TEESSIDE PENSION FUND COMMITTEE

A meeting of the Teesside Pension Fund Committee was held on Wednesday 14 December 2022.

PRESENT: Councillors D Coupe (Chair), A Bell, S Hill, J Hobson, E Polano (Vice-Chair), and G Wilson
Ms J Flaws and Mr T Watson

ALSO IN ATTENDANCE: W Bourne (Independent Adviser) and M Rutter (External Auditor) (Ernst Young)
P Mudd, XPS

VIRTUAL ATTENDANCE: Councillor R Creevy (Hartlepool Borough Council)
M Kerr (BCPP)
P Moon (Independent Adviser)
A Owen and G Rutter (CBRE)
J Baillie and V Batchler (Hymans Robertson)

OFFICERS: W Brown, S Lightwing and N Orton

APOLOGIES FOR ABSENCE: were submitted on behalf of Councillors J Beall, (Stockton Borough Council), T Furness, D McCabe, G Nightingale (Redcar and Cleveland Borough Council) and J Rostron

22/37 WELCOME, INTRODUCTIONS AND EVACUATION PROCEDURE

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

22/38 DECLARATIONS OF INTEREST

There were no declarations of interest received at this point in the meeting.

22/39 MINUTES - TEESSIDE PENSION FUND COMMITTEE - 21 OCTOBER 2022

The minutes of the meeting of the Teesside Pension Fund Committee held on 21 October 2022 were taken as read and approved as a correct record.

22/40 SUSPENSION OF COUNCIL PROCEDURE RULE NO 5

In accordance with Council Procedure Rule No 5, the Committee agreed to vary the order of business to deal with the items in the following order: Agenda Item 14, Agenda Item 15, Agenda Item 11, Agenda Items 5 to 10, Agenda Item 12 and Agenda Item 13.

22/41 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.

22/42 LOCAL INVESTMENT PROPOSAL

A report of the Director of Finance was presented to advise Members of a local investment proposal.

ORDERED as follows that:
1. the report was received and noted.
2. due diligence would be commissioned in respect of the local investment proposal.
3. a further report would be presented to a future Committee meeting with an investment recommendation informed by the due diligence.

22/43 **EXCLUSION OF PRESS AND PUBLIC**

ORDERED that the resolution excluding press and public ceased and the meeting was open to the press and public from this point forward.

22/44 **BORDER TO COAST RESPONSIBLE INVESTMENT, VOTING AND CLIMATE POLICIES**

A report of the Director of Finance was presented to advise the Committee of recent changes made by Border to Coast Pensions Partnership Limited ('Border to Coast') to its Responsible Investment Policy, Corporate Governance and Voting Guidelines and Climate Change Policy.

The revised Border to Coast documents were included as tracked changes versions in Appendices A, B and C attached to the submitted report.

Details of the key changes and a summary of the amendments were also provided in the submitted report.

ORDERED that Border to Coast Pensions Partnership Ltd's Responsible Investment Policy, Corporate Governance and Voting Guidelines and Climate Change Policy, as amended, were noted and approved by the Committee.

22/45 **INVESTMENT ACTIVITY REPORT**

A report of the Director of Finance was presented to inform Members of the Teesside Pension Fund Committee 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. For the period under discussion, bonds were still not considered value for the Fund, further comment was made under paragraph 8.5 of the submitted report in relation to future investments.

At the June 2018 Committee it was agreed that a maximum level of 20% of the Fund would be held in cash. Cash levels at the end of September 2022 were 11.51%.

Investment in direct property would continue where the property had good covenant, yield and lease terms. The Fund purchased a retail property in London – Zara, Covent Garden – at a purchase prices of £32 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. The Fund was underweight its customised benchmark and, providing suitable investment opportunities were available, would look to increase its allocation to this asset class up to the customised benchmark level. £110 million was invested in the quarter.

Appendix A to the submitted report detailed transactions for the period 1 July 2022 to 30 September 2022. There were net purchases of £162 million in the period, compared to net purchases of £131 million in the previous reporting period.

As at 30 September 2022, the Fund had £604 million invested with approved counterparties. This was a decrease of £120 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 30 September 2022, including cash, was £4,812 million, compared with the last reported valuation as at 31 June 2022, of £4,868 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 30 September 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 current 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 may 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.

W Bourne highlighted that currently the Fund had chosen to stay at the upper end of the risk level in order to keep contributions stable. If the Fund opted for lower risk investments, the contributions would have to rise.

At the end of September 2022 the Fund's equity weighting was 58.3% compared to 58.1% at the end of June 2022. There were no plans to purchase or sell equities at this time. A summary of equity returns for the quarter 1 July 2022 to 30 September 2022 was shown at paragraph 8.3 of the submitted report.

The Fund had no investments in bonds at this time, the level of cash invested is 11.51%. Discussions were held at the last Committee Meeting regarding investing in bonds. Although there was no directive to invest at that time, the Advisers had since indicated the levels at which they felt investment would be appropriate. Officers were monitoring the situation, and when the levels came into range would have further discussion with the Advisers. The current thinking was that an investment via the Border to Coast Sterling Index Linked Bond Fund would be the most appropriate vehicle.

To date the Fund had agreed three Local Investments. At the October Committee meeting it was agreed that a due diligence exercise would be carried out on a proposed Local Investment from FW Capital. The intention was to bring a report to the Committee in March 2023 for a decision.

As at 30 November 2022 total commitments to private equity, infrastructure, other alternatives and other debt were approaching £1,655 million and a breakdown of that figure was included at paragraph 8.8 of the submitted report.

ORDERED that the report was received and noted

22/46 **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 30 September 2022 the Fund had investments in the Border to Coast UK Listed Equity, Overseas Developed Markets Equity and Emerging Markets Equity sub funds. For all three sub funds the return target was an annual amount, expected to be delivered over rolling three 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. 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 7 of the meeting.

The Border to Coast report showed the market value of the portfolio as at 30 September 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 1.54% above benchmark over the last year, exceeding its 1% overachievement target, whereas the Overseas Developed Markets Equity Fund had achieved returns of 1.83% above benchmark over the last year, also comfortably above its 1% overachievement target, albeit for both Funds this was 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 the quarter to 30 September 2022 was above target, with the both the internal team and the external China managers contributing to this short term improvement in performance.

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 30 September 2022. Performance figures were also shown in the report over a number of time periods and from inception – the date the Fund started investing passively with State Street in that region. The nature of passive investment – where an index was closely tracked in an automated or semi-automated way – meant deviation from the index should always be low.

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. As the State Street investments were passive and closely tracked the appropriate regional equity indices, the portfolio's rating in these terms closely matched the benchmark indices ratings.

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: UK Listed Equity, Overseas Developed Markets Equity and Emerging Markets Equity. Amongst other information, the reports 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.

22/47 **PRESENTATION FROM BORDER TO COAST**

The Committee received a presentation from Border to Coast which included information in relation to the following:

- Recent Developments:
    - Border to Coast Update
    - Personnel Update
    - Fund Launch Pipeline
    - RI Policies Review
    - TCFD
- Investments Summary
- Equity Fund Performance
- Alternatives Update

The BCPP Adviser was asked how risk was allocated between the three managers in the hybrid Emerging Markets Fund. BCPP was not looking to take significant risk at a country level, most came from stock selection in that particular region. Most of the weights would be neutral versus benchmark. Exposure to China could be dialled down and there was some flexibility if there was a risk event. BCPP was mindful of the risks around China and this was one of the reasons they had restructured to have specialist China Managers who were on the

ground in the financial centres and emerging cities.
In relation to the current lock down in China due to the Covid-19 pandemic, whilst re-opening up of the economy should be positive from a growth perspective, there were questions around political stability and views.

It was noted that performance in the developed markets was good and the BCPP Adviser was asked why there were not more investments in that area. The investment philosophy of the team and the Fund since 2018 had always been to take small amounts of risk focussed on stock selection. The number of stocks since launch had been reduced from about 430 to 260 currently. This was still a reasonable amount of stocks but allowed the management team to focus on a smaller number of names. Active risk in the Fund had generally increased over the life of the Fund. Nevertheless, because of this strong track record, there was no need to take more risks to continue the performance. The externally managed global fund took more risk and aimed to deliver plus 2% and was currently outweighing that.

In relation to the performance of the unquoted alternative portfolio, the performance of private markets generally tended to lag public markets and BCPP expected to see some write downs of assets. This was not a widespread issue at the moment. In recent times coming through from Q3 BCPP would expect to see the IRI number come down slightly. However, over the life of the fund, BCPP felt that performance to June and the second half of the year was good.

ORDERED that the information provided was received and noted.

22/48 **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.

W Bourne highlighted that UK inflation was still at 11% and was a bit of an outlier in this, compared to the USA where inflation was reducing sharply. The markets were forecasting inflation to be 3% or 4% in a couple of years. In relation to Bond yields, the Bank of England would have to issue a lot of Bonds over the next few years. Financing the budget deficit and trying to get all the bonds it had bought back into the market at current bond prices would be difficult. Bond yields would rise over the next couple of years which would have implications for valuations. Bond yields were used to value long term cash flow and the valuations of all assets would reduce at some point.

The Fund was currently invested in infrastructure, equities and properties and it was likely they would all suffer. Whilst commitments had been made to private markets, a lot of the commitments had not been drawn down and the Fund could take advantage of new opportunities. However most of the investments the Fund had made were probably going to have less returns from over the next two years. The Fund needed to consider how to invest the 15% allocated to cash and bonds at some point.

P Moon stated that inflation was a real problem and core inflation at 6% would be difficult to stamp out. There would be a difficult financial environment for all types of asset classes for some time. Investing in alternatives would provide a decent return since there was a wider universe of investments to choose from. The Adviser stated that he was not averse to holding substantial amounts of cash at the moment given that the outlook for other investment types was not as good. Given that there was likely to be a further correction to come, now was not the right time to invest in Bonds. Index linked investments were currently the best option. Property was another area where the Fund could find some really good investments and spend some of the cash held to bring the level down.

ORDERED that the report was received and noted.

22/49 **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.

In terms of the economy and real estate market, 2022 had been a year of two halves. During the first half of the year there had been quite strong returns for real estate despite the energy crisis and rising inflation. The second half of the year had been weaker with yields increasing and values falling in all property sectors. Interest rates rising had made things difficult for debt backed buyers. There had been some cyclical selling of real estate as investors tried to rebalance portfolios. More recently there had been some structural changes mainly from defined benefit pension funds who were looking to reduce their exposure to real estate. The number of transactions had reduced during the second half of the year and yields in November were below the long term trend. There was an imbalance in the markets with sellers and buyers, and a number of real estate funds were selling. Debt backed buyers were mainly out of the market. Overseas buyers were still active and focussed mainly on central London. Pricing had softened and the number of competitive buyers had reduced from a year ago.

With regard to individual sectors, the value of industrial and logistics sheds had reduced the most during the second half of the year. Prior to that there had been the strongest demand for five or six years and the market had potentially got overheated. The retail sector had faired fairly well although traditional high streets and shopping centres continued to suffer. Supermarkets and out of town retail parks were trading well. In respect of the office sector, it was still too early to see the effect of home working and whether this trend would continue. The alternatives sector (anything not industrial, retail or office) had held up fairly well, for example student accommodation and health care.

In terms of inflation it may have peaked. Unemployment remained low and the labour market was competitive. Markets remained reasonably robust and given the imbalance in buyers and sellers there should be good opportunities in 2023.

During the last five months, the Fund had made three acquisitions:

- Zara/Vodaphone had completed in June and was trading very well. There was a lot of development work ongoing in the vicinity which would be advantageous in the longer term.

- A retail park in Tonbridge – a London commuter town. This was the only retail park in the area and rarely suffered any voids. Terms were agreed in May for a price of £27 million which had later been revised to £22 million and the purchase was completed at the end of October.

- An industrial unit in Swindon built in 2019 and let to Iceland. It was an ambient warehouse for dry goods. The unit was purchased for £31 million pounds which was less than an earlier agreed price. There was a 15 year lease subject to RPI reviews.

The asset management update was as per the report and the team had been very busy with rent renewals. Performance was positive across the board.

Finally the arrears were much improved from two years ago and were now down at less than a quarter of a million from over £2 million previously.

Overall it was a positive report and CBRE were pleased with the acquisitions.

ORDERED that the report was received and noted.

22/50 **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.

With regard to membership there had been a small drop in the number of active scheme members and a corresponding increase in deferred members. Numbers had increased again on the whole.

Self-service numbers remained low and ways to increase participation had been discussed. XPS had a quote in place to write to all active and pensioner members and provide them with a unique key and URL to access the website. To avoid additional postage costs work was ongoing to make the activation key available via the newsletter. The issue of how to contact those people who had deferred their pension also had to be addressed.

The website would be upgraded next year and allow scheme members to have more interactive ability within the site. As well as being able to look at contributions and payslips, XPS was considering whether members would be able to retire online as well. Online estimates could be produced and members able to choose to complete their paperwork online. Options would then be received by XPS more quickly. Whilst this would be an exciting improvement to the current website, it was highlighted that the existing paper based system for retirement options would still be available.

XPS continued to work on its data scores in readiness for the Pensions Regulator Dashboard in 2024. Data would be transmitted from XPS' internal dashboard to a national system which would enable people to look at all the pensions in once place online.

With regard to customer service, the next newsletter would contain details of an online survey for all scheme members to submit any feedback they had. An analysis of the survey responses would be provided to the Board and the Committee for discussion.

As part of the pensions remedy from the McCloud case, XPS Had been carrying out a data collection exercise with Employers. Once the new regulations were in place, XPS would write to scheme members to advise them of any changes due to their pensions. Members would not need to lodge a claim. It was anticipated that XPS would need to check a lot of pensions as part of remedy but the likelihood was that only a relatively small number would need amending.

XPS had also been working with the scheme actuary since January 2022 to ensure that all Employer data aligned well.

There had been one complaint in the last quarter.

The customer service data on page 179 of the agenda pack was queried as the responses were identical all the way through. The Officer agreed to check on the numbers to make sure the information was accurate.

ORDERED that the report was received and noted.

22/51 **VALUATION UPDATE**

A report was presented to update the Committee on progress on the ongoing triennial actuarial valuation of the Pension Fund as at 31 March 2022.

The Fund's Actuary, Hymans Robertson, had produced an update report (attached at Appendix A to the submitted report) that summarised some of the initial outcomes across Employers and considered how post valuation date events might impact on the result.

Hymans Robertson had also produced a document (attached at Appendix B to the submitted report) that summarised the main changes being made to the Funding Strategy Statement as a consequence of the actuarial valuation. This would be circulated to Employers with the revised Funding Strategy Statement as part of the consultation process.

ORDERED that the report was received and noted.

22/52 **ANY OTHER URGENT ITEMS WHICH IN THE OPINION OF THE CHAIR, CAN BE CONSIDERED**

None.