



# SURREY PENSION FUND COMMITTEE REPORT

**SURREY COUNTY COUNCIL**

**SURREY PENSION FUND COMMITTEE**

**DATE: 13 DECEMBER 2024**

**LEAD OFFICER: NEIL MASON, LGPS SENIOR OFFICER**

**SUBJECT: INVESTMENT MANAGER PERFORMANCE AND ASSET/LIABILITIES UPDATE**

## **SUMMARY OF ISSUE:**

This report is a summary of manager issues for the attention of the Pension Fund Committee, as well as an update on investment performance and the values of assets and liabilities.

## **RECOMMENDATIONS:**

It is recommended that the Pension Fund Committee:

1. Note the findings of the report in relation to the Fund's valuation and funding level, performance returns and asset allocation.
2. Acknowledge the Fund winning the Pensions for Purpose Impact Investing Principles Adopter award.

## **REASON FOR RECOMMENDATIONS:**

To assess and acknowledge performance of the Fund's investment managers against the Fund's target returns, and whether it is meeting its Strategic Investment objective.

## **DETAILS:**

Fund award success

1. In October 2024, the Fund was short-listed for Best Investment Innovation award at the annual LAPF Investment Awards. This was due to process innovation for the Fund's increasingly complex private markets programme.
2. In October 2024, the Fund won the Impact Investing Principles Adopter award from Pensions for Purpose given the Fund's commitment to continuously improve its Responsible Investment approach and the setting of a Net Zero date.

Funding Level

3. The funding level is derived as the ratio of the value of the Fund's assets to the value of its liabilities. The Fund's liabilities are the future benefit

payments due to members in respect of their service accrued in the Fund. The Fund's assets are used to pay member benefits accrued to date.

4. For the purpose of providing the quarterly funding updates following the 2022 valuation, it is appropriate (and the Fund Actuary's recommendation) that the 70% level of prudence remains fixed in the determination of the discount rate. This dynamic discount rate each quarter-end would therefore reflect the change in investment return expectations since the 2022 valuation date.
5. Assessing the liabilities using the dynamic discount rate also ensures that the factors leading to a change in asset values are being reflected in liability values. There is not a direct relationship (ie assets and liabilities do not react in the exact same way to changes in market conditions) but measuring the liabilities using the dynamic discount rate means that the assets and liabilities are being measured on a consistent market basis over time.
6. Results and assumptions when using a dynamic discount rate are in the table below.

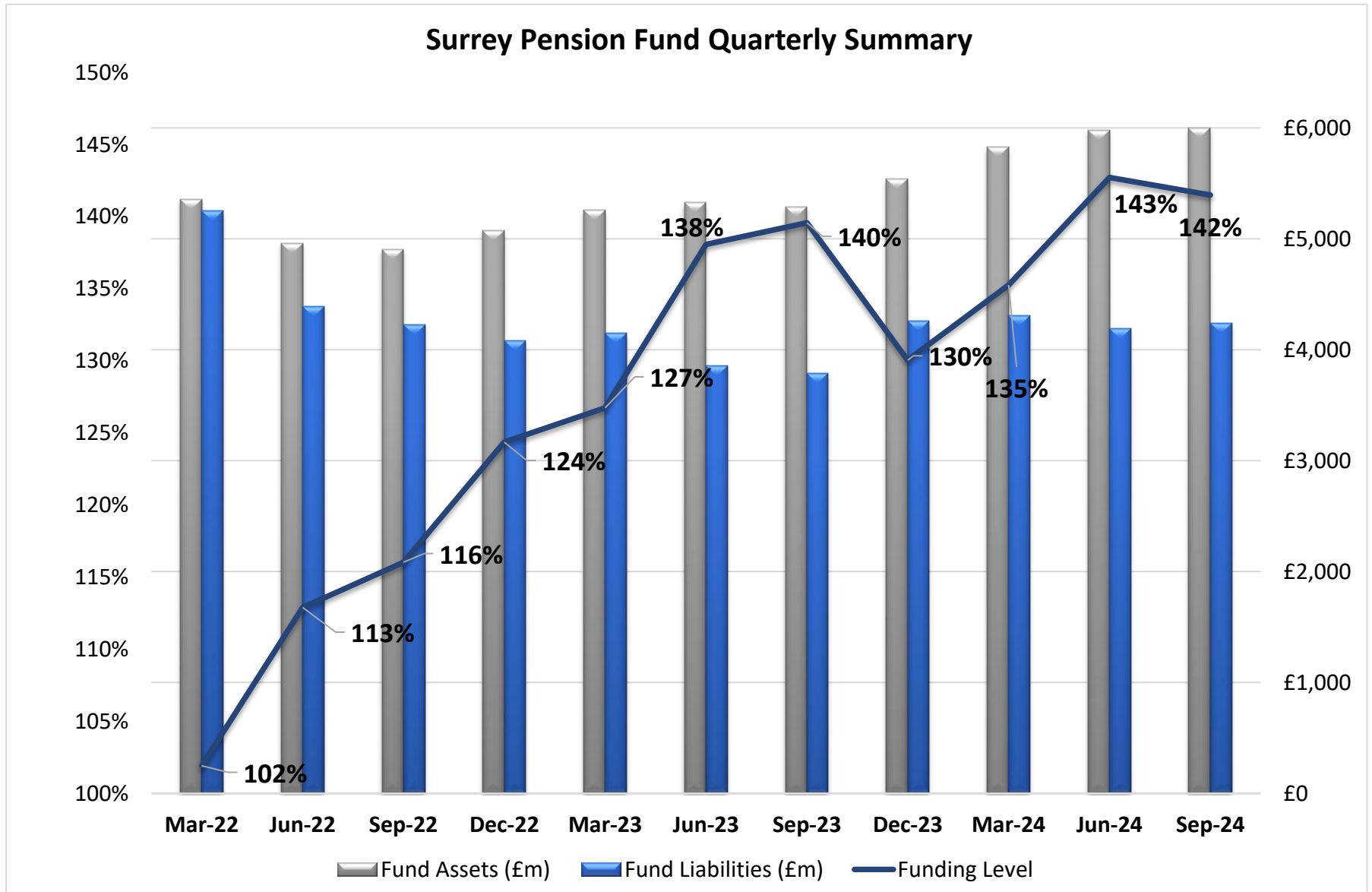
<b>Dynamic Discount Rate Table</b>	<b>31 March 2022</b>	<b>30 June 2024</b>	<b>30 Sep 2024</b>
Assets (£bn)	5.36	5.98	6.00
Past Service Liabilities (£bn)	5.26	4.19	4.24
Surplus (£bn)	0.10	1.79	1.76
Funding Level	102%	143%	142%
Discount Rate	4.4%	6.5%	6.4%
Salary Increases	3.7%	3.3%	3.3%
Pension Increases	2.7%	2.3%	2.3%
Likelihood of success	70%	70%	70%
Required return to be 100% funded	4.3%	4.4%	4.4%

7. The liability values in the above table as at 30 June 2024 and 30 September 2024 make allowances for both the April 2023 Pension Increase Order of 10.1% and the April 2024 Pension Increase Order of 6.7%.
8. The funding level has remained stable over the quarter from 30 June 2024. Investment performance has been positive (with the Fund achieving a return of 1.17% over the quarter) and higher liabilities have broadly offset one another.
9. The net position has slightly decreased to a surplus of £1.76 at 30 September 2024.

10. The improvement in the funding level since the 2022 valuation, whilst welcome, is primarily due to an increase in the expected rate of future investment returns, i.e. the discount rate. In the absence of these higher return expectations, it is likely that the funding level would have fallen since the 2022 valuation due to higher-than-expected inflation experience. To illustrate this, the required return (the level of returns required to ensure the Fund remains 100% funded) is slightly higher as at 30 September 2024 (4.4%) than it was as at 31 March 2022 (4.3%) i.e. higher asset returns are now required to maintain a funding level of 100%.
11. For comparison, the actuaries have also estimated the updated funding position of the Fund as 30 September 2024 based on the fixed discount rate of 4.4%, which was set at the 31 March 2022 valuation, results of which are shown in the table below.

<b>Static Discount Rate Table</b>	<b>30 Sept. 2024</b>
Assets (£bn)	6.00
Past Service Liabilities (£bn)	5.97
Surplus (£bn)	0.03
Funding Level	101%
Discount Rate	4.4%
Salary Increases	3.3%
Pension Increases	2.3%
Likelihood of success	88%

12. The graph below shows the development of the funding ratio since the last valuation.



## Market Review

13. Global equity markets rose over the quarter, rallying to all-time highs by the end of September. The key drivers were easing inflation figures in the US, a 50-basis-point (bps) interest rate cut by the US Federal Reserve (Fed) and continued optimism over advancements in artificial intelligence (AI).
14. US equities rose, with the S&P 500 trading at new highs. US inflation eased, landing at 2.5% in August, down from 3.0% in June. The Fed was expected to cut interest rates but the scale was somewhat surprising, which contributed to the market's rally. Meanwhile, data suggested US growth was decelerating rather than contracting. The US economy added 142,000 jobs in August, more than the 89,000 in July. The US composite purchasing managers' index (PMI), which came in at 54.4 in September, showed business growth remaining robust (a figure above 50 indicates expansion).
15. European shares rose over the quarter, chiefly influenced by the outlook for the US's economy and interest rates. Euro area inflation fell to 2.2% in August, and the European Central Bank cut its deposit rate by 25bps in September in its second rate cut of the cycle. The composite PMI for the eurozone fell to 48.9 in September, compared with 51.0 in August, which represented the lowest reading since January and the first fall in private sector activity in seven months. Political turbulence took its toll on sentiment as hard-right and hard-left parties performed well in elections across the continent.
16. UK equities were marginally higher but underperformed global equities. Inflation was flat at 2.2% in August, as expected. Retail sales grew by 1.0% month-on-month in August. However, GfK's Consumer Confidence Index fell from -13 in August to a worse-than expected -20 in September reflecting negative comments from the new Government ahead of the Autumn Budget.
17. Asia Pacific ex Japan was the best-performing region; China's stock markets soared on the government announcement of a raft of stimulus measures intended to boost the economy. Japan was the worst performer. Tokyo's stock market was hit hard by the fallout of an unexpected interest rate rise by the Bank of Japan in July.
18. Government bond yields fell, and so prices rose, over the quarter. Benchmark 10-year yields in the US, the UK, Germany and Japan all ended the quarter lower.
19. Yields on 10-year US treasuries fell from 4.37% to 3.78%. Notably, the US yield curve ended its inversion towards the end of the period, with 10-year treasuries once again yielding more than two-year bonds.
20. Ten-year gilt yields fell from 4.17% to 4.01%. Spreads between shorter- and longer-dated gilts tightened. The Bank of England cut interest rates by 25bps in August and left rates unchanged at its September meeting.

21. The quarter saw yields on global credit fall in the US, the eurozone and the UK. Bond prices consequently rose. Credit spreads generally tightened, but widened in the UK.
22. The US dollar fell against sterling, the euro and the Japanese yen as the Fed made its larger than expected interest rate cut, leading some analysts to believe rates could move another 75bps lower by year end.
23. The Japanese yen rose against the US dollar, the euro and sterling after the unexpected rate rise. Elsewhere in Asia, the Chinese yuan strengthened versus the US dollar on the back of domestic Chinese stimulus.

#### Performance Review

24. Overall, the Fund slightly outperformed the benchmark, returning 1.17% in Q2 2024/25 (July-September 2024), compared to the benchmark of 1.04%.
25. On an absolute basis and relative to benchmark, BCPP Multi-Asset Credit (MAC) and BCPP Listed Alternatives were the best performing funds. Both funds reacted positively to rate cut expectations and growing confidence in a soft economic landing rather than a recessionary period, especially in the US. Credit yields fell and spreads tightened, supporting MAC investments and real estate and private market exposures in Listed Alternatives. BCPP UK Equity Alpha also outperformed over this period as smaller capitalisation companies outperformed, supported by a number of corporate takeovers approaches.
26. This outperformance was offset by underperformance from private markets, BCPP Emerging Markets (EM) Alpha, CBRE Real Estate and BCPP Global Equity Alpha. Other than BCPP EM Alpha, these funds also saw absolute falls in value.
27. Private markets fell 4.9% over the period in absolute terms. The US dollar was down 5.8% versus the pound over the period and the majority of the private market allocations are in dollars. The euro was also down 1.5%.
28. BCPP EM Alpha underperformed primarily due to two impacts related to the Chinese exposure. First, BCPP sold the overweight position to China before the Chinese authorities initiated a stimulus package that drove the Chinese equity market higher. Second, the remaining Chinese exposure underperformed significantly as the market rally took the largest companies, especially those in the consumer sector, higher, whilst the fund's exposure is more through smaller companies and away from this sector. The latter issue of company size has been a common theme across all BCPP funds, negatively impacting performance.
29. CBRE Real Estate underperformed the benchmark over the quarter. The most significant negative impact was currency as the US dollar weakened against sterling, reducing the value of some assets in sterling terms. The weakest underlying asset performance came from Nuveen UK Shopping

Centre Fund which realised a significantly lower asset value when it sold the Princesshay Shopping Centre in Exeter.

30. BCPP Global Equity Alpha continued its run of underperformance, underperforming the benchmark by 1.05%. The fund has underperformed the benchmark by -5.76% and its target by -7.76% over the last 12 months. Previously, the underperformance was due to an underweight position to the largest US technology companies that have performed very well. On this occasion that positioning was actually beneficial but the underlying managers and their style combinations still produced a negative outturn. A more detailed review of BCPP Global Alpha is contained in paper 14 – Global Alpha Equity Review (Part 2).

## Fund Performance – Summary of Quarterly Results

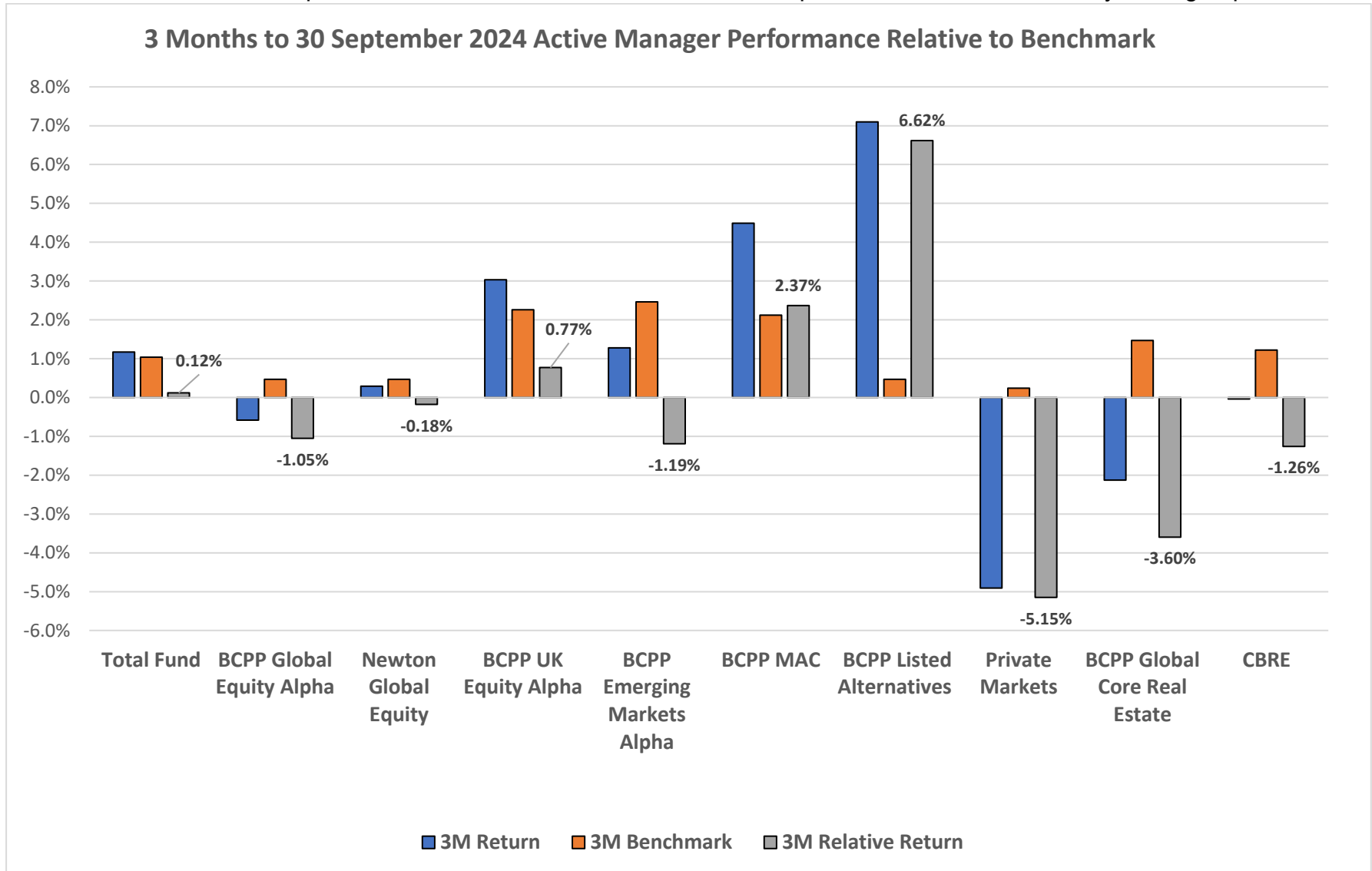
31. The table below shows manager performance for Q2 2024/25 (June - September 2024), net of investment manager fees, against manager specific benchmarks using Northern Trust data.

As at 30 September 2024	£m	3M Return	3M Benchmark	3M Relative Return	1Y Return	1Y Benchmark	1Y Relative Return	3Y Return	3Y Benchmark	3Y Relative Return
<b>Total Fund</b>	<b>6,038.33</b>	1.17%	1.04%	0.12%	13.60%	16.47%	-2.87%	4.24%	6.48%	-2.24%
<b>Active Global Equity</b>	<b>1,339.3</b>	-	-	-	-	-	-	-	-	-
BCPP Global Equity Alpha	873.3	-0.58%	0.47%	-1.05%	14.13%	19.89%	-5.76%	6.89%	8.28%	-1.38%
Newton Global Equity	466.1	0.29%	0.47%	-0.18%	22.59%	19.89%	2.70%	9.39%	8.28%	1.11%
<b>Active Regional Equity</b>	<b>694.5</b>	-	-	-	-	-	-	-	-	-
BCPP UK Equity Alpha	393.9	3.03%	2.26%	0.77%	13.52%	13.40%	0.12%	2.82%	7.41%	-4.60%
BCPP Emerging Markets Alpha	300.6	1.28%	2.46%	-1.19%	12.49%	14.70%	-2.21%	-	-	-
<b>Passive Global Equity</b>	<b>1,391.7</b>	-	-	-	-	-	-	-	-	-
LGIM - Future World Global	1,391.7	0.81%	0.74%	0.08%	21.93%	21.57%	0.36%	-	-	-
<b>Passive Regional Equity</b>	<b>127.8</b>	-	-	-	-	-	-	-	-	-
LGIM - Europe Ex-UK	61.1	0.25%	0.22%	0.03%	12.14%	15.35%	-3.21%	5.16%	6.26%	-1.10%
LGIM - Japan	19.5	0.64%	0.68%	-0.03%	10.67%	10.67%	0.00%	3.18%	3.19%	-0.01%
LGIM - Asia Pacific ex-Japan	47.2	1.56%	1.48%	0.08%	10.59%	10.61%	-0.03%	1.84%	1.91%	-0.07%
<b>Fixed Income</b>	<b>1,011.0</b>	-	-	-	-	-	-	-	-	-
BCPP MAC	886.6	4.49%	2.12%	2.37%	13.67%	8.88%	4.79%	-	-	-
LGIM - 15 Yr+ Gilts Index Fund	124.3	2.65%	2.64%	0.01%	-	-	-	-	-	-
<b>Private Markets Proxy</b>	<b>57.7</b>	-	-	-	-	-	-	-	-	-
BCPP Listed Alternatives	57.7	7.10%	0.47%	6.62%	21.72%	19.89%	1.83%	-	-	-
<b>Private Markets</b>	<b>945.6</b>	-	-	-	-	-	-	-	-	-
Private Markets	945.6	-4.91%	0.24%	-5.15%	-3.43%	20.50%	-23.93%	4.73%	9.27%	-4.54%
<b>Real Estate</b>	<b>291.7</b>	-	-	-	-	-	-	-	-	-
BCPP Global Core Real Estate	2.9	-2.13%	1.47%	-3.60%	-	-	-	-	-	-
CBRE	288.8	-0.04%	1.22%	-1.26%	-3.00%	1.71%	-4.71%	-1.09%	-0.42%	-0.66%
<b>LGIM Currency Overlay</b>	<b>22.5</b>	-	-	-	-	-	-	-	-	-
<b>LGIM Sterling Liquidity Fund</b>	<b>44.1</b>	1.31%	1.30%	0.01%	5.45%	5.38%	0.08%	-	-	-
<b>Liquidity*</b>	<b>112.5</b>	-	-	-	-	-	-	-	-	-

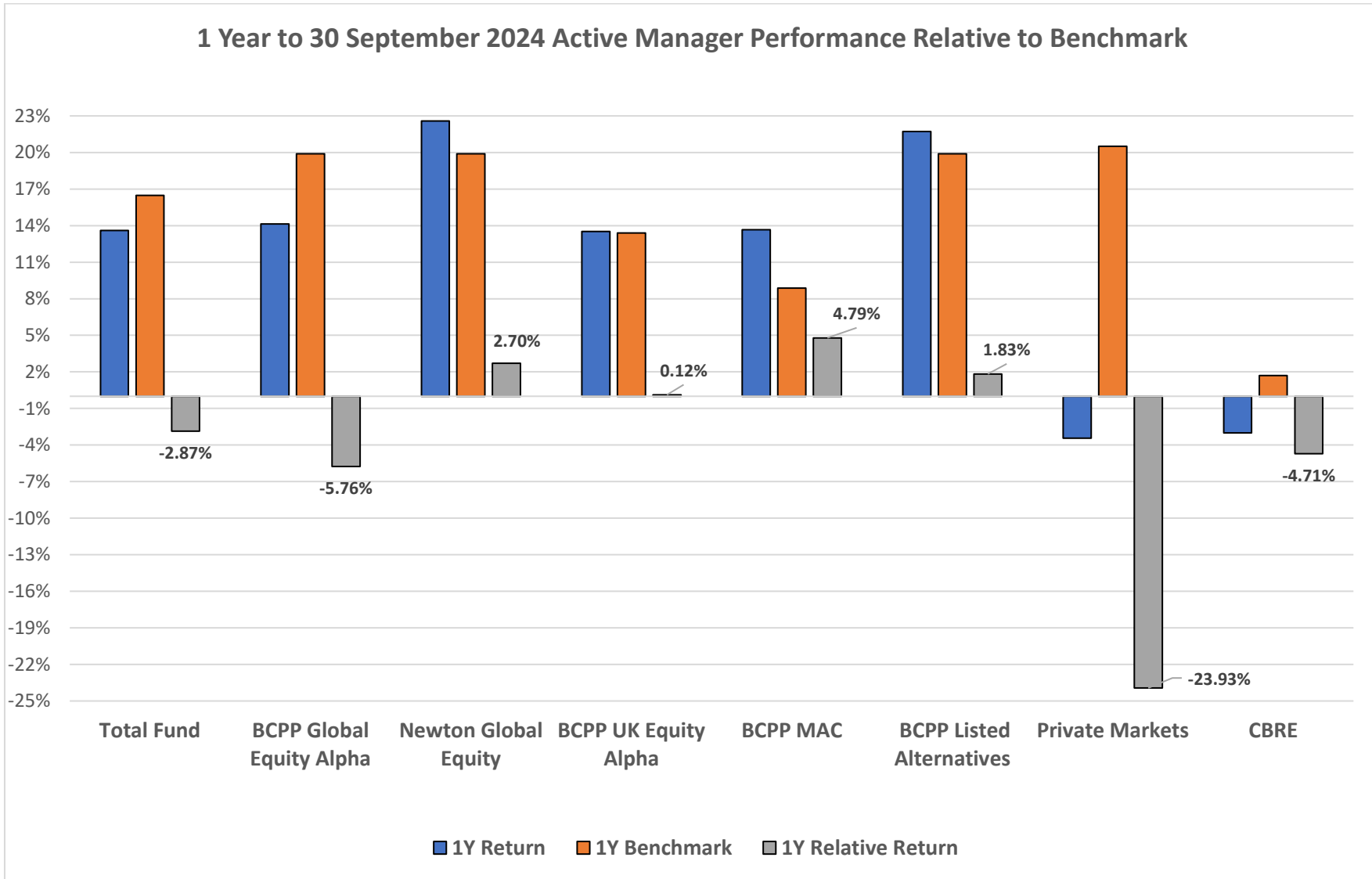
\*Includes £72.4m of money market funds



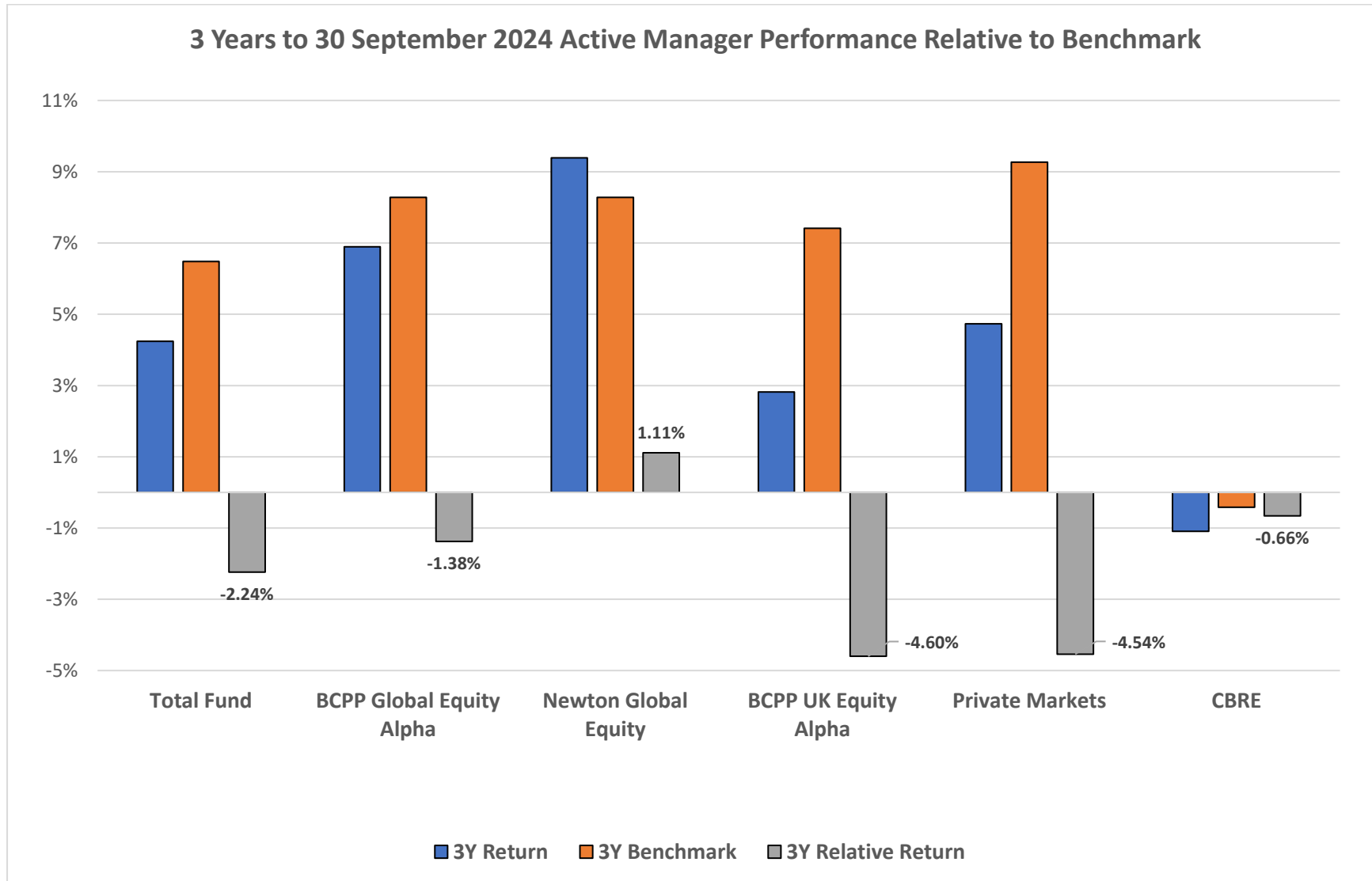
32. The chart below shows the performance, for the latest 3 months to 30 September 2024 for the actively managed portfolios.



33. The chart below shows the performance for the latest 12 months to 30 September 2024 for the actively managed portfolio.



34. The chart below shows the performance for the latest 3 years to 30 September 2024 for the actively managed portfolio.



## Recent Transactions

35. The asset allocation agreed in the December 2022 Committee meeting resulted in a series of transactions taking place in 2023.
36. In April 2023, the Fund invested another £100m into the LGIM Future World Global Equity Index Fund, funded by the redemption of £89m from the BCPP UK Equity Alpha Fund and an £11m in specie transfer from LGIM Future World Emerging Markets Fund. Also in April 2023, £60m was switched from LGIM Bespoke to the LGIM Sterling Liquidity Fund, thus reducing fees.
37. In July 2023, the Fund invested £267m into the BCPP Emerging Markets Equity Alpha Fund, which was funded by the full redemption of the Fund's remaining holding in the LGIM Emerging Markets Fund.
38. Following the Committee's approval of the Investment Strategy Statement in June 2023, the MAC fund exposure was increased. As at 30 September 2023, £60m of BCPP UK Equity Alpha had been sold and £60m of MAC purchased. In October 2023, £60m of Newton Global Equity was sold and £60m of MAC purchased. In November 2023, a further £60m of MAC was purchased.
39. The re-structure of the legacy LGIM Bespoke fund was approved by the Committee in September 2023. In November 2023, in line with that decision, the LGIM Bespoke Fund was liquidated, and a corresponding amount was purchased in the LGIM Over 15Y Gilt fund. The amount of the transaction was £111.4m.
40. To align the exposure to MAC to the Investment Strategy Statement (ISS), the final purchase was completed in January 2024. This amounted to a £60m purchase of MAC and takes the weighting to approximately 15%. There was a corresponding £60m sale of Newton Global Equity.
41. A sale of £20m in Listed Alternatives was completed in January 2024 to help fund ongoing private market capital commitments and drawdowns. Since December 2022, £317m has been redeemed from BCPP Listed Alternatives Fund to fund capital calls in private markets.
42. Capital calls have predominantly been funded by the BCPP Listed Alternatives Fund. Going forward, these calls may increasingly be funded by Newton Global Equity and LGIM Sterling Liquidity Fund assets.

43. The private market commitments to the BCPP programme for April 2024 are £50m to Climate Opportunities, £80 to Private Credit and £90m to UK Opportunities, as agreed at the Committee meeting in March 2024.
44. A sale of £20m in LGIM Sterling Liquidity Fund was completed in April 2024 and a redemption of £27m from Listed Alts in May 2024 to help fund ongoing private market capital commitments and drawdowns.
45. Funding of €2.3m was requested from BCPP in April 2024 for the first transaction in the BCPP Global Real Estate Fund.
46. Due to a build-up of money market funds, the Accounting & Governance team has requested that that regular transfer of income from the MAC and CBRE accounts should stop.
47. In August 2024, a £25m redemption from Newton provided funding for capital calls.

#### Stock Lending

48. In the quarter to 30 September 2024, stock lending earned a net income for the Fund of £8,656 compared with £14,663 for the quarter ended 30 June 2024.

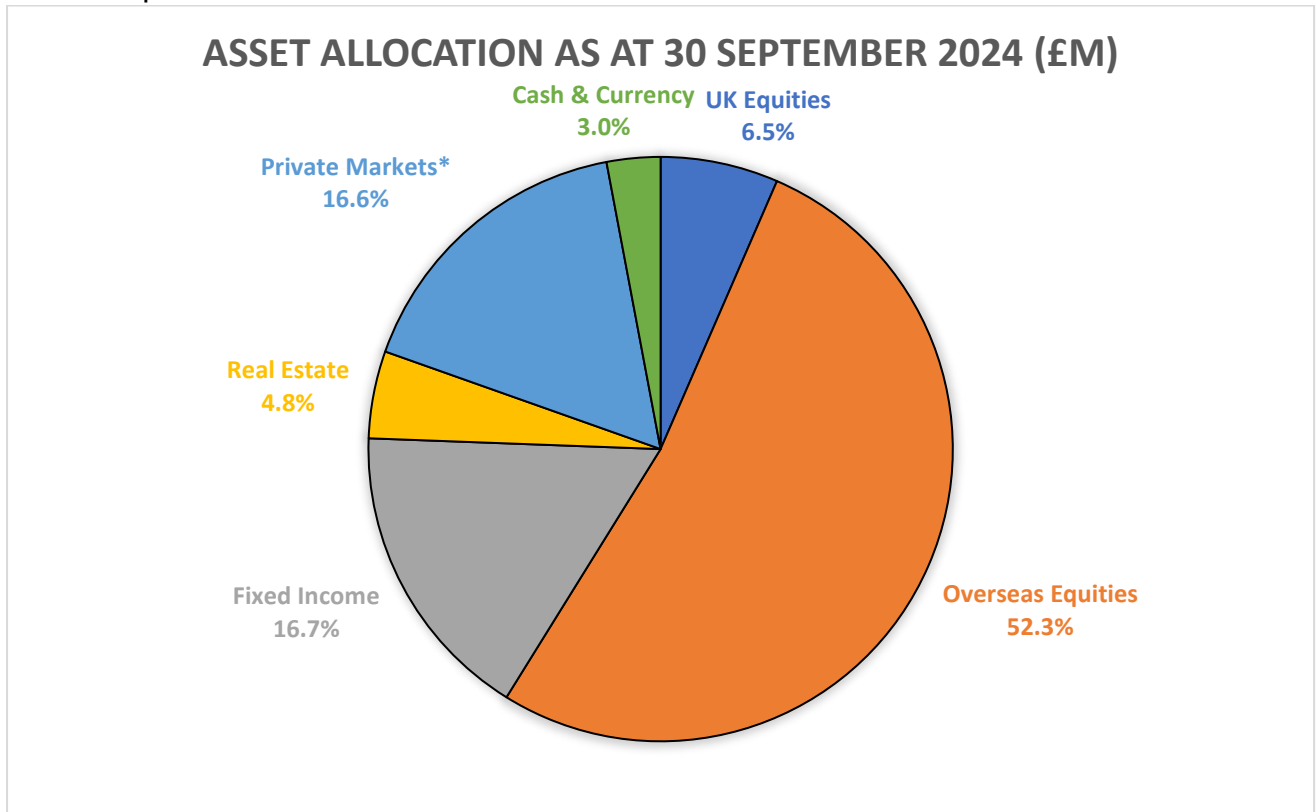
## Asset Allocation

49. The table and the graph below show the target and actual asset allocations for the quarter ending 30 September 2024.

These allocations were agreed by the Pension Fund Committee in the June 2023 meeting.

As at 30 September 2024	Total Fund (£M)	Actual (%)	Target (%)	Advisory ranges %	Role(s) within the strategy
<b>Listed Equities</b>	-	<b>58.8%</b>	<b>55.8</b>	<b>52.8 – 58.8</b>	Generate returns in excess of inflation, through exposure to the shares of domestic and overseas companies.
UK	393.9	6.5%	6.7	-	-
Global Market Cap	1,339.3	22.2%	21.8	-	-
Global Regional	127.8	2.1%	2.2	-	-
Emerging Markets	300.6	5.0%	5.6	-	-
Global Sustainable	1,391.7	23.0%	19.5	-	-
<b>Alternatives</b>	-	<b>21.4%</b>	<b>27.3</b>	<b>22.3-32.3</b>	Generate returns in excess of inflation, through exposure to illiquid assets that are not publicly traded, whilst providing some diversification away from listed equities and bonds.
Private Equity	317.9	5.3%	5	2.0-8.0	-
Infrastructure	367.8	6.1%	6	3.0-9.0	-
Private Debt	169.1	2.8%	6	2.0-8.0	-
Climate Opportunities	90.8	1.5%	3	0.0-6.0	-
Listed Alternatives	57.7	1.0%			-
Real Estate	291.7	4.8%	7.3	4.3–10.3	-
<b>Credit</b>	-	<b>16.7%</b>	<b>16.9</b>	<b>12.1-21.7</b>	Offer diversified exposure to global credit markets to capture both income and capital appreciation of underlying bonds.
Multi Asset Credit	886.6	14.7%	15.1	12.1-18.1	-
Fixed Interest Gilts	124.3	2.1%	1.8	0.0-3.6	-
<b>Cash &amp; Currency Overlay</b>	179.1	<b>3.0%</b>	-	-	-
<b>Total</b>	<b>6,038.3</b>	-	<b>100</b>	-	-

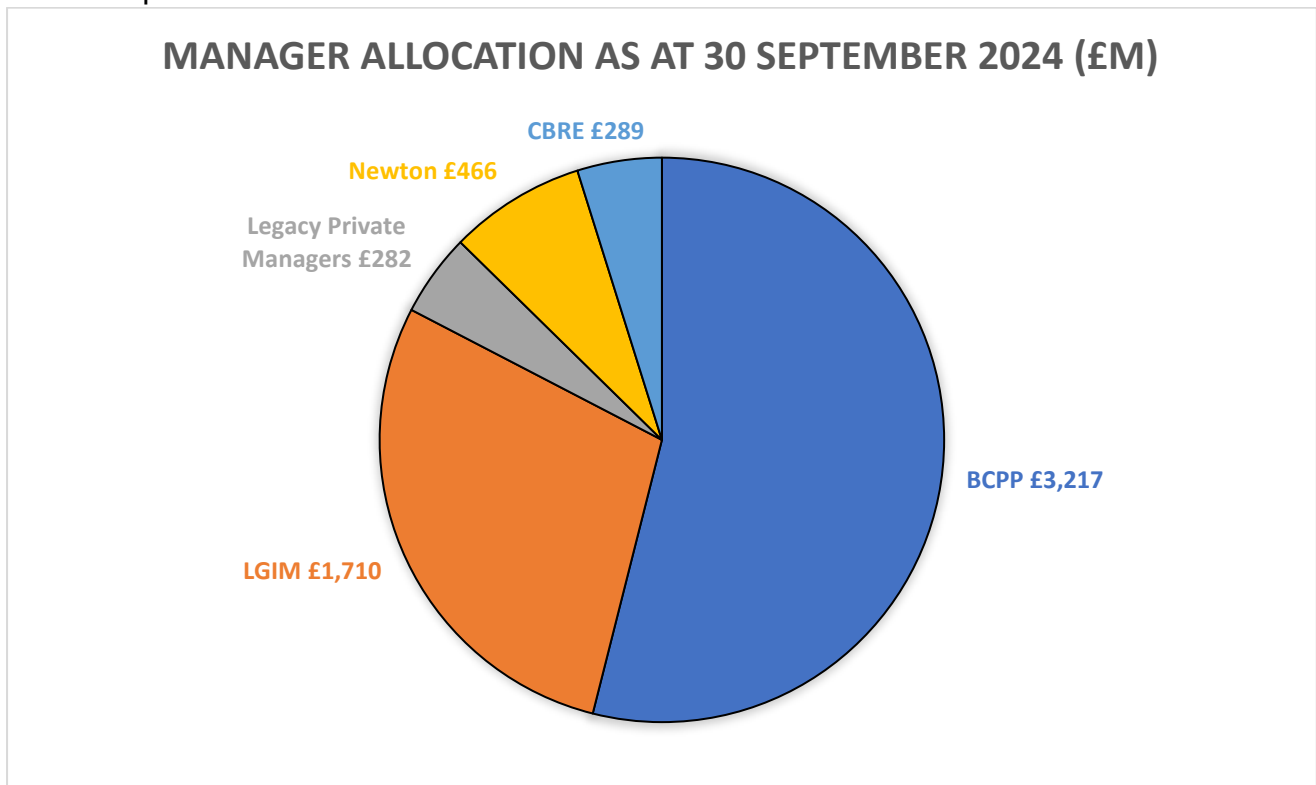
50. The graph below shows the asset allocation for the quarter ending 30 September 2024.



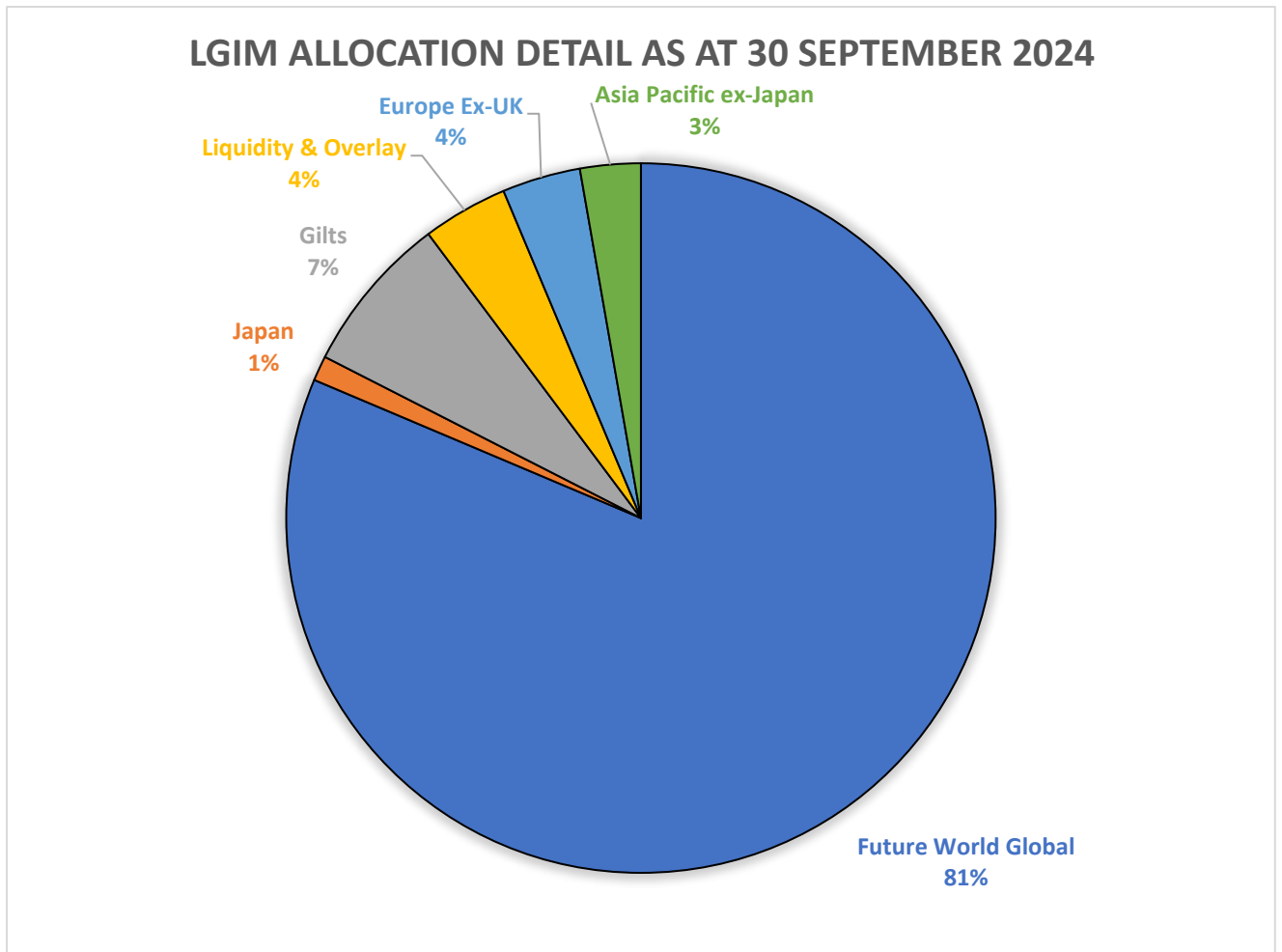
\*Private investment in this chart includes Listed Alternatives.

#### Manager Allocation

51. The graph below shows the manager allocation for the quarter ending 30 September 2024.



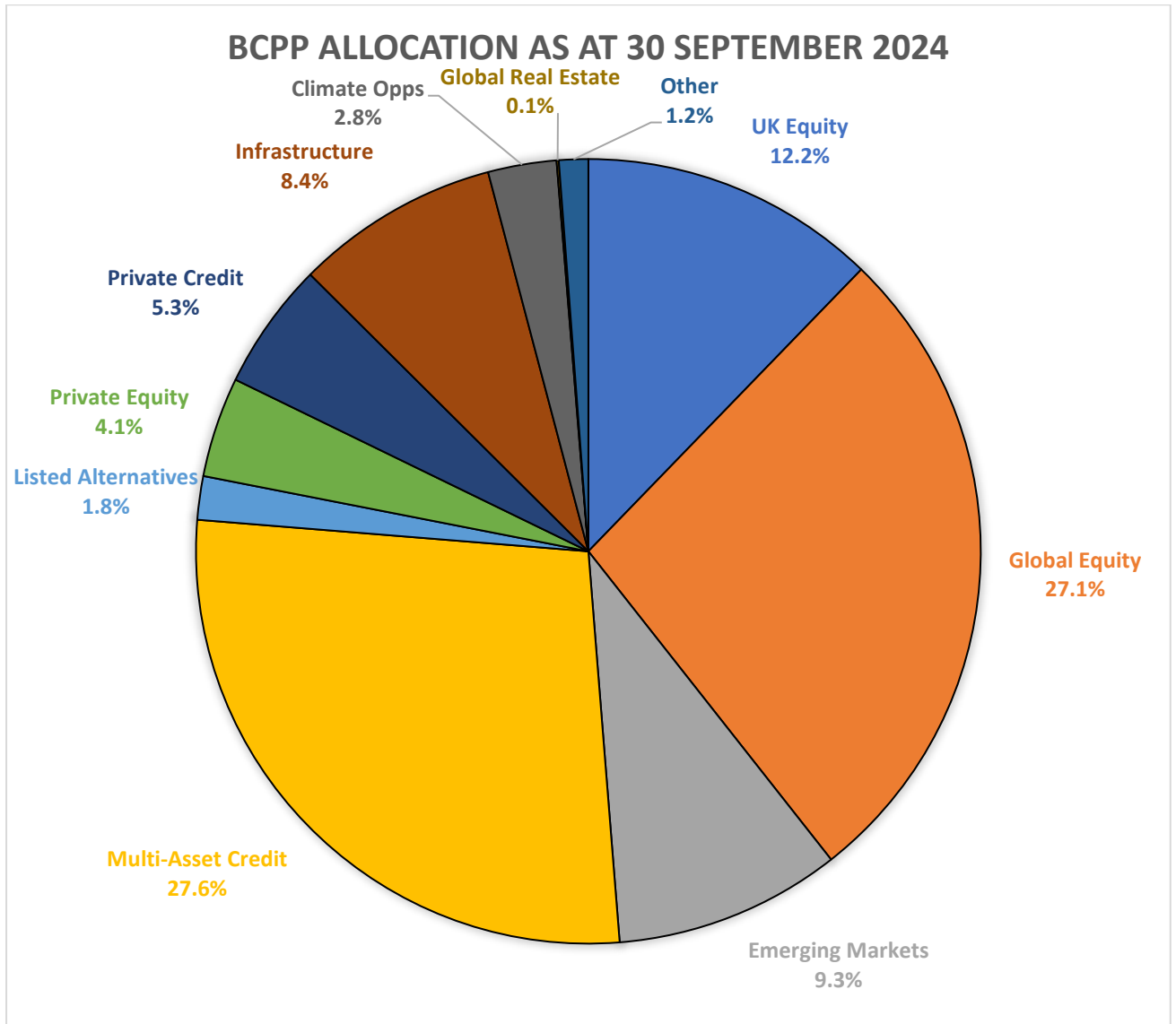
52. The graph below shows the asset allocation within LGIM as at 30 September 2024.



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53. The graph below shows the asset allocation within BCPP as at 30 September 2024.



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## Cashflow

54. Contributions are derived from employers and employees. Pension benefits are derived from pensions and lump sum benefits paid to retired members and benefits paid to employees on leaving the Fund. The table below shows the total contributions received, the total pension benefits paid and the net cashflow for the two most recent quarters to 30 September 2024.

<b>Period</b>	<b>Total contributions received £m</b>	<b>Total pension benefits paid £m</b>	<b>Net cashflow £m</b>
Quarter 1 2024/25 (1 Apr 2024 – 30 Jun 2024)	55.4	62.9	-7.5
Quarter 2 2024/25 (1 Jul 2024 – 30 Sep 2024)	85.7	66.7	19

55. Quarterly cashflow information has been provided by the Accounting & Governance Team who reported that the total contributions are higher than previous quarter due to the Finance team allocating more contribution funds.

## Membership Trends

56. An indication of the current membership trends is shown by movements in membership over Q1 and Q2. Member data for the last two quarters to 30 September 2024 as provided by the Accounting & Governance Team is listed below. Membership numbers include all status types.

<b>Period</b>	<b>Active members</b>	<b>Deferred members</b>	<b>Pension members</b>	<b>Total members</b>
Quarter 1 2024/25 (1 Apr 2024 – 30 Jun 2024)	36,000	62,195	31,360	129,555
Quarter 2 2024/25 (1 Jul 2024 – 30 Sep 2024)	34,994	62,109	31,635	128,738

## Benchmark Table

57. The table below shows the fund managers, the mandate, the benchmark and performance target.

<b>Manager</b>	<b>Mandate</b>	<b>Benchmark Index</b>	<b>Performance Target relative to Benchmark</b>
All	Surrey Pension Fund	Weighted across Fund	+1.0
BCPP	UK Equities Alpha	FTSE All Share	+2.0%
BCPP	Global Equities Alpha	MSCI ACWI	+2.0%
BCPP	MAC	SONIA	+3.5%
BCPP	Listed Alternatives	MSCI ACWI	
BCPP	Emerging Markets Equity Alpha	MSCI EM Index	+2.0%
Newton	Global Equities	MSCI ACWI	+2.0%
Various	Private Markets	MSCI World Index	+5.0%
CBRE	Real Estate	MSCI/AREF UK QPFI All Balanced Property Fund Index (for UK Assets)	+0.5%
LGIM	Europe ex-UK Equities Index	FTSE Developed Europe ex-UK Net Tax (UKPN)	-
LGIM	Future World Global Equity Index	Solactive L&G ESG Global Markets Net	-
LGIM	Japan Equity Index	FTSE Japan NetTax (UKPN)	-
LGIM	Asia Pacific ex-Japan Development Equity Index	FTSE Developed Asia Pacific ex-Japan NetTax (UKPN)	-
LGIM	Sterling Liquidity	SONIA	-
LGIM	15 Yr+ Gilts Index	FTA Over 15 Yr Total Return	-

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**CONSULTATION:**

58. The Chair of the Pension Fund Committee.

**RISK MANAGEMENT AND IMPLICATIONS:**

59. Any relevant risk related implications have been considered and are contained within the report.

**FINANCIAL AND VALUE FOR MONEY IMPLICATIONS:**

60. Any relevant financial and value for money implications have been considered and are contained within the report. The cost of the resources necessary for implementing the changes recommended above and for delivering the administering authority role is met from the pension fund (under Regulation 4(5) of The Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009).

**LEGAL IMPLICATIONS:**

61. There are no legal implications or legislative requirements.

**EQUALITIES AND DIVERSITY:**

62. There are no equality or diversity issues.

**OTHER IMPLICATIONS:**

63. There are no other implications.

**NEXT STEPS:**

64. The following steps are planned:

- a) Continue to implement asset allocation shifts as agreed by the Committee.
- b) Continue to monitor performance and asset allocation.

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**Contact Officer:**

Lloyd Whitworth, Head of Investment & Stewardship

**Annexes:**

- 1. Annexe 1 – Manager Fee Rates (Part 2)

**Sources/Background papers:**

None