

# **Pension Fund Investment Sub-Committee**

## **Risk Monitoring**

14 September 2020

### **Recommendation**

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

### **1. Executive Summary**

- 1.1 The Fund needs to be aware of risks that could impact on its ability to function as intended. This report provides an update on the risks to the Fund and actions taken to manage them. It covers both the general risk register and the COVID-19 risk register.
- 1.2 The focus is on changes, developments, and management actions.
- 1.3 The 'Warwickshire Pension Fund (WPF) risk register' has the February 2020 risk assessment as its anchoring point. The Fund has a separate risk register relating to COVID-19 due to the multi-faceted and unique nature of the pandemic as a risk event. This takes March 2020 as its anchor point.

1.5 Table 1 below summarises the 'WPF risk register' and compares how risks have changed since the original assessment in February.

Ref	Description	Original Risk Assessment		Change		August 2020 Risk Assessment		Commentary of Direction of Travel From Pre-Lockdown Original Annual Risk Assessment to Quarter 2
		Gross Risk	Net Risk	Gross Risk	Net Risk	Gross Risk	Net Risk	
1	Long term returns fail to be in line with assumptions	6	3	6	3	12	6	Covid impact on markets
2	Short term falls in asset values	6	4	3	2	9	6	Covid impact on markets
3	Cashflow requirements cannot be met	12	6	-3	0	9	6	Cashflow plan is in place and experience to date is positive. Significant employer contribution prepayments are now much less likely.
4	Poor performance of actively managed funds	6	4	3	2	9	6	Covid impact on markets
5	Failure to realise pooling benefits	6	4	0	0	6	4	
6	Fraud	6	3	3	3	9	6	Covid impact on controls and on incentives to commit fraud
7	Liabilities increase further than assumptions	6	2	3	2	9	4	Very low risk free rates of return due to Covid impact on markets and economies will increase the valuation of long term liabilities  Impact of McCloud
8	Inadequate data quality	16	9	-4	-3	12	6	Successful delivery of 2019 valuation data set  Implementation of governance action plan
9	Employer contributions not being paid	12	9	0	0	12	9	No systematic problem yet presenting from employers but risk is still considered to be high so no change to scores
10	Fund reputation is harmed	9	6	0	0	9	6	
11	Loss of service provision due to disruption	4	3	0	0	4	3	
12	Lack of skills and knowledge	9	4	0	0	9	4	
13	Failure to meet governance standards	12	8	-3	-2	9	6	Implementation of governance action plan

Key: Low Moderate Significant

1.6 This indicates that the risk areas with net increases are:

- Risk 1 – Long term asset values – while these have rebounded in comparison to the end of March values, there is much uncertainty around the outlook for global markets. COVID-19, trade disputes (US-China as well as Brexit), and a changing geopolitical landscape may have longer term impacts on asset values. We will continue to try and limit the impact through an investment strategy that mitigates risk and takes a long-term view.
- Risk 2 – Short term asset values - This risk has materialised - there have been significant short-term reductions in asset values and high volatility in certain asset classes. These losses have not generally

crystallised to date as there has been no need to sell volatile assets under distress.

- Risk 4 – Active management – active managers may find it more difficult to add value through skill due to the unprecedented economic climate created by global responses to COVID-19. Equally, this may be an instance in which active managers have an increased ability to add value. The range of outcomes from displaying judgement are likely to have increased.
- Risk 6 – Fraud – Pension fund members are at higher risk of fraud from those seeking to take advantage of the uncertainty and worry of the Covid-19 pandemic.
- Risk 7 – Liabilities increase – the prospect of lower long-term government bonds (which indicate the 'risk free rate of return' used in valuation assumptions) means that the valuation of the Fund's liabilities may increase. To a certain extent this is a theoretical increase if members' longevity and benefit payments remain unchanged. However, it may impact on the Fund's funding strategy.

The government consultation on altering benefits in the period 2015 – 2022 following the recent McCloud judgement is under consultation. If enacted this will marginally increase the Fund's expected liabilities.

1.7 Table 2 below sets out the risks considered in the 'WPF COVID-19 risk register' and shows how the assessment has changed since March.

Ref	Description	Original Risk Assessment (March 2020)		Change		August 2020 Risk Assessment		Commentary of Direction of Travel From Original Covid Assessment to Quarter 2
		Gross Risk	Net Risk	Gross Risk	Net Risk	Gross Risk	Net Risk	
1	Cashflow - Delayed Employer Contributions	12	12	-3	-3	9	9	Experience to date has not presented any systematic issues with employer contributions
2	Cashflow - Investments Impact	16	12	-4	-3	12	9	Cashflow has remained relatively neutral and the cashflow strategy is working positively
3	Losses in Investment Values and Returns	16	12	-4	0	12	12	Risk remains high however the funding strategy does not assume high risk/return on investments
4	Governance Disruption	12	9	-6	-3	6	6	Implementation of governance review actions
5	Health and Safety of Members	12	6	0	0	12	6	Experience has been positive to date but no change in risk assessment. Uncertainty about the seasonal impact on mortality.
6	Health and Safety of Staff	16	9	-4	0	12	9	Likelihood of an issue is lower given experience to date, however potential impact remains high and net risk remains the same
7	Loss of continuity working with advisers, partners, fund managers, and Border to Coast	9	6	0	-2	9	4	Experience to date is that partners and external advisers have proved to be resilient
8	Administration Service Disruption	16	9	-4	-3	12	6	Implementation of governance review actions
9	Inability to Recover	9	6	0	0	9	6	Critical operations continue effectively, and this reduces the reliance upon recovery

1.8 Based on information experienced over the past few months, the Fund's view is that none of the risks considered have increased relative to expectations, and several have decreased. However, there remains significant uncertainty surrounding the nature of these risks, and many risks continue to be 'significant' or 'moderate'.

### Management Actions

1.9 The risk registers include management actions currently in place to mitigate risks as well as further risk mitigation actions to progress. Most actions are progressing broadly to plan, with a small number delayed or deferred.

## 2. Financial Implications

2.1 The actions identified will assist in mitigating financial risks to the fund.

## 3. Environmental Implications

3.1 Environmental concerns, including climate change, present risks to the Fund and these manifest in places in the risk register – for example having the potential to cause an impact on long term returns and an impact on the reputation of the Fund.

## 4. Supporting Information

4.1 The risk register scores set out above are based on the following convention:

- Gross risk – risk before mitigating actions
- Net risk – risk after mitigating actions

4.2 Risk probability and impact are classified into 4 categories as follows:

		Likelihood			
		Unlikely 1	Possible 2	Likely 3	Very Likely 4
Impact	Very High 4	4	8	12	16
	High 3	3	6	9	12
	Medium 2	2	4	6	8
	Low 4	1	2	3	4

4.3 Risk impact and likelihood are multiplied together to provide an overall risk score. Red risks are those with scores of 10 or higher, green risks have scores of 3 or lower, and the remainder are amber.

## 5. Timescales associated with the decision and next steps

5.1 Risks will continue to be monitored, with quarterly reporting to the PFISC.

## Appendices

Appendix 1 – WPF risk register

Appendix 2 – WPF COVID-19 risk register

## Background Papers

None.

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