplify asset class allocation, albeit the allocation will continue to be heavily tilted towards UK commercial property. The IIMT believes that this will allow the Fund's Discretionary Direct Property Manager to actively source additional opportunities, whilst reducing the investment management fees payable by the Fund. Some exposure to indirect property will be maintained to increase portfolio diversification.

Given the quantum of the proposed changes between the current and final SAAB, the IIMT recommends that an intermediate SAAB is also approved to allow the IIMT to manage the transition risk towards the final SAAB. It is proposed that the intermediate SAAB would come into effect at the beginning of 1 April 2024, with the final SAAB coming into effect by 1 April 2025 at the latest.

2.2 Investment Strategy Statement

The Fund's SAAB is included in the Fund's Investment Strategy Statement. LGPS Regulations require an administering authority to prepare an Investment Strategy Statement in accordance with the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016 (the 2016 Regulations). The Fund's Investment Strategy Statement was last revised in November 2020.

Under the 2016 Regulations, the Investment Strategy Statement must be reviewed, and if necessary revised, following a material change in the factors which are judged to have a bearing on the stated investment policy, and at least every three years. Given the proposed changes to the Fund's SAAB set out in this report, a revised Investment Strategy Statement has been prepared, a copy of which is set out at Appendix 2.

The Investment Strategy Statement must cover:

- A requirement to use a wide variety of investments

- The authority's assessment of the suitability of particular investments and types of investment
- The authority's approach to risk, including how it will be measured and managed
- The authority's approach to pooling investments, including the use of collective investment vehicles and shared services
- The authority's policy on how social, environmental and corporate governance considerations are taken into account in the selection, non-selection, retention and realisation of investments
- The authority's policy on the exercise of rights (including voting rights) attached to its investments

The Investment Strategy Statement must also set out the maximum percentage of the total value of all investments of fund money that it will invest in particular investments or classes of investment and the authority is required to consult such persons as it considers appropriate regarding the proposed contents of its investment strategy.

The Fund's independent investment adviser, Anthony Fletcher, has reviewed the revised Investment Strategy Statement and the proposed changes to the SAAB and a copy of the advisor's review is set out at Appendix 3.

2.2 LGPS Pooling Consultation Response

The response from the Department for Levelling Up, Housing & Communities (DLUHC) to the 'Local Government Pension Scheme (England and Wales): Next steps on investments' consultation was published at the same time as the government's Autumn Statement.

DLUHC intends to publish revised investment strategy statement guidance to reflect its expectations with respect to LGPS investment pooling, a requirement for LGPS funds to have a plan to invest up to 5% in levelling up projects and the government's ambition for LGPS funds to invest 10% of assets in private equity.

The Fund's Investment Strategy Statement will be subject to further review when the new guidance is published.

3. Consultation

- 3.1 It is intended to consult with scheme members, scheme employers, members of Derbyshire Pension Board, and other stakeholders on the revised Investment Strategy Statement. The results of the consultation will be reported to Committee in March 2024.

4. Implications

- 4.1 Appendix 1 sets out the relevant implications considered in the preparation of the report.

5. Background Papers

- 5.1 Working papers held by the Pension Fund Team.

6. Appendices

- 6.1 Appendix 1 – Implications
6.2 Appendix 2 – Draft Investment Strategy Statement
6.3 Appendix 3 – Report of the Fund’s Independent Investment Adviser

7. Recommendation(s)

That Committee:

- a) approves the draft revised Investment Strategy Statement attached as Appendix 2, which includes the proposed changes to the Fund’s Strategic Asset Allocation Benchmark, for consultation with the Pension Fund’s stakeholders.

8. Reasons for Recommendation(s)

- 8.1 The Committee is responsible for reviewing and approving the Pension Fund’s statements, strategies and policies.

Report Author: Neil Smith

Contact details: neil.smith2@derbyshire.gov.uk

Appendix 1

Implications

Financial

1.1 None

Legal

2.1 The Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016 require an administering authority to prepare an investment strategy statement.

Human Resources

3.1 None

Information Technology

4.1 None

Equalities Impact

5.1 None

Corporate objectives and priorities for change

6.1 None

Other (for example, Health and Safety, Environmental, Sustainability, Property and Asset Management, Risk Management and Safeguarding)

7.1 None