

LONDON BOROUGH OF CAMDEN	WARD: ALL
REPORT TITLE: Triennial Valuation update	
REPORT OF: Executive Director of Corporate Services	
FOR SUBMISSION TO: Pension Board	DATE: 16 March 2022
SUMMARY OF REPORT: This report updated the Pension Committee on an interim valuation of the Fund by the Fund's actuary, Hymans Robertson. The Pension Committee noted the report.	
Local Government Act 1972 – Access to Information No documents required to be listed were used in the preparation of this report. Contact Officer: Nigel Mascarenhas Interim Director of Finance Finance and Procurement Corporate Services Dennis Geffen Annexe 110-112 Camley Street London. N1C 4DG Telephone: 0207 974 1904 Email: nigel.mascarenhas@camden.gov.uk	
RECOMMENDATIONS: The Pension Board is asked to note the contents of this report.	
Signed by Director of Finance Agreed Date 07/03/2022	

1. INTRODUCTION AND BACKGROUND

- 1.1. Every three years the Fund's assets and liabilities must be valued by a qualified actuary as set out in the regulations which govern the Local Government Pension Scheme (LGPS). The last valuation was undertaken in 2019 by our actuaries who are Hymans Robertson (Hymans).
- 1.2. The primary purpose of a valuation is to determine whether the Pension Fund has sufficient assets to meet its long-term pension liabilities. A scheme that is 100% funded would have sufficient assets (over time) to meet its current pension promises in the future, assuming the current assumptions are borne out in practice. The actuary is required to certify the appropriate contribution rates each employer in the Fund must make over the next three years. This involves setting rates for all employers in the Fund (not just the Council) whose employees participate in the Fund whether these are community admission bodies or transferee admission bodies using the LGPS regulations to determine benefits.
- 1.3. The next formal triennial valuation will occur during 2022 with the results based on March 2022 asset values and liability data. This is a major milestone for the Fund and involves considerable work by the Pensions Shared Service, officers and Hymans. This will be reported to Committee in the autumn of 2022. This report presents an interim position for Pension Committee based on 30 September 2021 data and is indicative but by no means as detailed and accurate as the actual Triennial Valuation.
- 1.4. Hymans' work is presented in Appendix A and they will join our meeting to talk through the detail of the report.

2. RESULTS

- 2.1. As at the last valuation the assets of the Fund were £1.6bn. As at the end of September Fund assets stood at £2.2bn which is an annualised return of 31% and is obviously much higher than expectations embedded in the last triennial valuation of investment returns of 4.5%.
- 2.2. Liabilities are estimated to have risen from £1.6bn to £1.7bn and by comparison to assets have not risen so quickly.
- 2.3. This leads to an overall funding level rising from 103% funded as at March 2019 to an estimated 130% funded as at September 2021. The surplus for the whole Fund, in cash terms, has risen from £41m to £522m. Hymans attribute the strong surplus to the increase in asset values over the period.
- 2.4. The investment rate required to be notionally fully funded has reduced from the last valuation from 4.3% to an estimated 2.8% as at the end of September.
- 2.5. Given the likely improving position for employers underlying the whole fund picture, this will mean that secondary contributions (set to catch up with deficit funding positions) should, all things being equal, reduce at the next valuation.
- 2.6. Hymans also caution that this interim valuation whilst welcomed also comes with some health warnings:
 - Yields may stay low

- Future Inflationary pressures being seen in the wider economy may erode these as liabilities are linked to CPI
 - Market volatility may impact the Fund
- 2.7. The Hymans work comments on managing investment risk. Once the full valuation is received in September 2022 the Fund will consider its investment strategy in light of this. The steps set out in the investment risk section of Appendix A will then be considered. The Fund has already considered rebalancing recently and agreed to reduce the equity allocation from 65% to 50% and with the Improvement and Development Agency Substitution of Funds and reduction at Harris we will achieve this shortly.

3. ISIO AND THE INDEPENDENT INVESTMENT ADVISOR VIEWS

- 3.1. The results of the interim valuation have been shared with the Fund's Investment Consultant, **Isio**, and they have made the following comments.
- 3.2. Since the date of the last formal actuarial valuation (March 2019) the Fund's funding position has seen a material improvement (from 103% to 130%) and a rise in surplus (from £41m to £522m). The key driver behind this improved position is strong investment returns (both in absolute terms and relative to the long-term investment return assumption employed by the Fund Actuary). Equity markets, along with other growth asset markets, have performed particularly strongly, driven by high levels of central bank and government financial stimulus, to help combat market volatility caused by the COVID pandemic.
- 3.3. Throughout 2020 and 2021, following receipt of the last formal actuarial valuation, the Committee has agreed to (and begun to implement) a lower risk target investment strategy. This includes reducing the equity allocation from 65% to the target weight of 50%, reducing the diversified growth allocation from a target weight of 15% to 5%, increasing index-linked gilts from 3% to 8%, and adding an allocation of 5% to inflation-linked property.
- 3.4. Given the strong interim actuarial valuation results, Isio believe the focus should be on fully implementing the aforementioned lower risk strategy (we understand that this is well underway). Once this is complete there may be further strategic changes which could be considered in order to better manage the risk and return profile of the Fund, given the new circumstances.
- 3.5. Following implementation of the lower risk strategy, the key risks for the Fund will remain as equities (given the large strategic allocation here) and rising realised and expected inflation (given the uncapped inflation uplifts inherent in the Fund's liability structure). As such, we propose that any further strategic changes look to reduce these key risks and thereby further lower the overall risk profile of the Fund (whilst still ensuring the Fund targets sufficient return to meet its objectives, e.g. meeting future accrual requirements).
- 3.6. Reduction of these risks is particularly important given the current market environment, where we are seeing upward inflationary pressures, which are now beginning to feed into rising longer-term inflation expectations. The market is also anticipating central bank interest rate rises to help manage this rising inflation, and these rate rises could lead to increased market volatility for

growth assets (e.g. equities) as financial stimulus and government support is removed.

3.7. Strategic options that the Fund could consider are:

- to increase the allocation to the Fund's current mandates which have returns directly linked to inflation (e.g. infrastructure equity, inflation-linked property and index-linked gilts)
- or to implement new allocations to other assets which are able to provide this direct inflation linkage (e.g. infrastructure debt).
- There could also be a focus to reduce the equity allocation further from 50% - either to fund the allocations noted above, or to allocate to senior private debt, which would help to diversify the Fund's overall return & risk drivers.

3.8. In terms of nearer-term changes that could help to reduce the risk profile of the Fund, the Committee could consider reallocating a portion of the equity allocation to index-linked gilts or multi-asset credit. Given the high liquidity of these assets, these switches could be done relatively easily, and would reduce the overall risk/return profile of the Fund. We are mindful however that there has been some concern previously expressed by the Committee around pricing of index-linked gilts.

3.9. There should also be consideration given to the Fund's private market mandates (LCIV Infrastructure Fund and LCIV Inflation Plus Fund). These positions will likely be underweight versus their benchmark allocations, given the strong returns that other areas of the portfolio have experienced. A top-up to these allocations would help to lower overall risk (although there would be some deployment lag time).

3.10. The **Independent Investment Advisor comments** that this could be an opportunity to de-risk the portfolio further, given the surplus. However, with this being an open pension fund, some exposure to growth assets will still be needed. Inflation risk is a growing concern.

3.11. Possible options the Fund could consider are:

- explore increased allocations to the existing 'secure income' asset classes to de-risk equities further;
- consider allocations to new secure income asset classes to de-risk equities;
- review the level of inflation protection in the fund with a view to exploring new asset classes or increasing allocations to the existing inflation-linked investments.

4. **FINANCE COMMENTS OF THE EXECUTIVE DIRECTOR CORPORATE SERVICES**

4.1. It is welcome to see the Funding level increase from 103% to an estimated 130% as at September 2021. As Hymans set out before receiving the next valuation in September 2022 there are a number of variables which could, and no doubt, will change which will mean the final triennial valuation results will change. Once the Fund receives these results they can revisit the Fund's

Investment Strategy and the Investment Consultant and Independent Investment Adviser set out useful options to consider once we have a more accurate valuation.

5. LEGAL COMMENTS OF THE BOROUGH SOLICITOR

- 5.1. The Local Government Pension Scheme Regulations 2013 requires an Administering Authority to obtain an actuarial valuation of its fund every three years. The administering authority must obtain a report by an actuary in respect of the valuation, and a rates and adjustments certificate provided by the actuary. The report must contain a statement of the demographic assumptions used in producing the valuation, and how these assumptions relate to events which have actually occurred in relation to the scheme membership. The recommendations in this report are in accord with the Pension Committee legal and regulatory duties.

6. APPENDICES

APPENDIX A – Hymans - Triennial Valuation update