

CLWYD PENSION FUND COMMITTEE	
Date of Meeting	Wednesday, 31 st August 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 30 June 2022, and are attached as appendices to this report.

Key points to note:

Economy and Markets

- Trends seen in the first quarter continued throughout the second quarter of 2022. Surging commodity prices, to a large degree the result of the ongoing conflict in Ukraine and supply chain disruptions from Chinese lockdowns led to new multi-decade inflation records.
- Central banks in major regions doubled down on monetary tightening, as the US Federal Reserve and Bank of England raised interest rates several times and are expected to continue to tighten policy throughout the rest of 2022. Consequently, this elevated market volatility and a sell-off in virtually all asset classes except commodities (+10.6%).
- Headline inflation continued to rise in the UK with the 12 month CPI rate reaching 9.4% in June.
- Global bond yields continued to rise over the second quarter of 2022.

Performance Monitoring Report

- Over the three months to 30 June 2022, the Fund's total market value decreased by £184.8m to £2,280.2m, allowing for net cashflows of +£7.9m.
- Fund Performance over 3 months, 12 months and 3 years; -7.5%, -1.5% and +5.7% p.a. respectively.
- Fund Performance is ahead of the composite benchmark over the 12 month and 3 year period. However, Fund performance is behind of the Strategic target and Actuarial targets over the 12 month and 3 year period.
- All asset classes are broadly in line with strategic target weight.

Performance of the Fund is reviewed monthly by the Fund's Officers and advisers.

RECOMMENDATIONS

1.00	That the performance of the Fund over periods to the end of June 2022 are noted along with the Economic and Market update which effectively sets the scene.
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REPORT DETAILS

2.00	INVESTMENT AND FUNDING RELATED MATTERS
2.01	<p>Economic and Market Update 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
2.02	<p>Trends seen in the first quarter continued throughout the second quarter of 2022. Surging commodity prices, to a large degree the result of the ongoing conflict in Ukraine and supply chain disruptions from Chinese lockdowns led to new multi-decade inflation records.</p> <p>Inflation continued to rise, as the 12 month CPI rate for the UK in June reached 9.4%, ongoing energy price increases further exacerbated the inflation outlook.</p> <p>The Bank of England and the US Federal Reserve increased interest rates twice over the second quarter in an attempt to bring inflation under control. Further increases are expected for the rest of the year, some of which we have already witnessed as we draft this report.</p> <p>Equity markets were significantly weaker across the globe as financial conditions tightened, input prices rose and recessionary risk increased.</p> <p>Emerging markets were impacted by the supply chain disruptions and fears of global slowdown that could have a negative impact on exports.</p> <p>UK, Global and Emerging Market Equities all generated negative returns for the quarter, returning -5.0%, -13.3% and -7.3%, respectively.</p> <p>Commodity markets were one of the few major asset classes with positive performance for the quarter (+10.6). There was material divergence in the sector, however, positive performance was exclusively led by energy, which faced material tailwinds from actual and anticipated energy supply disruptions as a result of sanctions against Russia.</p> <p>Sterling depreciated against the US Dollar and Euro, but appreciated against the Yen.</p>

	A verbal update will be provided to Committee on market movements since the writing of this report.																								
2.03	<p>Performance Monitoring report</p> <p>Over the 3 months to 30 June 2022, the Fund's total market value decreased by £184.8m to £2,280.2m, after allowing for net cashflows.</p> <p>The Total Fund has decreased in value by £46.2m in 12 months to 30 June 2022.</p>																								
2.04	<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 WPP Global Opportunities Equity Fund and WPP Emerging Market Equity Fund. <p>The performance against all benchmarks is shown on Page 8 of the report, and repeated below:</p> <table border="1"> <thead> <tr> <th>Total</th> <th>Quarter (%)</th> <th>1 Year (%)</th> <th>3 Years (%)</th> </tr> </thead> <tbody> <tr> <td>Total Scheme</td> <td>-7.5</td> <td>-1.5</td> <td>5.7</td> </tr> <tr> <td>Total Benchmark</td> <td>-6.4</td> <td>-2.2</td> <td>5.4</td> </tr> <tr> <td>Strategic Target (CPI +3.4% p.a.)</td> <td>4.9</td> <td>13.1</td> <td>7.6</td> </tr> <tr> <td>Actuarial Target – Past Service Liabilities (CPI +1.75% p.a.)</td> <td>4.5</td> <td>11.3</td> <td>5.9</td> </tr> <tr> <td>Actuarial Target – Future Service Liabilities (CPI +2.25% p.a.)</td> <td>4.6</td> <td>11.9</td> <td>6.4</td> </tr> </tbody> </table> <p>Strategic and Actuarial targets are derived from realised CPI over the corresponding periods. Prior to Q2 2022, CPI was based on Mercer's Market Forecasting Group assumptions.</p> <p>The table shows the Fund outperformed its total benchmark over the 1 and three year periods. The Fund underperformed against the strategic and actuarial targets</p>	Total	Quarter (%)	1 Year (%)	3 Years (%)	Total Scheme	-7.5	-1.5	5.7	Total Benchmark	-6.4	-2.2	5.4	Strategic Target (CPI +3.4% p.a.)	4.9	13.1	7.6	Actuarial Target – Past Service Liabilities (CPI +1.75% p.a.)	4.5	11.3	5.9	Actuarial Target – Future Service Liabilities (CPI +2.25% p.a.)	4.6	11.9	6.4
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2.05	The strongest absolute returns over the quarter came from Private Markets, returning +7.7%. Within Private Markets the strongest returns were seen in Timber/ Agriculture, Local/ Impact and Private Credit with																								

	<p>returns of +15.7%, +12.3% and +11.5%, respectively.</p> <p>Hedge Funds also generated positive returns over the quarter, returning +0.3%.</p> <p>In the 12 months to 30 June 2022, the best returns came from Private Markets, Total Tactical Allocation (Best Ideas) Portfolio, and Hedge Funds. Private Markets returned +26.2%, whilst the Best Ideas Portfolio and Hedge Funds returned +9.0% and +4.3%, 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. The strategy will be reviewed in the coming year following the results from the triennial actuarial valuation as at 31 March 2022.</p>
2.06	Private Markets are well within the agreed strategic tolerance. Within Private Markets, allocations to Infrastructure and Local/Impact remain slightly underweight; allocation to Property is marginally above weight.

3.00	RESOURCE IMPLICATIONS
3.01	None directly as a result of this report.

4.00	CONSULTATIONS REQUIRED / CARRIED OUT
4.01	None directly as a result of this report.

5.00	RISK MANAGEMENT
5.01	<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>
5.02	<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
5.03	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.
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6.00	APPENDICES
6.01	Appendix 1 - Economic and Market Update – 30 June 2022 Appendix 2 – Performance Monitoring Report – 30 June 2022

7.00	LIST OF ACCESSIBLE BACKGROUND DOCUMENTS
7.01	Economic and Market Update and Investment Strategy and Manager Summary 30 June 2022. Contact Officer: Philip Latham, Head of Clwyd Pension Fund Telephone: 01352 702264 E-mail: philip.latham@flintshire.gov.uk

8.00	GLOSSARY OF TERMS
8.01	<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>

(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.

A comprehensive list of investment terms can be found via the following link:

<https://www.schroders.com/en/uk/adviser/tools/glossary/>