

CLWYD PENSION FUND COMMITTEE

Date of Meeting	Wednesday, 9th February 2022
Report Subject	Economic and Market update and Performance Monitoring report
Report Author	Head of Clwyd Pension Fund

EXECUTIVE SUMMARY

The purpose of this report is to update the Committee on the Economy and Markets, and the Performance of the Fund's investments.

The reports cover periods ending 31 December 2021, and are attached as appendices to this report.

Key points to note:

Economy and Markets

- Major equity markets including US, UK and European saw positive returns over Q4 2021, Japanese and Emerging Market Equities struggled over the period generating negative returns.
- Inflation continued to be a key threat in developed markets. The Bank of England responded by tightening the monetary policy and raising interest rates from 0.1% to 0.25%, the first rate rise since August 2018.
- In the US, projections by members of the Federal Open Market Committee pointed towards three lots of 0.25% increases in the federal funds rate in 2022.

Performance Monitoring Report

- Over the three months to 31 December 2021, the Fund's total market value increased by £102m to £2,484.6m
- Fund Performance over 3 months, 12 months and 3 years; +4.7%, +17.7% and +11.9% p.a. respectively.
- Fund Performance is ahead of Composite benchmark over all periods shown
- The Fund performance is comfortably ahead of the Strategic target and both Actuarial targets over all periods
- Asset classes are broadly in line with their strategic target weights, with the exception of the Private Market assets, which are still growing towards their strategic targets.

Performance of the Fund's assets are monitored and reviewed monthly by the Fund's Officers and advisers.

RECOMMENDATIONS

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| 1. | That the performance of the Fund over periods to the end of December 2021 are noted along with the Economic and Market update which effectively sets the scene. |
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REPORT DETAILS

1.00	INVESTMENT AND FUNDING RELATED MATTERS
1.01	<p>Economic and Market Update</p> <p>The economic and market update for the quarter from the Fund's Investment Consultant is attached at Appendix 1. The report contains the following key sections:</p> <ul style="list-style-type: none">• Economic and Market Background – an overview of markets in the quarter, including commentary on key economic indicators• Equity Market Review – information on the performance of equity markets during the quarter and key drivers of markets• Bond Market (Fixed Income) Review – provides an update on bond yield movements and interest rates for the period• Currencies, Commodities and Alternatives Review – provides an update on the performance of Sterling against other currencies as well as highlighting movements in major commodity and alternatives asset classes for the period
1.02	<p>The quarter was another generally positive one, with most major markets seeing positive returns. Inflation continued to be of concern with rates rising to 5.4% in December. The initial scare over the latest COVID-19 variant quickly dissipated as it appears to be neither as severe nor as vaccine resistant as initially feared. As a result, most countries have not imposed major restrictions. Equity investors continued to focus on the strong earnings outlook for the year ahead now that the economic recovery is less likely to be disrupted by COVID-19.</p> <p>Strong returns (+6.2%) were seen in Global equities over the quarter, with UK equities also performing well; returning +4.2%.</p> <p>In the UK Government Bond yields fell over the quarter, resulting in positive returns from long dated fixed interest gilts of +5.6%.</p> <p>Sterling rose against the US Dollar, Euro and the Yen over the quarter.</p> <p>Commodities markets continued their growth with another positive return, albeit less strong than previous quarters, returning 1.1%.</p> <p>A verbal update will be provided to Committee to provide an update to market movements since the writing of this report.</p>

1.03	<p>Performance Monitoring report</p> <p>Over the three months to 31 December 2021, the Fund’s total market value increased by £102m to £2,484.6m</p> <p>This means that the Total Fund has increased in value by £362.9m in the calendar year 2021.</p>																								
1.04	<p>It is appropriate to measure performance at a Total Fund level by comparing to a number of different targets:</p> <ul style="list-style-type: none"> • The first of these is the assumed return that the Actuary includes within the triennial valuation - Actuarial Target. This is the most crucial target as actual performance needs to be ahead of this to ensure that the Fund maintains, or improves its funding level. This currently set at CPI (Consumer Price Index) +1.75% p.a. for past service liabilities and CPI + 2.25% for future service liabilities. • The second performance measure is the overall assessment of potential return when the Fund reviews and sets its investment strategy – Strategic Target. (This is currently CPI +3.4% p.a.) • The final target is the composite benchmark – Total Benchmark. This is a composite of each of the individual manager benchmarks, weighted by strategic target allocation. For most investment managers the benchmark does not include an expectation of outperformance, with the exception of Wellington Emerging Market equities and WPP Global Opportunities equity. <p>The performance against all benchmarks is shown on Page 6 of the report, and repeated below:</p> <table border="1" data-bbox="320 1198 1326 1574"> <thead> <tr> <th></th> <th>Quarter (%)</th> <th>1 Yr (%)</th> <th>3 Yrs (%)</th> </tr> </thead> <tbody> <tr> <td>Total</td> <td>4.7</td> <td>17.7</td> <td>11.9</td> </tr> <tr> <td>Total Benchmark</td> <td>4.2</td> <td>13.2</td> <td>10.4</td> </tr> <tr> <td>Strategic Target (CPI +3.4% p.a.)</td> <td>1.3</td> <td>5.5</td> <td>5.5</td> </tr> <tr> <td>Actuarial Target – Past Service Liabilities (CPI +1.75% p.a.)</td> <td>0.9</td> <td>3.8</td> <td>3.8</td> </tr> <tr> <td>Actuarial Target – Future Service Liabilities (CPI +2.25% p.a.)</td> <td>1.1</td> <td>4.3</td> <td>4.3</td> </tr> </tbody> </table> <p>The table shows strong outperformance by the Fund against all measures over 3 months, 1 year and 3 years periods.</p>		Quarter (%)	1 Yr (%)	3 Yrs (%)	Total	4.7	17.7	11.9	Total Benchmark	4.2	13.2	10.4	Strategic Target (CPI +3.4% p.a.)	1.3	5.5	5.5	Actuarial Target – Past Service Liabilities (CPI +1.75% p.a.)	0.9	3.8	3.8	Actuarial Target – Future Service Liabilities (CPI +2.25% p.a.)	1.1	4.3	4.3
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1.05	<p>The strongest absolute returns over the quarter came from the Cash and Risk Management Framework (CRMF), Private Markets and Tactical Allocation (Best Ideas) portfolio. The CRMF returned +10.7%, Private markets returned +4.6% and Tactical Allocation portfolio returned 3.8%.</p> <p>Within Private Markets the strongest returns were seen in the Local/Impact and Private Credit portfolios with returns of +7.6% and +5.9% respectively.</p> <p>The BlackRock ESG Equity portfolio generated another strong quarter of performance, returning +6.8%.</p>																								

	<p>In the 12 months to 31 December 2021, the best returns came from the CRMF, Private Markets and Tactical Allocation portfolio. The CRMF returned +33.6%, with Private Markets and the Tactical Allocation portfolio returning +22.4% and +16.4% respectively.</p> <p>The performance of individual managers is shown in the report and is regularly reviewed by Officers and advisers, and at this stage there are no concerns that need addressing, however all positions are being monitored closely.</p>
1.06	<p>The transition of assets in the summer of 2021 brought most asset classes in line with the target strategic weights. Due to strong performance of listed developed market equities in the quarter, Global equity remain marginally overweight. As a result the Private Markets assets are now nearly 4% under target weight, although this is well within the agreed strategic tolerance, and a work plan is in place to bring this in line over the next couple of years. All other asset classes are well within the agreed strategic ranges.</p>
2.00	RESOURCE IMPLICATIONS
2.01	<p>None directly as a result of this report.</p>
3.00	CONSULTATIONS REQUIRED / CARRIED OUT
3.01	<p>None directly as a result of this report.</p>
4.00	RISK MANAGEMENT
4.01	<p>The Fund's investment strategy has been designed to provide an appropriate trade-off between risk and return. The Fund faces three key investment risks: Equity risk, Interest Rate Risk and Inflation Risk.</p> <p>Diversification of the Fund's growth assets away from equities seeks to reduce the amount of the equity risk (though it should be recognised that Equities remain an important long term source of expected growth). The implementation of the Fund's De-Risking Framework (Flightpath) has been designed to mitigate the Fund's Interest Rate and Inflation Risks.</p>
4.02	<p>This report addresses some of the risks identified in the Fund's Risk Register. Specifically, this covers the following (either in whole or in part):</p> <ul style="list-style-type: none"> • Governance risk: G2 • Funding and Investment risks: F1 - F6 •
4.03	<p>The Flightpath Strategy manages/controls the interest rate and inflation rate impact on the liabilities of the Fund to give more stability of funding outcomes and employer contribution rates. The Equity option strategy will provide protection against market falls for the synthetic equity exposure via the Insight mandate only. The collateral waterfall framework is intended to increase the efficiency of the Fund's collateral, and generating additional yield in a low governance manner. Hedging the currency risk of the market value of the synthetic equity portfolio will protect the Fund against a strengthening pound.</p>

5.00	APPENDICES
5.01	Appendix 1 - Economic and Market Update – 31 December 2021 Appendix 2 – Performance Monitoring Report – 31 December 2021
6.00	LIST OF ACCESSIBLE BACKGROUND DOCUMENTS
6.01	Economic and Market Update and Investment Strategy and Manager Summary 31 December 2021. Contact Officer: Philip Latham, Head of Clwyd Pension Fund Telephone: 01352 702264 E-mail: philip.latham@flintshire.gov.uk
7.00	GLOSSARY OF TERMS
7.01	<p>A list of commonly used terms are as follows:</p> <p>(a) Absolute Return – The actual return, as opposed to the return relative to a benchmark.</p> <p>(b) Annualised – Figures expressed as applying to 1 year.</p> <p>(c) Duration – The weighted average time to payment of cash flows (in years), calculated by reference to the time and amount of each payment. It is a measure of the sensitivity of price/value to movements in yields.</p> <p>(d) Market Volatility – The impact of the assets producing returns different to those assumed within the actuarial valuation basis, excluding the yield change and inflation impact.</p> <p>(e) Money-Weighted Rate of Return – The rate of return on an investment including the amount and timing of cash flows.</p> <p>(f) Relative Return – The return on a fund compared to the return on index or benchmark. This is defined as: Return on Fund minus Return on Index or Benchmark.</p> <p>(g) Three-Year Return – The total return on the fund over a three year period expressed in percent per annum.</p> <p>(h) Time-Weighted Rate of Return – The rate of return on an investment removing the effect of the amount and timing of cash flows.</p> <p>(i) Yield (Gross Redemption Yield) – The return expected from a bond if held to maturity. It is calculated by finding the rate of return that equates the current market price to the value of future cash flows.</p> <p>A comprehensive list of investment terms can be found via the following link: https://www.schroders.com/en/uk/adviser/tools/glossary/</p>