TEESSIDE PENSION FUND COMMITTEE

A meeting of the Teesside Pension Fund Committee was held on Wednesday 15 March 2023.

PRESENT: Councillors Councillor David Coupe, (Chair), J Beall, A Bell, R Creevy, Ms J Flaws, Mr B Foulger, T Furness, S Hill, J Hobson, E Polano (Vice-Chair), J Rostron and Mr T Watson
Ms J Flaws, Mr B Foulger

ALSO IN ATTENDANCE: W Bourne (Independent Adviser), D Green (Hymans Robertson), A Owen (CBRE) and Kerr (Border to Coast)
P Mudd (XPS)
M Rutter (EY)

VIRTUAL ATTENDANCE: P Moon (Independent Adviser)

OFFICERS: Susan Lightwing, Nick Orton, Wendy Brown and Paul Mudd

APOLOGIES FOR ABSENCE: were submitted on behalf of Councillors D McCabe, G Nightingale and G Wilson

22/53 WELCOME, INTRODUCTIONS AND EVACUATION PROCEDURE

The Chair welcomed all present to the meeting and read out the Building Evacuation Procedure.

22/54 DECLARATIONS OF INTEREST

Name of Member	Type of Interest	Item/Nature of Interest
Councillor Beall	Non Pecuniary	Member of Teesside Pension Fund
Councillor Creevy	Non Pecuniary	Member of Teesside Pension Fund
Councillor Rostron	Non Pecuniary	Member of Teesside Pension Fund

22/55 MINUTES - TEESSIDE PENSION FUND COMMITTEE - 14 DECEMBER 2022

The minutes of the meeting of the Teesside Pension Fund Committee held on 14 December 2022 were taken as read and approved as a correct record.

22/56 INVESTMENT ACTIVITY REPORT

A report of the Director of Finance was presented to inform Members of the how the Investment Advisors' recommendations were being implemented.

A detailed report on the transactions undertaken to demonstrate the implementation of the Investment Advice recommendations and the Fund's valuation was included, as well as a report on the treasury management of the Fund's cash balances and the latest Forward Investment Programme.

The Fund continued to favour growth assets over protection assets and currently had no investments in Bonds.

At the June 2018 Committee it was agreed that a maximum level of 20% of the Fund would be held in cash. The cash level at the end of December 2022 was 8.37%.

Investment in direct property would continue on an opportunistic basis where the property had good covenant, yield and lease terms. The Fund had purchased two properties in the quarter at a total cost of £53 million.

Investment in Alternatives, such as infrastructure and private equity, offered the Fund diversification from equities and bonds. They came with additional risks of being illiquid, traditionally had costly management fees and investing capital could be a slow process. £89 million was invested in the quarter.

Appendix A to the submitted report detailed transactions for the period 1 October 2022 to 31 December 2022. There were net purchases of £144 million in the period, compared to net sales of £162 million in the previous reporting period.

As at 31 December 2022, the Fund had £414 million invested with approved counterparties. This was a decrease of £189 million over the last quarter. Appendix B to the submitted report showed the maturity profile of cash invested as well as the average rate of interest obtained on the investments for each time period.

The total value of all investments as at 31 December 2022, including cash, was £4,953 million, compared with the last reported valuation as at 31 March 2022, of £4,812 million.

A summary analysis of the valuation, attached at Appendix C to the submitted report, showed the Fund's percentage weightings in the various asset classes as at 31 December 2022 compared with the Fund's customised benchmark.

The Forward Investment Programme provided commentary on activity in the current quarter and looked ahead to the next three to five years. Details of the Strategic Asset Allocation agreed at the March 2021 Pension Fund Committee were shown at paragraph 8.2 of the submitted report.

It had been agreed by the Pension Fund Advisers and Fund Officers that there would be no changes to the Strategic Asset Allocation following the Actuarial Valuation. However it was acknowledged that work would continue to ensure the Fund's assets were more closely aligned to the strategic asset allocation. It was also acknowledged that there might be times in the short to medium term where the strategic allocation to a particular asset class was above the long term target. In any such case it should remain within the maximum level set out in the table at paragraph 8.2 of the submitted report.

At the end of 31 December 2022 the Fund's equity weighting was 60.2% compared to 58.3% at the end of September 2022. There were no plans to purchase or sell equities at this time. A summary of equity returns for the quarter 1 October 2022 to 31 December 2022 was shown at paragraph 8.4 of the submitted report.

To date the Fund had agreed three Local Investments. The Committee considered two further local investment proposals at its October 2022 and
December 2022 meetings, and agreed that due diligence should be carried out in relation to those proposals.

As at 28 February 2023 total commitments to private equity, infrastructure, other alternatives and other debt were approaching £1,675 million and a breakdown of that figure was included at paragraph 8.8 of the submitted report.

A Member requested information in relation to the Fund's exposure to tobacco companies in BCP and State Street.

ORDERED as follows:
1. That the report was received and noted.
2. Information detailing to the Fund's exposure to tobacco companies in Border to Coast and State Street would be provided.

22/57 **EXTERNAL MANAGERS' REPORTS**

A report of the Director of Finance was presented to provide Members with quarterly investment reports in respect of funds invested externally with Border to Coast Pensions Partnership Limited (Border to Coast) and with State Street Global Advisers (State Street).

As at 31 December 2022 the Fund had investments in the Border to Coast UK Listed Equity, Overseas Developed Markets and Emerging Markets Equity Funds. For all three sub funds the return target was expected to be delivered over rolling 3 year periods, before calculation of the management fee. The Fund also had investments in the Border to Coast Private Equity sub-fund and the Border to Coast Infrastructure sub-fund. To date, total commitments of £650 million had been made to these sub-funds (£350m to infrastructure and £300m to private equity) with around 28% of this commitment invested so far. In addition, a commitment to invest £80 million over a three year period to the Border to Coast Climate Opportunities Fund had been made. These investments were not reflected within the Border to Coast report attached at Appendix A to the submitted report but were referenced in the Border to Coast presentation at Agenda Item 11 of the meeting.

The Border to Coast report showed the market value of the portfolio as at 31 December 2022 and the investment performance over the preceding quarter, year, and since the Fund's investments began. Border to Coast had also provided additional information within an appendix to that report in relation to the Overseas Developed Markets Equity Fund, giving a breakdown of key drivers of and detractors from performance in relation to each of its four regional elements. Market background information and an update of some news items related to Border to Coast were also included. Border to Coast's UK Listed Equity Fund had achieved returns of 2.06% above benchmark over the last year, nearly meeting its 1% overachievement target. The Overseas Developed Markets Equity Fund had achieved returns of 2.02% above benchmark over the last year, comfortably above its 1% overachievement target, albeit in a falling market. Since inception, both Funds had delivered performance roughly in line with their targets. The performance of the Emerging Markets Equity Fund had been below benchmark throughout most of the period of the Fund's investment – performance over quarter and year to 31 December 2022 below target and below benchmark.

State Street had a passive global equity portfolio invested across four different region tracking indices appropriate to each region. The State Street report (attached at Appendix B to the submitted report) showed the market value of the State Street passive equity portfolio and the proportions invested in each region as at 31 December 2022.

State Street continued to include additional information with their report this quarter, giving details of how the portfolio compared to the benchmark in terms of environmental, social and governance factors including separate sections on climate and stewardship issues.

The latest report shows performance of the State Street funds against the revised indices – excluding controversies (UN Global Compact violators) and excluding companies that manufacture controversial weapons. As expected for a passive fund, performance closely matched the performance of the respective indices.

Appendix C to the submitted report contained the latest available ESG and carbon exposure in relation to the three Border to Coast listed equity sub-funds the Fund invested in. Amongst other information, the report included information on the highest and lowest ESG-rated companies within those Border to Coast sub-funds, together with an analysis of the carbon exposure of the sub-funds on a number of metrics. The sub-funds' ESG position and carbon exposure was also compared to benchmarks representing the 'average' rating across the investment universe
of that particular benchmark.

ORDERED that the report was received and noted.

22/58 **DRAFT ACTUARIAL VALUATION REPORT AS AT 31 MARCH 2022**

A report of the Director of Finance was presented to provide Members with a copy of the draft actuarial valuation report as at 31 March 2022. The draft actuarial valuation report was provided at Appendix A to the submitted report. The final valuation report would be published at the end of March 2023 and would set the employer contribution rates for scheme employers for the three year period starting 1 April 2023. The Actuary was present at the meeting and provided additional commentary.

Almost all scheme employers had already been provided details of how the valuation outcome would affect them, including details of their expected future employer contribution rate for the three year period from 1 April 2023. At the time of writing the report a small number of employer results were still being finalised - this might affect entries in the Rates and Adjustments certificate included within the report and the whole fund rate disclosed throughout the report. The actuary had confirmed they did not expect any changes to be significant or to materially impact the draft report as presented.

The valuation outcome at a whole Fund level had been positive, with the funding level improving slightly from around 115% to around 116%, largely because of investment returns significantly above the level forecast at the last valuation. Although the value of the Fund had increased by around £1 billion or 25% in the three years since the last valuation, an increase to the expected future inflation rate and a reduction in expected future investment returns had meant the value of liabilities and the future cost of providing scheme benefits had also increased significantly.

The main tax-raising employers in the Fund would see an increase in their employer contribution rate for the three years up to the next valuation. At the end of the three years their employer rates would have increased by 1.5% of pensionable pay. It was highlighted that these employers would still be paying some of the lowest employer contribution rates in the LGPS nationally, partly as a consequence of the Fund's ongoing funding surplus. As at the last valuation, prudence was being applied by the Fund by reducing expectations of the level of future investment returns.

The actuary would continue to work to complete the remaining individual employer outcomes and they would be issued as they were finalised. The final valuation report would be completed by 31 March 2023 and published on the Fund website, with a link circulated to all employers and other relevant parties including Committee and Teesside Pension Board Members.

ORDERED that the report was received and noted.

22/59 **REVISED FUNDING STRATEGY STATEMENT**

A report was presented, the purpose of which was to ask Members to approve a revised Funding Strategy Statement (FSS), a copy of which was attached at Appendix A to the submitted report.

The Fund actuary presented a report to the Committee at its meeting on 21 October 2022, setting out proposals to consult with the Pension Fund Employers on changes to the Funding Strategy Statement.

The revised FSS was in a more accessible format and took into account the changing regulations and environment the Fund worked in and also reflected the updated approach to funding working with the new Fund actuary (Hymans Robertson).

The most significant changes to the FSS included:

- Review of funding assumptions and approach
  The actuary had reviewed the funding approach and assumptions as part of the 2022 valuation. These had been updated to reflect Hymans Robertson's actuarial methodology, and emerging experience and market conditions as at 31 March 2022, The revised approach and assumptions were incorporated into the updated FSS.

- Climate risk
  The Fund recognised that climate change was a key risk due to the open-ended time horizons of the liabilities. As part of the modelling analysis for reviewing the Council's contribution strategy, the actuary had stress-tested the results under additional climate scenarios. The updated FSS included this ongoing work.

- Risk-based exit valuation approach
  The Fund had reviewed the approach to cessation valuations that were carried out when an employer left the Fund. The previous approach was closely tied to gilt yields on a particular day, an approach which introduced much volatility into cessation valuations over time. The revised approach was instead linked to the expected investment return of the assets held by the Fund, with a prudent level of risk incorporated for the protection of the Fund.

Concern was raised in relation to employees who were transferred via TUPE regulations where the new employer might subsequently decide to leave the Fund. It was clarified that employees who transferred to an admission body would have all the protections and that protection would follow them. The changes to the FSS would streamline some of those issues so that there would be less incentive for Employers to leave the Fund and no gain in the future.

All Fund employers were sent a copy of the revised draft FSS as part of the consultation process. A small number of employers responded, with one providing a detailed response. After careful consideration, it was felt no changes were required to the draft FSS following the consultation.

Once approved, the revised FSS would be published on the Fund's website.

ORDERED as follows that the:
1. Report was received and noted.
2. Revised Funding Strategy Statement was approved.

22/60 **PENSION FUND BUSINESS PLAN 2023-26**

The Head of Pensions Governance and Investment presented the annual Business Plan for the Fund.

The 2023/2024 forecast income and expenditure was set out in the Business Plan and summarised at paragraph 3.1 of the report.

A copy of the Business Plan for 2023/25 was attached at Appendix 1 to the submitted report and included:

- The purpose of the Fund, including the Teesside Pension Fund Service Promise (see Appendix A);
- The current governance arrangements for the Fund;
- The performance targets for the Fund for 2023/24, and a summary of the performance for 2022/23 (latest available) (see Appendix B);
- The arrangements in place for managing risk and the most up to date risk register for the Fund (see Appendix C);
- Membership, investment and funding details for the Fund;
- An estimated outturn for 2022/23 and an estimate for income and expenditure for 2023/24 (see Appendix D and page 21 of Appendix 1); and
- An annual plan for key decisions and a forward work programme for 2023/26 and an outline work plan for 2023 – 2026.

A Member requested a comparison between the previous management costs for the Fund and the costs since pooling. The Head of Pensions Governance and investment commented that it would be difficult to produce a comparison as the asset classes and style of investing had changed with pooling.

ORDERED as follows that the:
1. Report was received and noted.
2. Business Plan including the 2023/24 Pension Fund budget was approved.
3. A comparison of previous and present Fund management costs would be provided.

22/61 **INTERNAL AUDIT REPORTS**

A report of the Director of Finance was presented to provide Members with the outcome of two recent internal audit reports.

Middlesbrough Council's Internal Auditor, Veritau, carried out two planned audits of the Pension Fund's activities during the 2022/23 financial year, one covering investments and one covering administration. The reports and recommendations in respect of both audits were attached at appendices A and B to the submitted report.

Both audits had an overall audit opinion of "Substantial Assurance" and concluded that a sound system of governance, risk management and control existed, with internal controls operating effectively and being consistently applied to support the achievement of objectives in the area audited.

ORDERED that the internal audit reports were received and noted.

22/62 **BORDER TO COAST PRESENTATION**

The Committee received a presentation from the Customer Relationship Manager from Border to Coast which in relation to the following:

- Strategic Plan.
- Investments Summary.
- Equity Fund Performance.
- Alternatives Update.

It was five years since the launch of Border to Coast and the core building blocks that partner funds needed to implement their investment strategies were in place. Once of the key focus alongside building investment solutions was ensuring resilience by having the appropriate financial approach, employees and improving processes, technology and data. Economic conditions were difficult for organisations, there was greater regulation and an ever changing political landscape.

Details of BCP's key launches over the next three years were included on slide 6 of the presentation and other capabilities such as currency hedging were also being explored.

A new Stewardship Manager had been employed and a dedicated Climate Change Manager would also be joining BCP. The organisation continued to look for new talent.

A details overview of performance was provided and it was noted that whilst it was still too early to evaluate the success of private market strategies, three years in, every £1 invested now had a value of £1.38. Expectations to this point had been exceeded.

In relation to the recent collapse of the Silicon Valley Bank it was confirmed that BCP had no direct exposure.

ORDERED that the information provided was received and noted.

22/63 **INVESTMENT ADVISORS' REPORTS**

The Independent Investment Advisors had provided reports on current capital market conditions to inform decision-making on short-term and longer-term asset allocation, which were attached as Appendices A and B to the submitted report.

Further commentary was provided at the meeting.

William Bourne stated that inflation was slowly coming down due to central banks raising rates and stopping quantitative tightening. Japan, China and the UK had been pushing money into the system. However in the US Bond market the yield curve was inverted, which was a good indicator there was going to be a recession. It was less likely that interest rates would be raised as much as previously thought, due to the social aspects of a potential recession.

With regard to Bonds, they were now yielding about a 4% positive return and the Fund needed to consider this investment opportunity going forward.

Peter Moon commented on the Silicon Valley Bank collapse adding that despite the rapid action of the authorities there was still some concern for financial sectors.

Whilst the Fund's investment policy was potentially too growth orientated it was a struggle to find safe protection assets that will provide the required returns. The Fund should stay with its current policy in terms of weightings and cash and use equities to finance any excess demands on cash over time.

ORDERED that the information provided was received and noted.

22/64 **CBRE PROPERTY REPORT**

A report was submitted that provided an overview of the current property market and informed Members of the individual property transactions relating to the Fund.

Following valuation falls in Quarter 4 last year, the real estate market looked more positive. There were relatively low levels of activity in January 2023 and investors were attracted to lower pricing. Currently there were stable yields in industrial, stronger in retail, and stable in supermarkets. A more positive outlook was founded on the prime end of markets although there was activity in all sectors. Offices, high street shops and offices were all trending weaker compared with end of last year.

£3.2 billion had been invested in commercial property in January which was 64% down on the five year average. Although more investors were feeling more confident about investing in industrial and retail warehouse sectors, there was a perception that it had bottomed out. With realistic pricing and less competition, UK institutions were also looking more favourably on UK real estate and increased activity was anticipated in Quarter 2. It was likely that 2023 would be a year of two halves in terms of transactions. Increased competition for the lowest risk assets would see lower yield compression in the coming months.

There had been no sales during the period but the Fund had completed the purchase of two new assets in Quarter 4 of 2022.

The total Collectable Arrears on the entire portfolio was £256,995 as at 23 February 2023. This had now reduced to £206, 000. One of the tenants in arrears was due to sign a new lease next week and their arrears would be cleared at the same time.

The Fund's Real Estate Loan Portfolio currently had two committed loans total £35 million. All existing loans were performing in line with the loan agreements. All were covenant compliant and all interest and amortisation payments had been made on time.

ORDERED that the report was received and noted.

22/65 **XPS PENSIONS ADMINISTRATION REPORT**

A report was presented to provide an overview of administration services provided to the Teesside Pension Fund by XPS Administration.

The report provided information on the following:

- Overview
- Member Movement
- Member Self Service
- Pension Regulator Data Scores
- Customer Service
- Completed Cases Overview
- Completed Cases by Month
- Complaints.

The following issues were highlighted:

The LGA were working on guidance to assist administering authorities with McCloud data issues. The guidance would set out what options administering authorities in England and Wales might consider if they were unable to collect the data needed to implement the McCloud remedy. It would cover both missing data and data the authority was not confident was accurate. The Scheme Advisory Board (England and Wales) hoped to publish the guidance by the end of February 2023.

On 20 February 2023, H M Treasury (HMT) published a written ministerial statement confirming the rates of annual revaluation, earnings and pensions increase (PI) due to apply in April 2023 on 10.1%.

On 10 February 2023, the Department for Levelling Up, Housing and Communities (D LUHC) published a consultation and draft regulations on changing the annual revaluation date in the LGPS. If laid, the regulations would take effect from 31 March 2023. The proposed change in the revaluation date sought to bring in line the inflationary increases between the opening value of pension benefits and the annual CARE revaluation to remove the imbalance. Previously due to low inflation levels this imbalance has been low however due to this years unprecedented September CPI of 10.1% and imbalance of 7% this would see many more pension scheme members breach the Annual Allowance under current regulations. The outcome of the consultation was awaited.

There had been a reset on the dates for the Pensions Dashboard although this had not yet been confirmed. XPS had improving data quality for readiness and would continue as though the timescales had not moved. In readiness for the pensions dashboard, there was a minimum requirement pension schemes must be able to demonstrate against as required and defined by the Pensions Regulator. This standard was available to XPS through a product used by the central team and were currently undertaking a data mapping exercise in order to be able to carry out the necessary tests. Once this work had been completed, XPS would be able to report a data score in accordance with the Pensions Regulator standards.

With regard to Membership movement there had been increases in the numbers of Actives, Deferred and Pensioner members. There was a positive increase in cash flow from the Actives but more pensions in payment.

On the Completed Cases Overview, an error was highlighted in the column showing Cases Completed Outside Target. There were 3 cases and the Therefore the November monthly percentage was 98.4% and the average over the quarter was 99.6 %.

ORDERED that the report and information provided was received and noted.

22/66 **ANY OTHER URGENT ITEMS WHICH IN THE OPINION OF THE CHAIR, CAN BE CONSIDERED**

The Chair thanked Members, Officers and Advisors for their contributions to the Committee during the last four years.

22/67 **EXCLUSION OF PRESS AND PUBLIC**

ORDERED that the press and public be excluded from the meeting for the following items on the grounds that, if present, there would be disclosure to them of exempt information as defined in Paragraph 3, of Part 1 of Schedule 12A of the Local Government Act 1972 and that the public interest in maintaining the exemption outweighed the public interest in disclosing the information.

22/68 **BORDER TO COAST STRATEGY UPDATE**

The Committee received a Strategy Update from Border to Coast.

ORDERED that the report was received and noted.

22/69 **LOCAL INVESTMENT UPDATE**

The Committee received an update on due diligence that had been completed regarding a local investment.

ORDERED that the proposed local investment was not progressed.