Pension Fund Investment Sub-Committee

Date: Friday 3 February 2023
Time: 11.00 am
Venue: Committee Room 2, Shire Hall

Membership

Councillor Christopher Kettle (Chair)
Councillor Bill Gifford (Vice-Chair)
Councillor Brian Hammersley
Councillor Sarah Millar
Councillor Mandy Tromans

Items on the agenda:

Monica Fogarty
Chief Executive
Warwickshire County Council
Shire Hall, Warwick

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Disclosures of Pecuniary and Non-Pecuniary Interests
Members are required to register their disclosable pecuniary interests within 28 days of their election of appointment to the Council. Any changes to matters registered or new matters that require to be registered must be notified to the Monitoring Officer as soon as practicable after they arise.

A member attending a meeting where a matter arises in which they have a disclosable pecuniary interest must (unless they have a dispensation):

- Declare the interest if they have not already registered it
- Not participate in any discussion or vote
- Leave the meeting room until the matter has been dealt with
- Give written notice of any unregistered interest to the Monitoring Officer within 28 days of the meeting

Non-pecuniary interests relevant to the agenda should be declared at the commencement of the meeting.

The public reports referred to are available on the Warwickshire Web
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Pension Fund Investment Sub-Committee

Monday 12 December 2022

Minutes

Attendance

Committee Members
Councillor Christopher Kettle (Chair)
Councillor Bill Gifford (Vice-Chair)
Councillor Brian Hammersley
Councillor Sarah Millar
Councillor Mandy Tromans

Officers
John Cole, Senior Democratic Services Officer
Jane Farrell, Technical Expert Senior Solicitor, Commercial and Regulatory
Andy Felton, Assistant Director, Finance
Martin Griffiths, Technical Specialist – Pension Fund Policy and Governance
Paul Higginbotham, Investment Analyst, Pensions and Investment
Victoria Moffett, Lead Commissioner – Pensions and Investment
Chris Norton, Strategy and Commissioning Manager (Treasury, Pension, Audit and Risk)
Max Taylor, Graduate Management Trainee
Nic Vine, Strategy and Commissioning Manager (Legal and Democratic)

Others Present
Rob Bilton, Hymans Robertson
Anthony Fletcher, Independent Advisor
Philip Pearson, Hymans Robertson
Bob Swarup, Independent Advisor

1. General

The Chair thanked members of the Sub-Committee for agreeing to reschedule the time of the meeting.

(1) Apologies

Apologies were received from Viktoria Bachtler (Hymans Robertson).

(2) Members' Disclosures of Pecuniary and Non-Pecuniary Interests

There were none.

Warwickshire County Council

(3) Minutes of the Previous Meeting

Resolved:

That the minutes of the meeting held on 14 October 2022 be approved as a correct record and signed by the Chair.

There were no matters arising.

2. Review of the Minutes of the Warwickshire Local Pension Board Meeting of 12 July 2022

Resolved:

That the Pension Fund Investment Sub-Committee notes the minutes of the Local Pension Board meeting of 12 July 2022.

3. Governance Report

Martin Griffiths (Technical Specialist – Pension Fund Policy and Governance) introduced the report which provided updated governance information relating to Warwickshire Pension Fund's forward plan, risk monitoring, training, and policy. He requested that the Sub-Committee give specific attention to the Funding Strategy Statement (FSS) which had been issued to employers and members of the Fund as part of an official consultation. He highlighted the changes that had been made to the Risk Monitoring Chart, including an increased residual impact score for climate change. He advised that the Climate Policy was currently being reviewed by Hymans Robertson following a workshop held with officers and advisors. It would be presented to the Sub-Committee for approval in March 2023.

Rob Bilton (Hymans Robertson) provided a summary of the FSS which set out the strategy objectives of the Fund, including measures to secure long-term solvency. The role of Hymans Robertson as the Fund's actuary was to recommend changes to the FSS where appropriate. He advised that very few changes to the funding strategy had been made following the recent valuation. The principal revision was to introduce a corridor approach for academy schools. This would lead to greater stability of contribution rates. He advised that other material changes to content could be viewed in appendix C, including details of how the Fund would manage climate change risks and appendix D, where the underlying actuarial assumptions have been updated. He stated that it was positive that very few changes to the content of the FSS had been required. The layout of the document had been overhauled to improve its accessibility for stakeholders.

Rob Bilton advised that the appendices to the FSS provided details of specific policies, such as the Fund's approach for payment of exit credits. He advised that the consultation had been launched at the Fund's Annual General Meeting in November 2022. Employers and members of the Fund had been asked to submit comments by the end of January 2023. Feedback would be reviewed prior to bringing a finalised version of the FSS to the Sub-Committee in March 2023.

In response to the Chair, Anthony Fletcher (Independent Advisor to the Sub-Committee) advised that he had no specific concerns in relation to the Risk Register. He stated that the Fund had enacted measures to mitigate the harms caused by climate change. However, it was questionable whether net zero carbon by 2050 would be achieved internationally. This would be an area for continued scrutiny and discussion.

Bob Swarup (Independent Advisor to the Sub-Committee) stated that climate change was a key policy consideration. He suggested that risks be set out as clearly and succinctly as possible to limit the likelihood of any risks being overlooked.

Councillor Millar left the meeting at 15.00.

In response to the Chair, Victoria Moffett (Lead Commissioner – Pensions and Investment) advised that the Risk Register was updated on a quarterly basis. It was informed by a review of the Risk Appetite which took place annually. The risk scores determined how the Fund's resources should be allocated to address specific risks.

In response to the Chair, Victoria Moffett advised that the Carbon Footprint Report, reviewed by the Sub-Committee in June 2022, outlined the ways in which climate change could place the Fund at risk. Since then, the risk status for climate change had been upgraded. It was difficult to quantify the extent of the risk presented by climate change; however, it would be monitored closely.

Councillor Hammersley underlined the importance of continued monitoring of climate risks.

Philip Pearson (Hymans Robertson) stated that the Carbon Footprint report provided a key tool for monitoring of the level of risk posed by climate change. He emphasised the significance of transition risk, where a company that is reluctant to act on climate change is eventually forced out of business by regulatory changes.

In response to Councillor Hammersley, Philip Pearson stated that climate change reporting was a developing area. There were parts of the portfolio, such as private markets, where data was quite limited. Companies had a responsibility to declare their carbon emissions. Companies' reports were now being scrutinised by independent organisations to call out companies that made spurious declarations.

The Chair acknowledged that it was difficult to quantify risks associated with climate change. However, he suggested that it would be helpful to include a summary alongside the Risk Register identifying the implications of specific risks. This would provide assurance to members of the Pension Scheme, allowing them to gauge the impact of changes to the Risk Register.

Bob Swarup stated that this was a governance and transparency consideration. He suggested that, following a review of the Risk Appetite, a commentary be provided to give an idea of whether a specific risk was within acceptable parameters or moving towards the threshold of becoming a serious concern. This would capture a sense of the direction of travel and whether, from a fiduciary perspective, the Fund was comfortable with the level of risk.

The Chair queried whether the diversity of the portfolio would suffer if a resolution was made to reduce the Fund's exposure to certain high-risk areas, leading to lower returns.

Bob Swarup advised that higher risk investments did not always signify higher returns. There was a fundamental balance; the Fund should strive to reduce risk and increase its return on investments.

In response to Councillor Hammersley, Victoria Moffett advised that within a diverse portfolio there were different levels of risk. Different asset types had different types of risk. However, measures were in place to ensure that the risk to members of the Scheme was extremely low; the Fund would be able to honour its commitments.

Councillor Gifford queried whether there were risks associated with a move by the Fund to mitigate specific risks. For example, by withdrawing from fossil fuels in favour of environmentally sustainable assets (which also attracted other responsible investors), there could be danger of entering a sellers' market, leading to escalating prices.

Andy Felton (Assistant Director, Finance) advised that there was a range of actions that the Fund could take to mitigate specific risks. However, there were also external factors that could increase risk. Climate change was an area which presented a wide range of potential actions. There was scope for officers to supply a more detailed commentary to provide improved context for members.

In response to Councillor Hammersley, Anthony Fletcher advised that investment should be targeted at companies that were looking sustainably at the future. This brought longevity; responsible investment was not limited to green technologies.

In response to the Chair, Rob Bilton advised that Hymans Robertson had met with officers to undertake a line-by-line assessment of employers of the Fund to determine funding positions. Engagement was undertaken with high-risk employers to mitigate the risk of deficits being incurred if they choose to leave the Fund. He offered to liaise with officers to look at how information could be presented to support members' understanding of the profile of sub-funds.

Councillor Millar re-joined the meeting at 15.40.

Resolved:

That the Pension Fund Investment Sub-Committee:

1. Notes the items contained within the Governance Paper.
2. Notes the Funding Strategy Statement (FSS) that was previously issued to employers and members in an official consultation.

4. Reports Containing Exempt or Confidential Information

Resolved:

That members of the public be excluded from the meeting for the items mentioned below on the grounds that their presence would involve the disclosure of exempt information as defined in paragraph 3 of Part 1 of Schedule 12A of the Local Government Act 1972.

5. Liquidity Fund Selection

The Sub-Committee resolved to defer this item for future consideration.

6. Infrastructure Fund Recommendation

The Sub-Committee resolved to defer this item for future consideration.

7. Liability Benchmark

The Sub-Committee resolved to defer this item for future consideration.

8. AVC Review

The Sub-Committee resolved to defer this item for future consideration.

9. Quarterly Investment Monitoring Report

The Sub-Committee received a confidential briefing.

10. General Activity Update

The Sub-Committee received a confidential briefing.

11. Exempt Minutes of the Previous Meeting

Resolved:

That the exempt minutes of the meeting held on 14 October 2022 be confirmed as an accurate record and signed by the Chair.

There were no matters arising.

The meeting rose at 16.55.

……………………………
Chair

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Pension Fund Investment Sub-Committee

3 February 2023

Macro Update

Recommendation

That the Pension Fund Investment Sub-Committee (PFISC) notes and comments on the report.

1. Executive Summary

1.1 The purpose of this report is to provide a six-monthly update on the wider factors having the greatest influence on the Pension Fund's performance, particularly from a macroeconomic perspective.

1.2 The key areas brought out by the Camdor Global report (Appendix 1) are:

- UK interest rates, with inflation taken into consideration (real rates), seem to have stopped falling following a steep decline between mid-2021 and mid-2022. This could influence the Fund's implementation of a proposed protection portfolio restructure which relies on 20yr real rates being above 0.5%.
- Global inflation is likely to have peaked, though the global economy continues to contract. This means that there is greater value in some investment areas, e.g. corporate bonds and UK equities.
- Interest rate increases are expected to continue into 2023, but market expectations are that they may stop by the end of the year. Camdor's expectation is that the UK may encounter a harsher period of austerity than following the 2007/8 financial crisis which took real GDP c.7 years to recover from.
- Civil unrest continues to increase globally which is destabilising for the global economy.
- UK company insolvencies are at their highest level since Q3 2009, this could affect the Fund's private debt and UK corporate bonds holdings.
- UK commercial property rent expectations have fallen, as has capital value expectations. This may be reflected in the Fund's property holdings.
- Private equity managers' expectations around asset prices have fallen since early 2020 (pre-covid).
- The UN expects an average temperature rise of 2.8 degrees Celsius this century given current policies. This is significantly above the

unconditional nationally determined contributions (NDCs) from The Paris Agreement 2015. Significant investment is required to transform the global economy to a low-carbon setting. Some additional investment is going into renewables, and hydrocarbons. The Fund's Climate metrics are likely to be affected by the gradual movements.

2. Financial Implications

2.1 None

3. Environmental Implications

3.1 None arising directly from this report. Whilst the matters covered by Camdor in their general overview are likely to impact on the environmental position of the Fund, these impacts will be dealt with in respect of individual investments and decisions as appropriate.

4. Supporting Information

4.1 See Appendix 1.

5. Timescales associated with the decision and next steps

5.1 N/a

Appendices

Appendix 1 – The Bigger Picture (Camdor Global Advisors)

	Name	Contact Information
Report Authors	Paul Higginbotham, Victoria Moffett, Chris Norton	paulhigginbotham@warwickshire.gov.uk, victoriamoffett@warwickshire.gov.uk, chrisnorton@warwickshire.gov.uk
Assistant Director	Andrew Felton (Assistant Director – Finance)	AndrewFelton@warwickshire.gov.uk
Strategic Director	Rob Powell (Strategic Director for Resources)	RobPowell@warwickshire.gov.uk
Portfolio Holder	Cllr Peter Butlin (Finance and Property)	peterbutlin@warwickshire.gov.uk

The report was circulated to the following members prior to publication:
Local Member(s):
Other members: Cllrs Kettle and Gifford

Camdor GLOBAL ADVISORS

MAKING THE COMPLEX SIMPLE

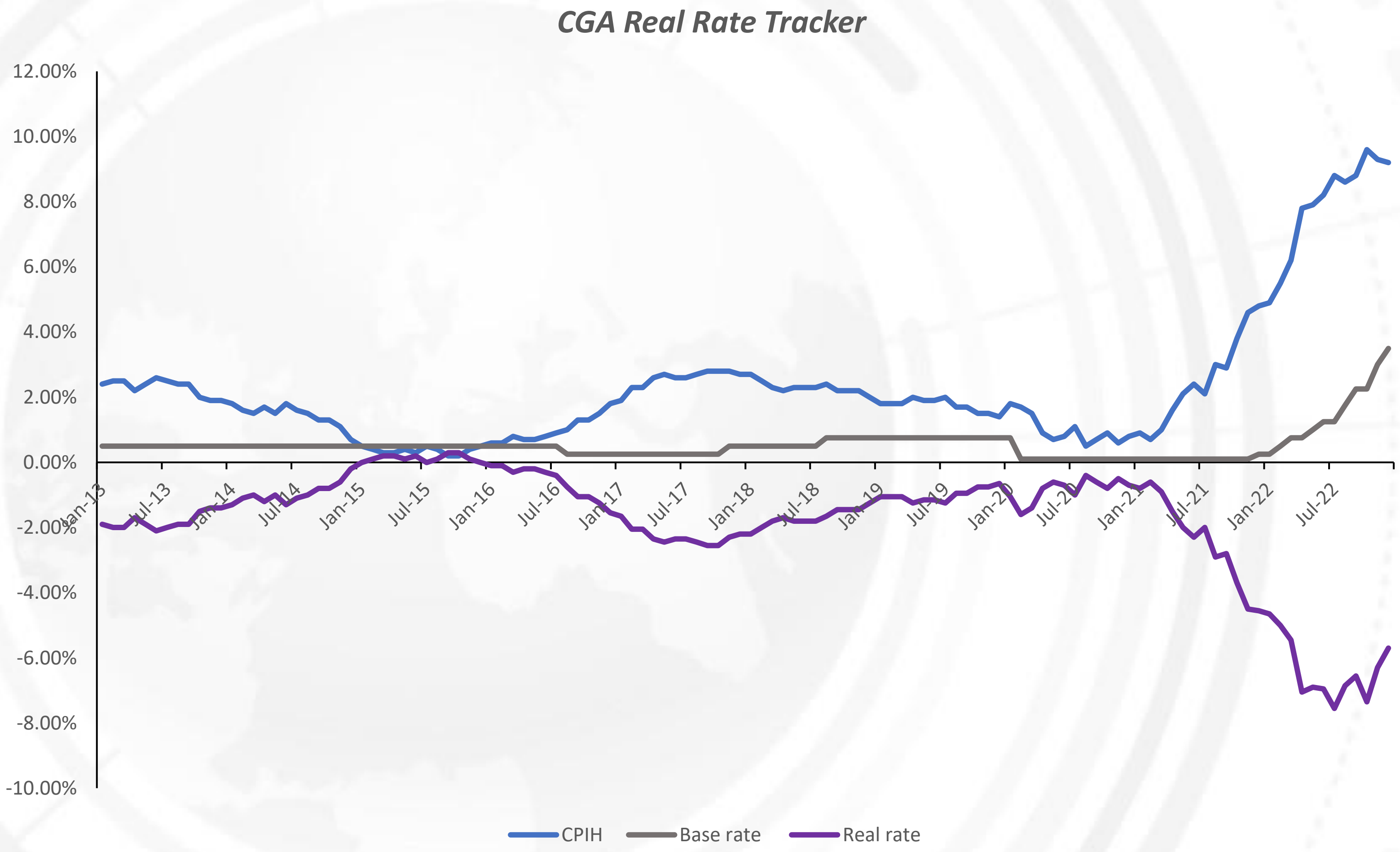
THE BIGGER PICTURE

Key macro dynamics of relevance

January 2023

Dr Bob Swarup
Camdor Global Advisors

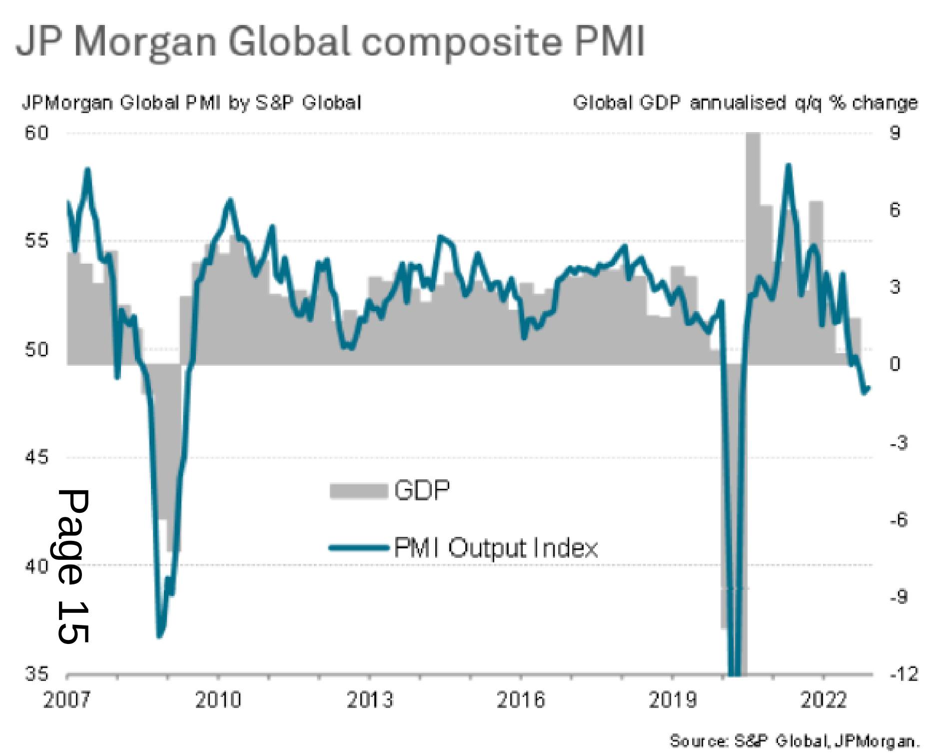
UK real rates appear to be bottoming…

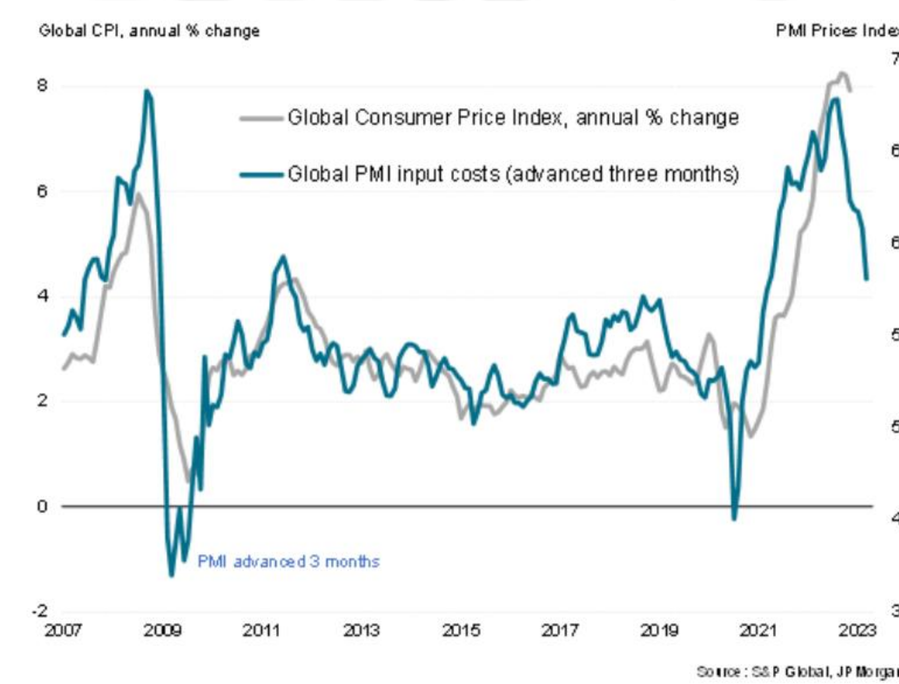


Source: Camdor Global, ONS

The continued and rapid rise in interest rates is starting to lead to inflation falling and real rates bottoming out. However, there is significant ground to claw back, indicating continued rises in the coming months.

There is good and bad



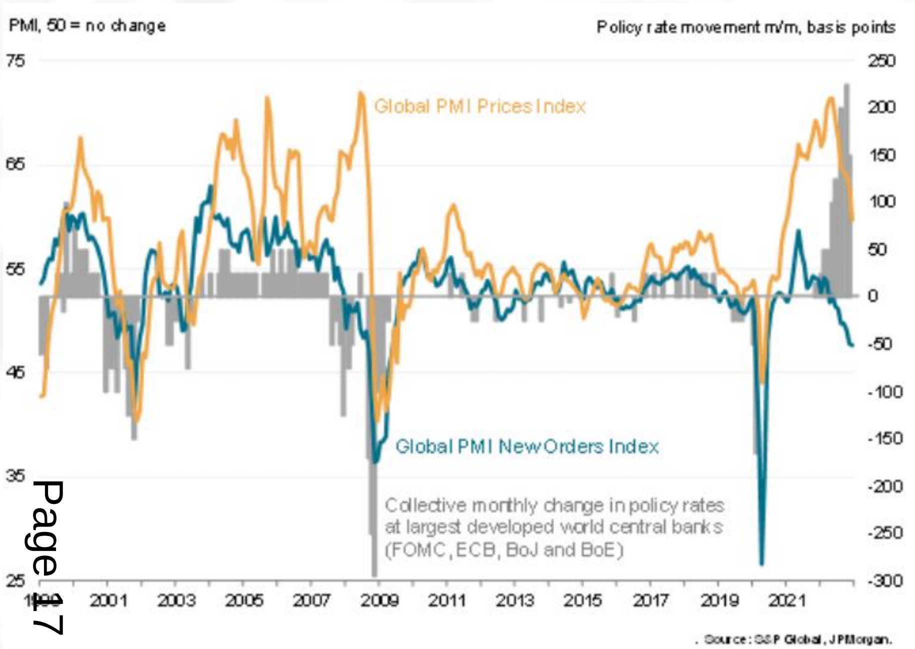


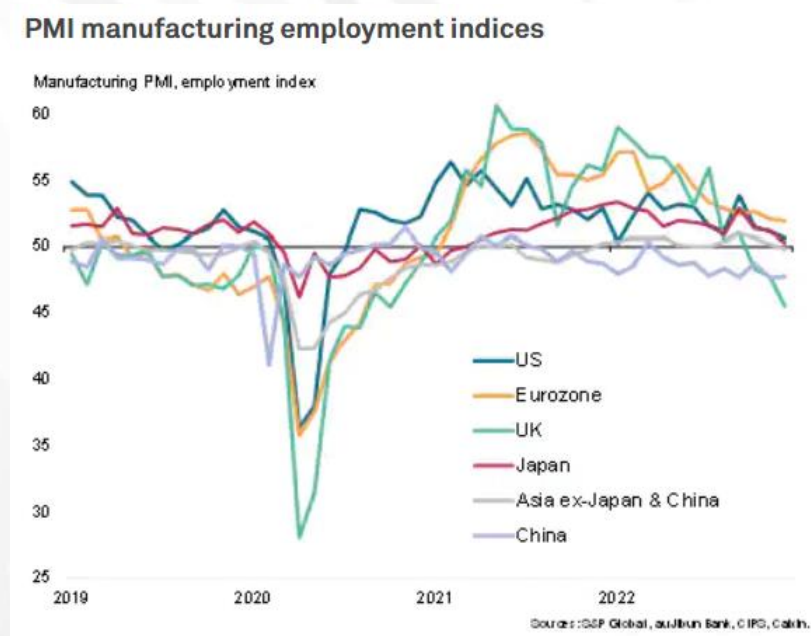
The latest PMI numbers indicate a fifth straight month of global contraction, but inflation should also fall sharply in the coming months, looking at input costs. The implication is amelioration in Q2 onwards, albeit against the backdrop of a weak economy. Meanwhile, a number of areas, such as corporate bonds and UK equities are showing value.

Markets are looking ahead and show some value…

The year has begun with a strong rally, and future rate expectations are declining, as a) markets believe that the rate cycle will come to an end in 2023, and b) economies have shown a little more resilience in the data than anticipated, e.g. the UK's surprise economic growth (albeit thanks to the World Cup).

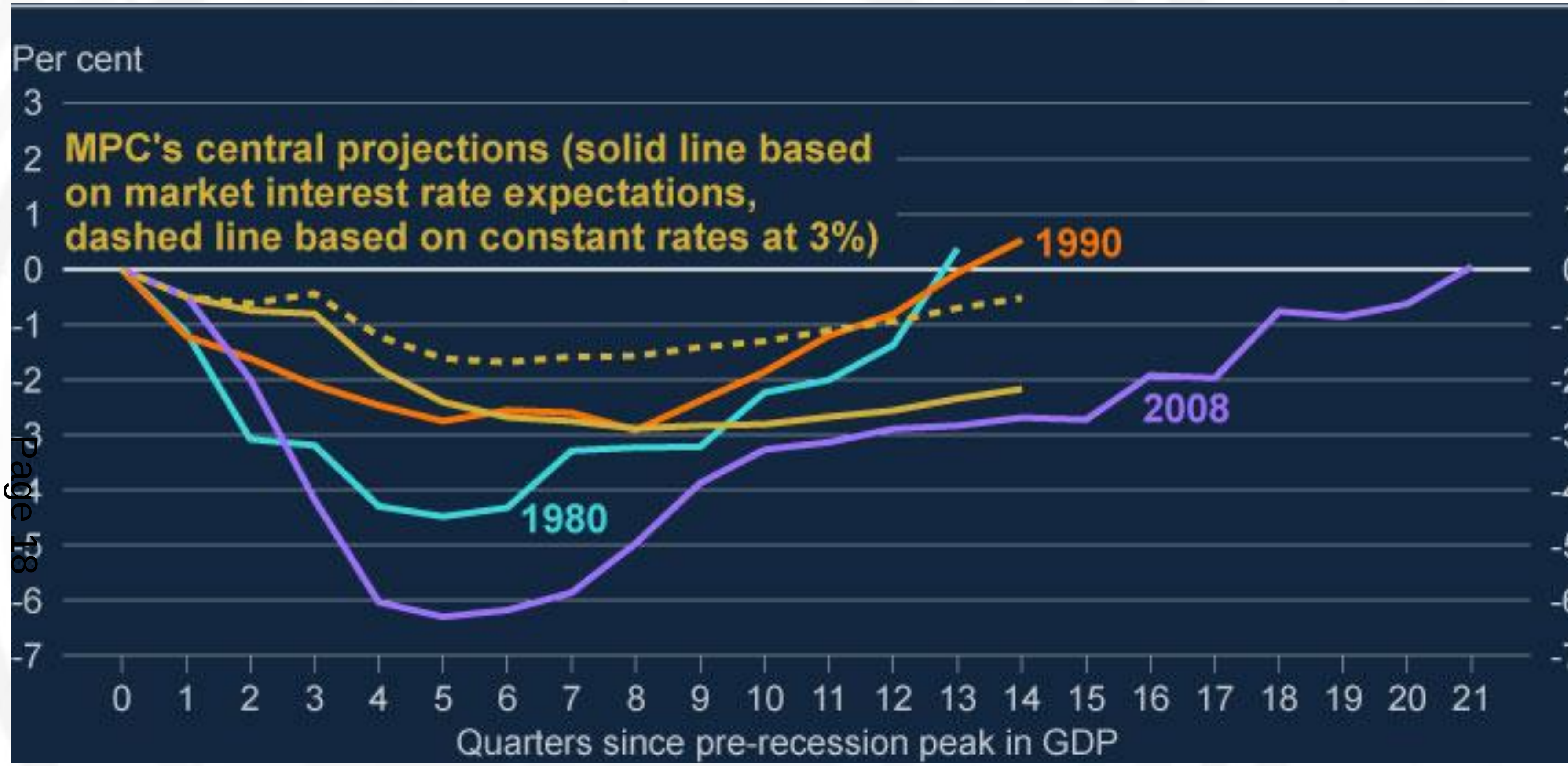
…but there are also challenges bubbling up





Central banks are continuing to hike into a downturn, putting added pressure. Employment is beginning to stagnate or even contract (e.g. in the UK manufacturing sector) as businesses manage costs and falling demand, but wage inflation and inflationary sentiment still remains high.

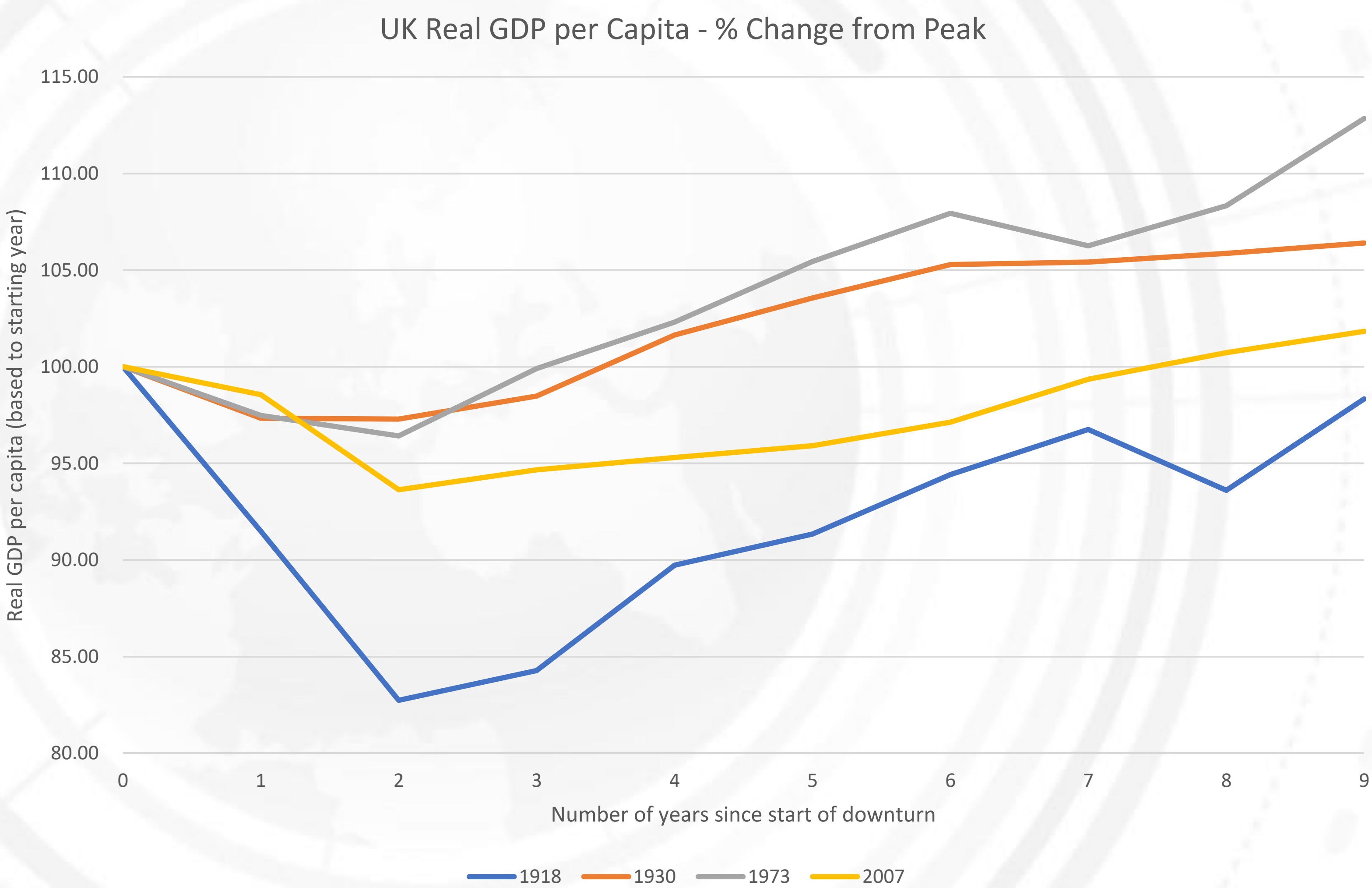
The UK's financial turmoil



Source: Bank of England

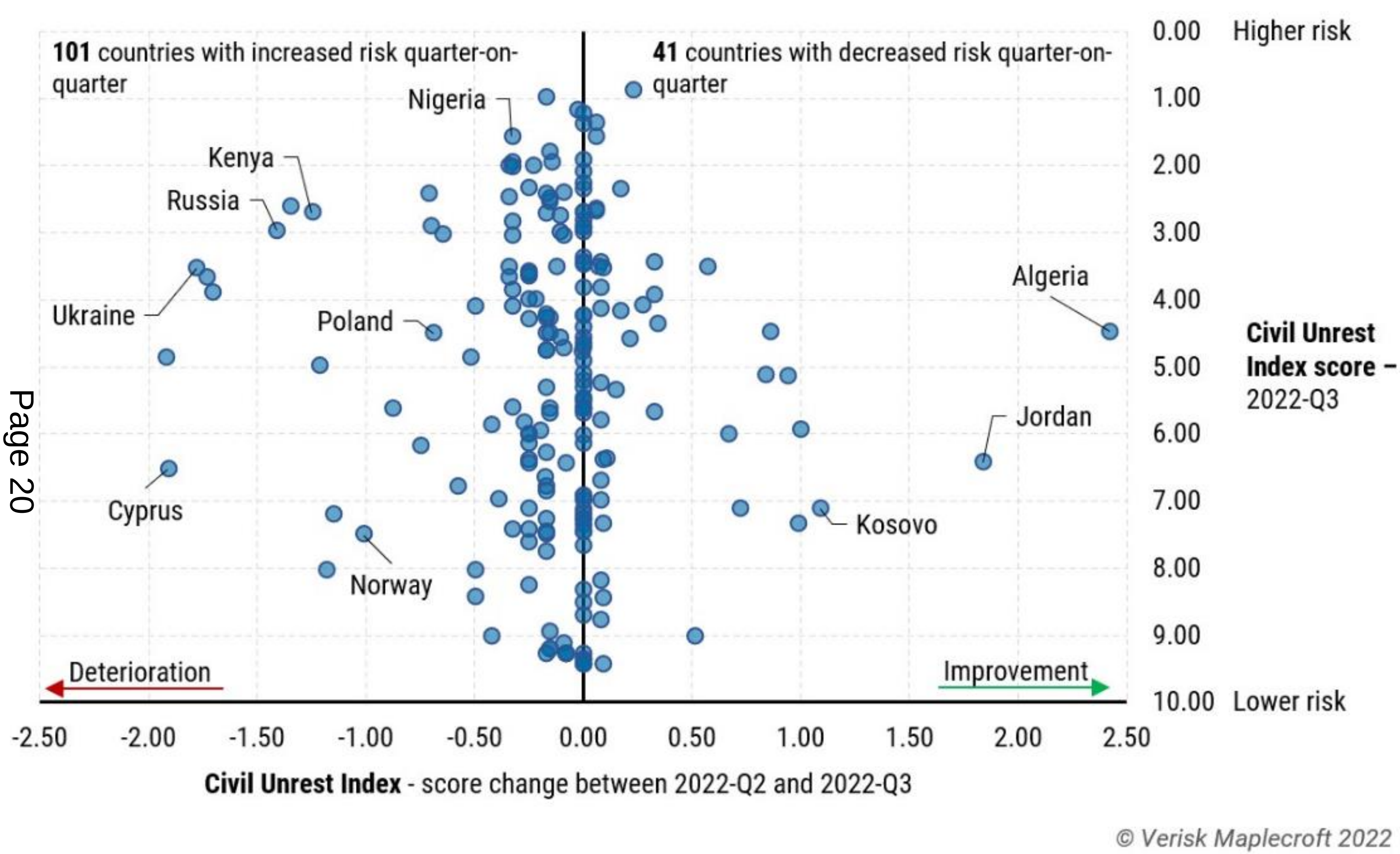
Markets think rates need to go up more but that has to be balanced against a multi-year recession. Given fiscal issues, the UK may potentially encounter a more difficult period of austerity than the period after the 2008 financial crisis in order to stabilize the economy.

The last decade of austerity

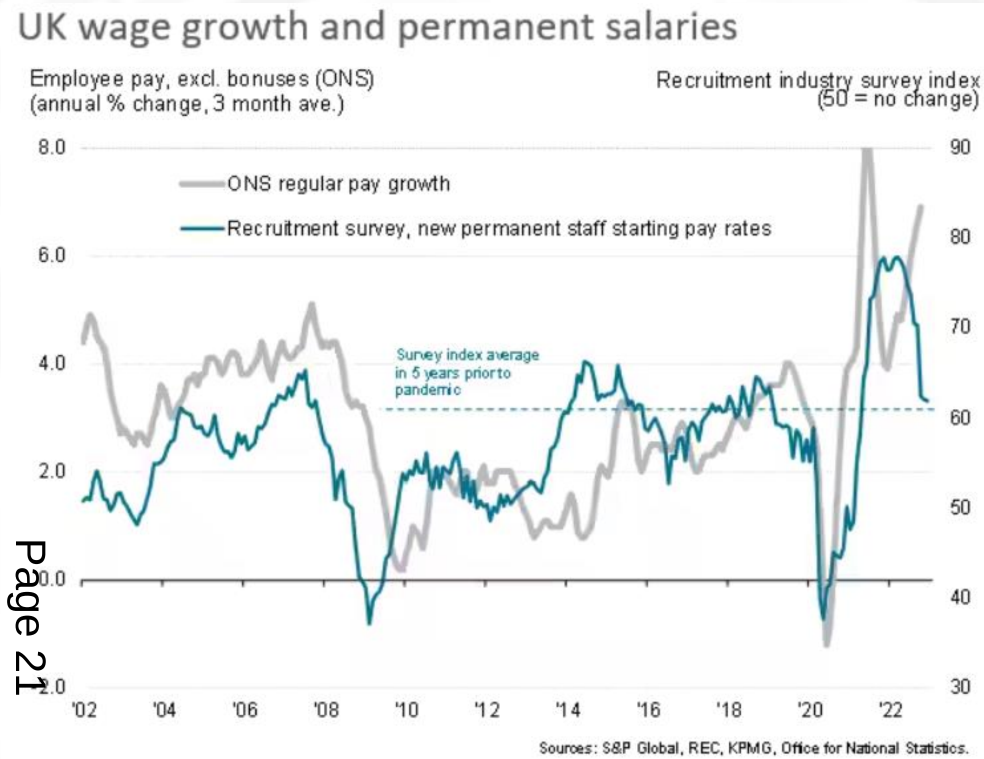


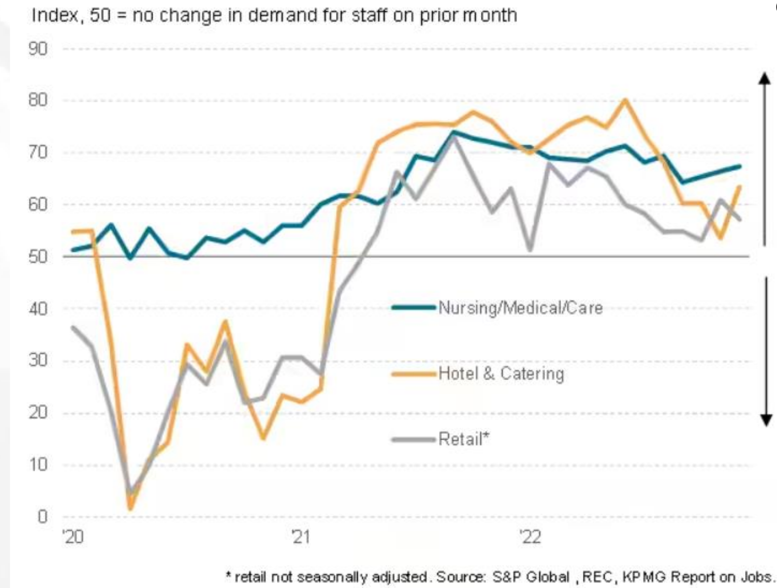
Source: Camdor Global Advisors

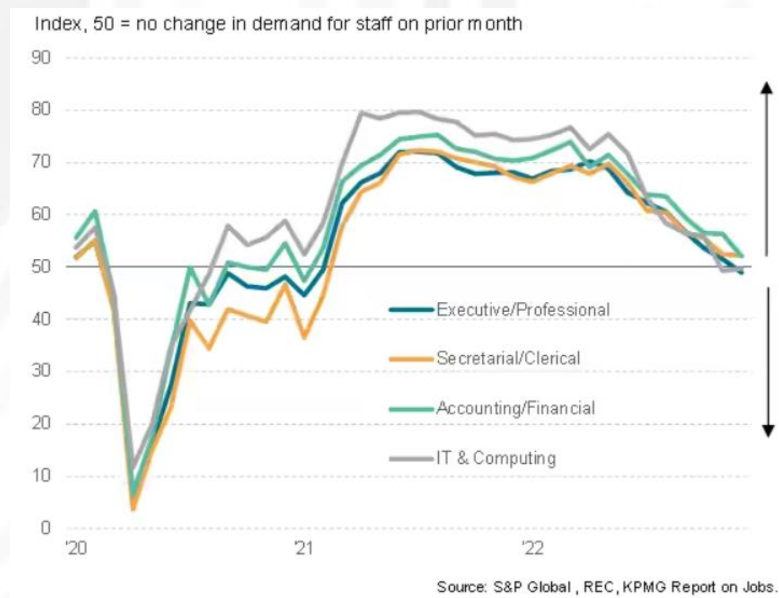
But we have more discontent today…



Wages will be a flashpoint in 2023

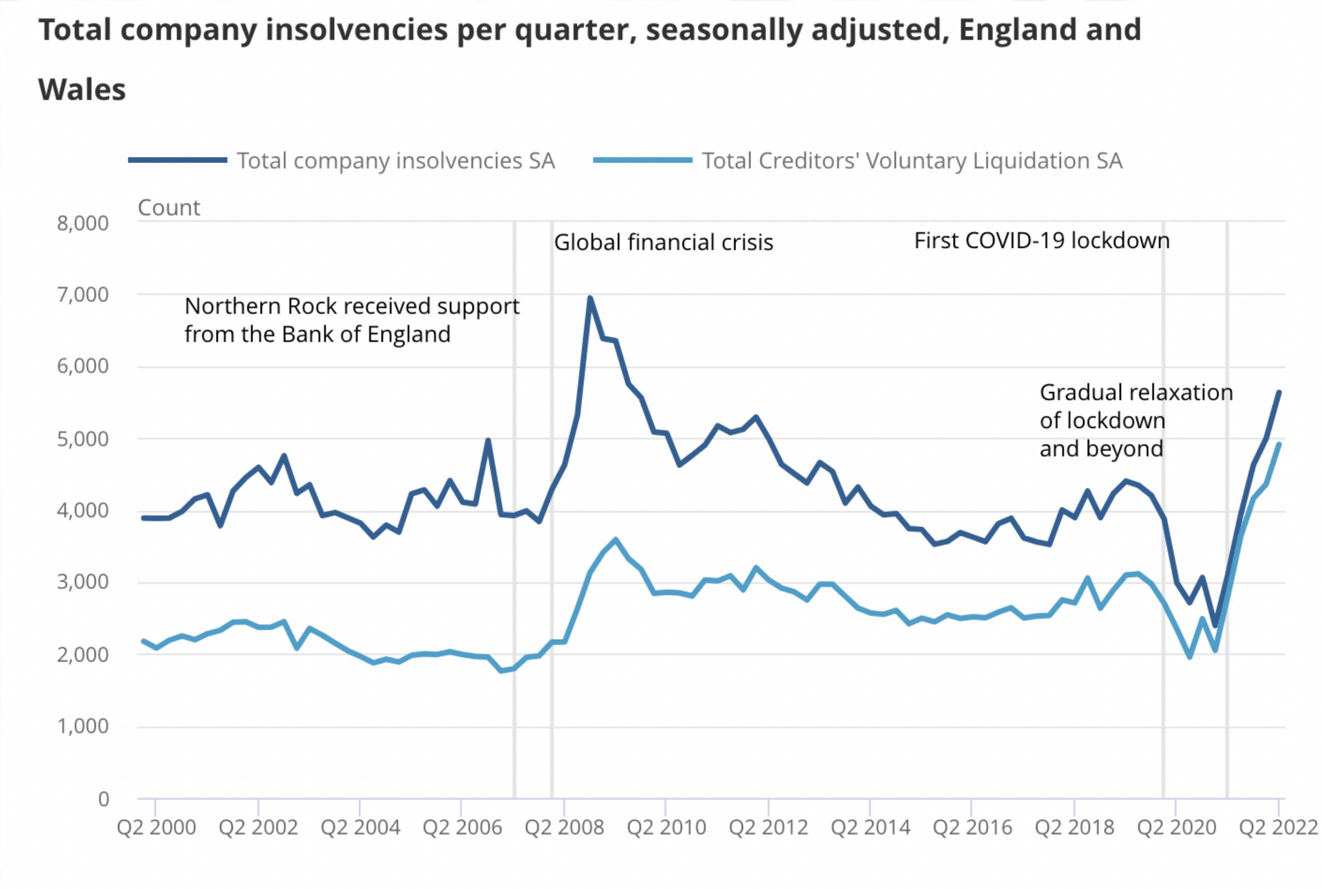






The data is showing mixed signals and divergence, supporting arguments for both employers and employees. Meanwhile, the calls for managing wage inflation are likely to grow stronger.

Businesses are under pressure…

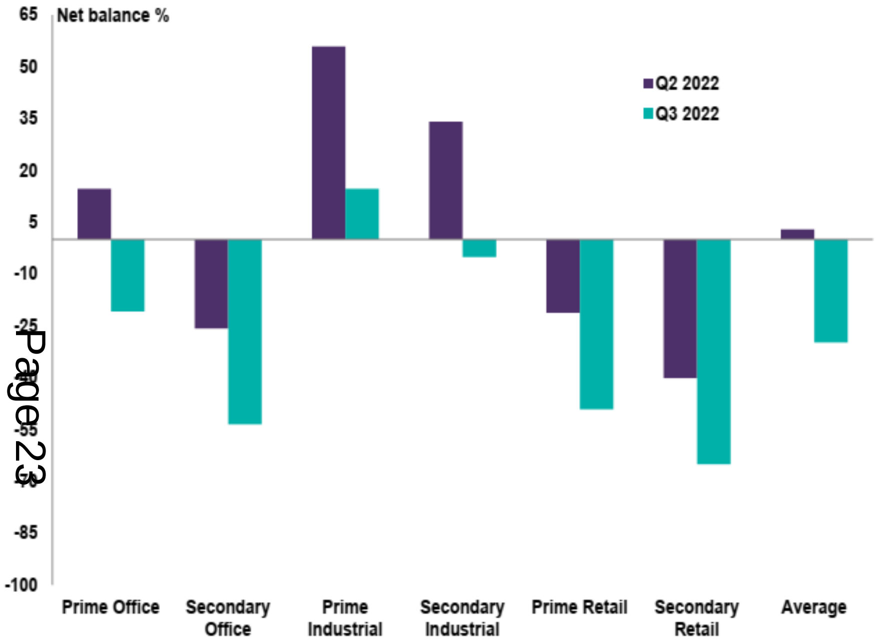


Source: Insolvency Service

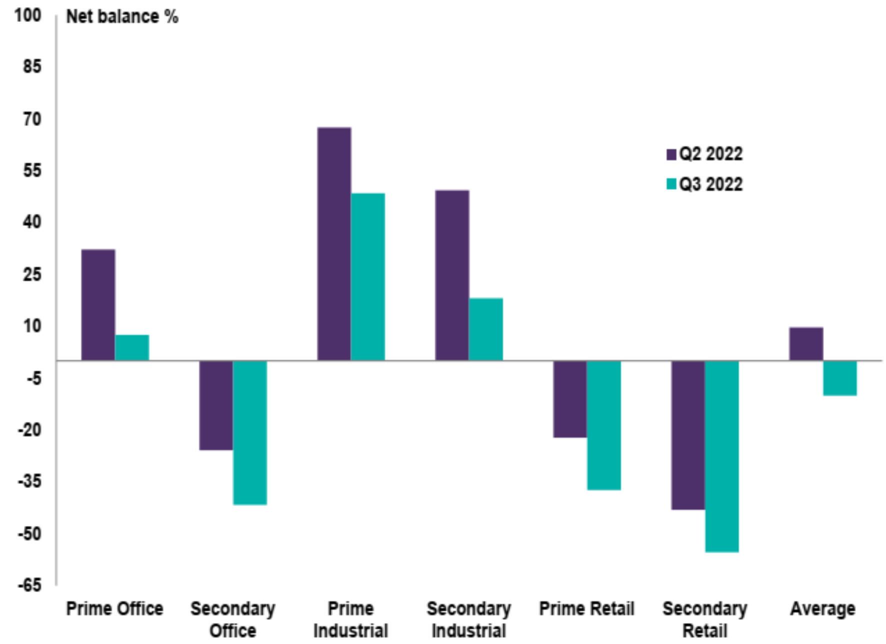
Many are struggling to manage creditors, with company insolvencies in England and Wales reaching their highest quarterly level since Q3 2009 in Q2 2022, driven by Creditors' Voluntary Liquidations.

…leading to pressures elsewhere

12-month capital value expectations



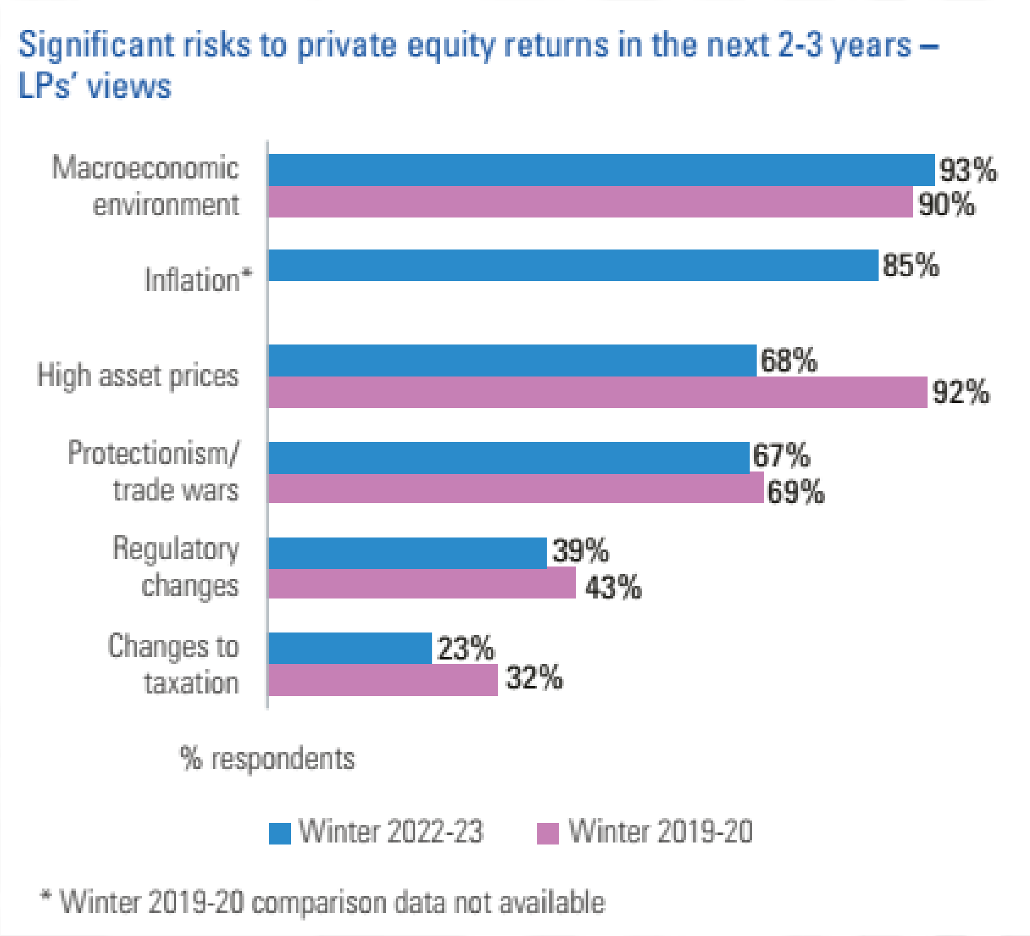
12-month rent expectations



Source: RICS

Commercial property yields have moved sharply upwards, both due to softening occupier demand and rapid rises in rates. Capital values have also decreased in turn, with a fall in capital values of -15% for industrials, -8.0% for retail and -7.4% for offices over the three months to October 2022.

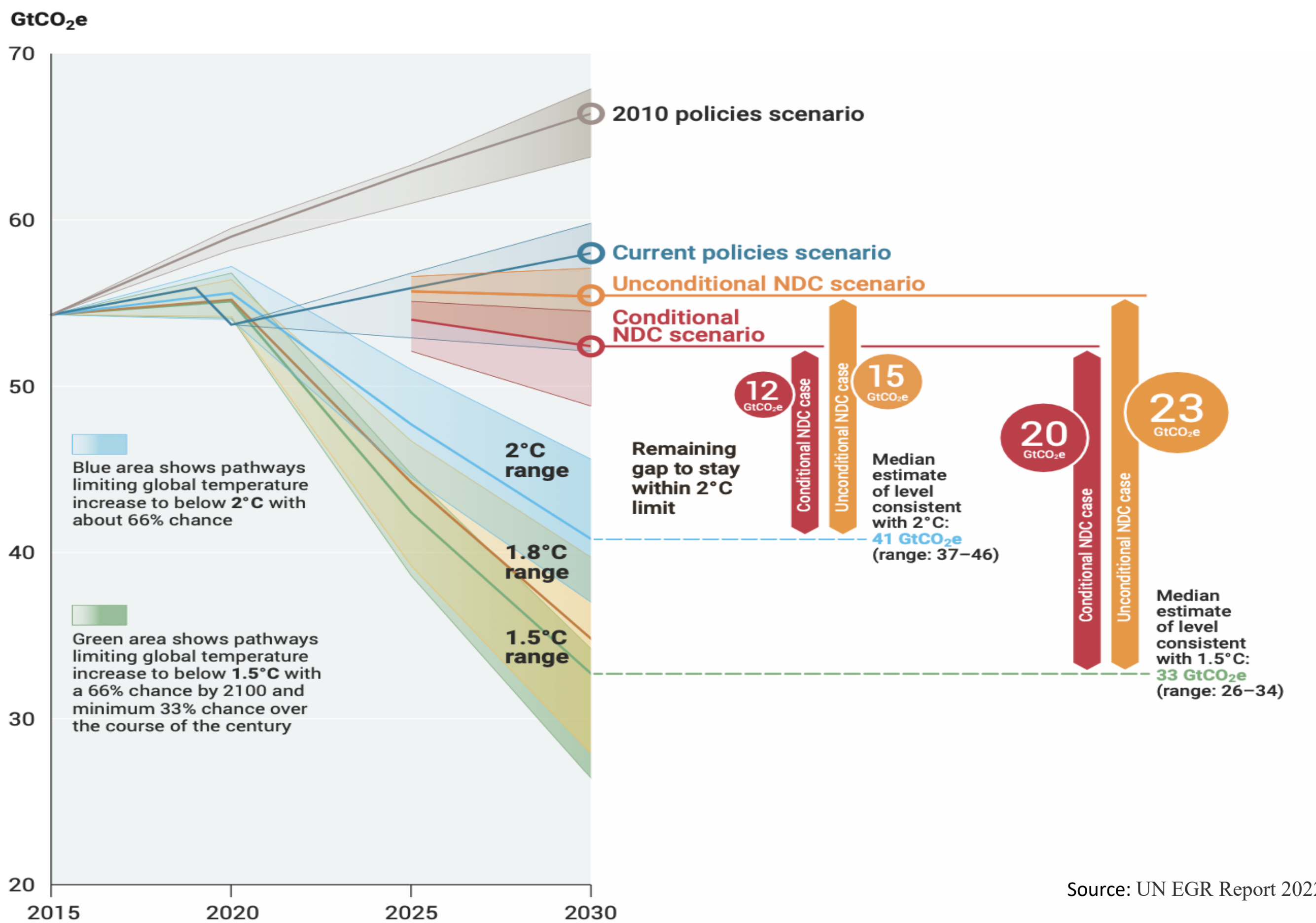
Private assets are not immune to this



Source: Coller Research Institute

Meanwhile, climate plans are going nowhere

Figure ES.3 Global GHG emissions under different scenarios and the emissions gap in 2030 (median estimate and tenth to ninetieth percentile range)

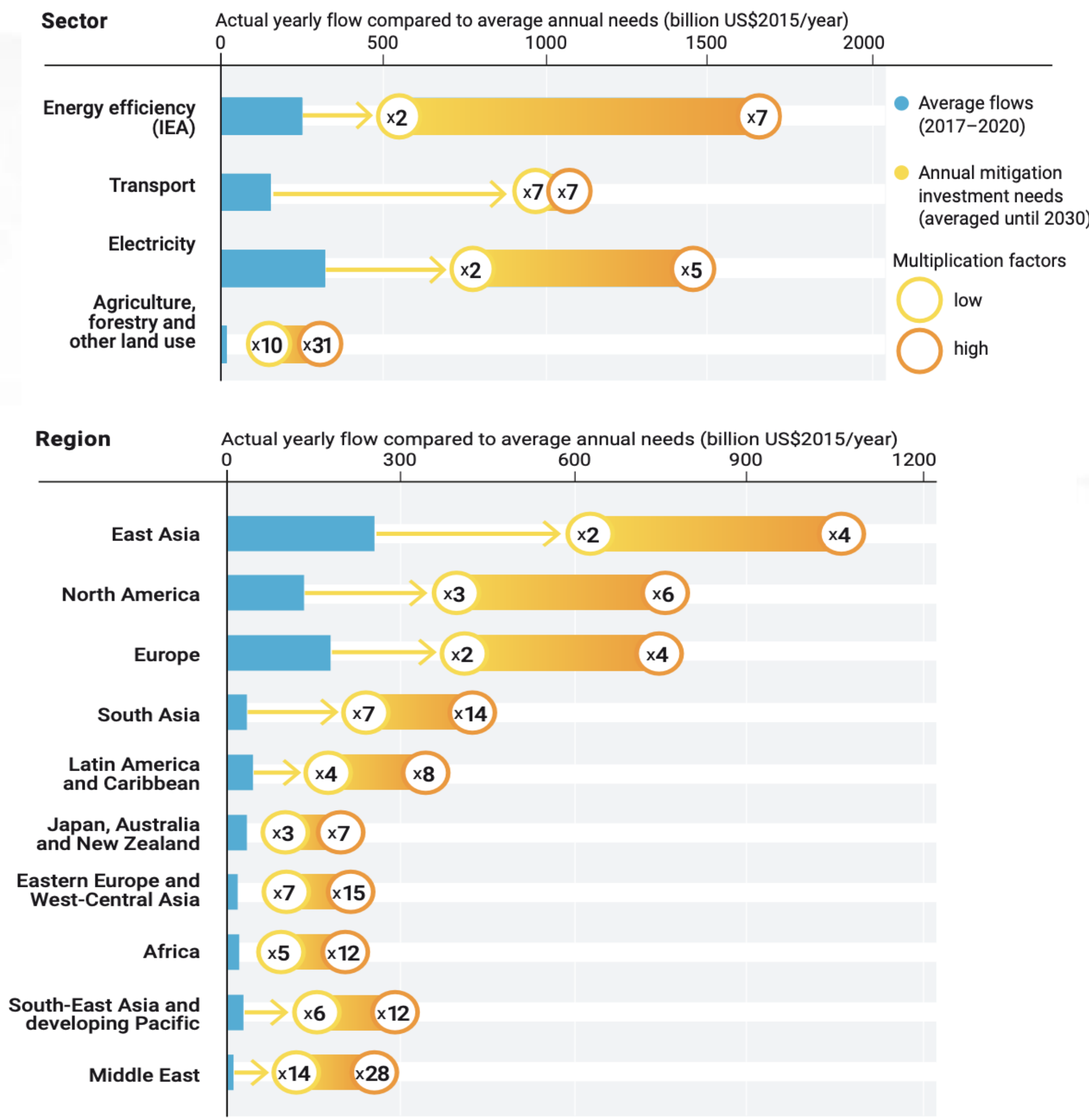


Source: UN EGR Report 2022

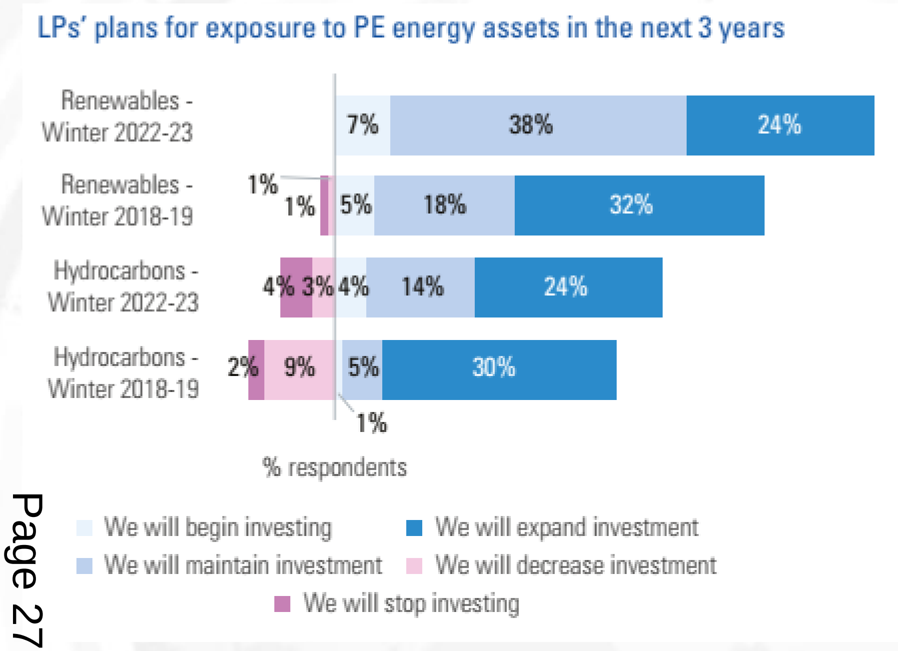
Current government climate policies leave the world on track to reach an average temperature rise of 2.8 degrees Celsius this century.

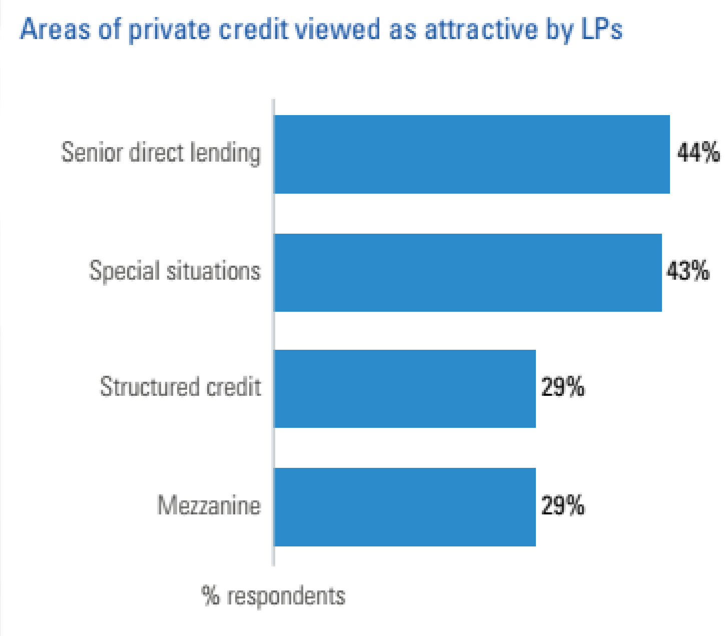
And significant monies are needed

- The financial system must overcome internal and external constraints to become a critical enabler of transformation across all sectors.
- A global transformation to a low-carbon economy is expected to require investments of at least $4-6 trillion a year. This is a relatively small (1.5-2 %) share of total financial assets managed, but significant (20-28 %) in terms of additional annual resources needed.



Where are allocations flowing?





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Source: Coller Research Institute

- More interest in renewables – and in hydrocarbons.
- Barbelling of risk appetite between protection (senior debt) and distressed value (special situations)
- Some investors have highlighted liquidity shortfalls will lead to reduction in the pace of commitments, indicating both continued stress as well as opportunity.

APPENDIX

Presenter Bio

Dr Bob Swarup is a respected international expert on financial markets, investment strategy, alternatives, ALM and regulation. He is Principal at Camdor Global Advisors, an advisory firm that works with institutions and investors around the world on strategic investment, risk management, ALM and business issues. He also served as Senior Investment Advisor to the Pensions Regulator, advising them on the development of the new regulatory framework for DB schemes from an investment, risk and governance perspective.

Bob was formerly a partner at Pension Corporation, a leading UK-based pension buyout firm, where he ran alternative investments, was Chief Risk Officer and oversaw Thought Leadership.

Bob is a former Senior Visiting Fellow at Cass Business School; on the Advisory Council of the Columbia Committee for Global Thought and on the Editorial Board of the *Journal of Alternative Investments*. He holds a PhD in cosmology from Imperial College London and an MA (Hons) in Natural Sciences from the University of Cambridge. Bob has written extensively on diverse topics, with his work being featured in the Financial Times, Economist, Guardian, CNBC, Bloomberg, Pensions Week and IPE amongst others. He is also the author of the internationally acclaimed bestseller *Money Mania* on two millennia of financial crises and the lessons to learn (Bloomsbury, 2014).

Contact Us

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Agenda Item 4

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Agenda Item 6

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Agenda Item 7

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Agenda Item 8

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