



Complete Agenda

Democratic Service
Swyddfa'r Cyngor
CAERNARFON
Gwynedd
LL55 1SH

Meeting

PENSIONS COMMITTEE

Date and Time

2.00 pm, THURSDAY, 8TH NOVEMBER, 2018

Location

Ystafell Gwyrfai, Council Offices, Caernarfon, Gwynedd. LL55 1SH

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(DISTRIBUTED 31/10/18)

PENSIONS COMMITTEE

MEMBERSHIP (7)

Plaid Cymru (4)

Councillors

Aled Wyn Jones
Peter Read

Simon Glyn

Peredur Jenkins

Independent (2)

Councillors

John Brynmor Hughes

John Pughe Roberts

Individual Member (1)

Councillor

Stephen W. Churchman

Co-opted Members

Councillor David Cowans	Conwy Borough Council
Councillor Robin Wyn Williams	Ynys Mon Council

Ex-officio Members

Chair and Vice-Chair of the Council

A G E N D A

1. APOLOGIES

To receive any apologies for absence

2. DECLARATION OF PERSONAL INTEREST

To receive any declaration of personal interest

3. URGENT ITEMS

To note any items which are urgent business in the opinion of the Chairman so that they may be considered

4. MINUTES

5 - 7

The Chairman shall propose that the minutes of the meeting of this committee held on 19.06.2018 to be signed as a true record

5. INVESTMENT STRATEGY STATEMENT

8 - 18

To consider the report of the Head of Finance

6. TREASURY MANAGEMENT 2018/19 - MID YEAR REVIEW

19 - 23

To consider the report of the Head of Finance

7. GUARANTEED MINIMUM PENSION (GMP) RECONCILIATION

24 - 25

To consider the report of the Pensions Manager

8. EXCLUSION OF PRESS AND PUBLIC

The Chairman shall propose that the press and public be excluded from the meeting during the discussion on the following item due to the likely disclosure of exempt information as defined in paragraph 14, Part 4, Schedule 12A of the Local Government Act 1972. There is an acknowledged public interest in openness in relation to the use of public resources and related financial issues. It is also acknowledged that there are occasions, in order to protect the financial interests of public authorities that matters related to commercial information need to be discussed without being publicised. The report deals specifically with a price offer in relation to a software licence which is commercially sensitive information. Publication of such commercially sensitive information could undermine suppliers confidence to engage with the Council and therefore the Councils ability to procure effectively. This would be contrary to the wider public interest of securing value for money and the best overall outcome. For those reasons the matter should be exempt in the public interest.

9. SELF SERVICE SYSTEM

To consider the report of the Pensions Manager

(Copies for Committee members only)

PENSIONS COMMITTEE 19.06.2018

Present: Councillors: Stephen Churchman, David Cowans (Conwy Borough Council), Simon Glyn, Peredur Jenkins, Aled Wyn Jones, Peter Read, John Pughe Roberts, Robin Williams (Anglesey Council) and Osian Richards (Pensions Board - Observing).

Officers: Dafydd Edwards (Head of Finance Department), Caroline Roberts (Investment Manager) and Lowri Haf Evans (Member Support Officer).

Councillor Stephen Churchman was thanked for his work as Chair of the Committee for 2016-2018. It was noted that the additions to the role's responsibilities were recently escalated following establishing the Pension Board and the All Wales Fund. He was thanked for his leadership, his tireless work at a challenging and innovative time, and for his work as the Chair of the Partnership's Joint Committee, where he represented the Gwynedd Fund with dignity.

In response, Councillor Stephen Churchman thanked everyone for the kind words. He noted that it had been a busy but interesting time. He gave tribute to the work of the officers who served the Wales Pension Partnership and gave a special thanks to the Council's officers for their commitment. He also thanked the Committee for their support.

Councillor Robin Williams (Anglesey representative) was welcomed to his first meeting. The previous Anglesey representative, Councillor John Griffith, was thanked for his service.

1. ELECTION OF CHAIR

It was decided to elect Councillor John Pughe Roberts as Chair of this Committee for 2018/19.

2. ELECTION OF VICE-CHAIR

It was decided to elect Councillor Peredur Jenkins as Vice-chair of this Committee for 2018/19.

3. APOLOGIES

An apology was received from Councillor John Brynmor Hughes.

4. DECLARATION OF PERSONAL INTEREST

None to note

5. URGENT ITEMS

The Head of Finance Department presented certificates to Councillors Simon Glyn and Aled W Jones for completing basic training.

6. MINUTES

The Chair signed the minutes of the meeting of this committee, held on 15 March 2018, as a true record.

7. ATTENDANCE AT CONFERENCES

Information was presented about relevant conferences in order to select representatives to attend them. It was reported that the Council sent representatives on a rota basis to a number of conferences during the year, in order to maintain and improve skills and knowledge.

RESOLVED to send the below representatives to the conferences:

- LAPF Strategic Investment Forum, Hertfordshire, July 2018
Councillors Simon Glyn and Peter Read to check whether they could attend, with Councillor Stephen Churchman as a reserve, and no officers.
- LGC Investment Summit, Newport, September 2018
Councillors John Pughe Roberts and Peredur Jenkins to attend, with the Head of Finance Department.
- Local Authority Pension Fund Forum (LAPFF) annual conference, Bournemouth, December 2018
Councillor John Pughe Roberts and Caroline Roberts (Investment Manager) to attend, with a representative of the Board.
- LGPS Governance Conference, Bristol, January 2019
Councillors John Brynmor Hughes and Robin Williams to attend, with an officer and a representative from the Board, and with Councillor John Pughe Roberts as a reserve.
- Russell Investments annual summit, London, November 2018
Councillors John Pughe Roberts and Peter Read to attend, with the Head of Finance Department.

8. PENSIONS MEETING DATES

Submitted, for information, a report by the Head of Finance Department, noting the dates of pensions meetings for the year 2018 / 2019 so that the members could note the dates in their diaries and plan ahead accordingly.

It was noted that the LGPS Governance Conference was held in Bristol on 17-18 January 2019 which conflicted with a meeting of the Pensions Committee. It was proposed to change the date of the Pensions Committee to 21 January 2019 so that Members and Officers could attend the conference.

Reference was made to the dates of the Investment Panel that was held every quarter to scrutinise the performance of the Pension Fund's investments. It was noted that these were held in London and Caernarfon and it was confirmed that the dates for the Caernarfon meetings would be 21 February 2019 and 16 May 2019.

RESOLVED to accept the information and to amend the date of the Pensions Committee in January 2018 to the 21st.

9. EXCLUSION OF PRESS AND PUBLIC

RESOLVED to exclude the press and public from the meeting during the discussion on the following item due to the likely disclosure of exempt information as defined in paragraph 14, Schedule 12A of the Local Government Act 1972 - information about the financial or business transactions of any specific person (including the authority that

retains that information). There is an acknowledged public interest in openness in relation to the use of public resources and related financial issues. It is also acknowledged that there are occasions, in order to protect the financial interests of public authorities that matters related to commercial information need to be discussed without being publicised. Publication of such information in relation to investment intentions and selection of proposed investment companies could have a negative impact on commercially sensitive activities. This would be contrary to the wider public interest of securing value for money and the best overall outcome and for those reasons the matter should be exempt in the public interest. For these reasons, the matter was closed for the public interest.

10. ASSET ALLOCATION TO THE WALES PENSION PARTNERSHIP GLOBAL EQUITY FUNDS

Submitted - a report of the Head of Finance Department, asking the Committee for the right to act, in consultation with the Committee Chair, on allocating assets to the global equity funds of the Wales Pension Partnership.

It was noted that regular updates had been submitted to the Committee on the progress of the Wales Pension Partnership (WPP) in setting up an investment pool, in accordance with the requirements of Westminster. It was explained that the aims of the Government were improved investment outcomes, reduced risk and reduced costs whilst enabling each constituent authority to implement its own investment strategy.

Following advice from the WPP Operator, and to demonstrate the scale of the pooling to the Government, actively managed global equity was chosen as the type of assets for the initial funds, and it was noted that Link and Russell gave a presentation to Committee members on 15 March, and informal meetings were held on 30 April and 17 May, where expert advice was received from the consultant Hymans Robertson on the matter.

RESOLVED:

- **In accordance with recommendation A, that the Pensions Committee supports the Wales Pension Partnership in setting up two funds, and to include those in the prospectus that will be presented to the Financial Conduct Authority.**
- **In accordance with recommendation B, that the Pensions Committee delegate the power to the Head of Finance Department to re-allocate 80% of the actively managed global equity by the Fund, equally between Fund 1 and Fund 2 of the Wales Pension Partnership.**

The meeting commenced at 2:00pm and concluded at 2:30pm.

The meeting commenced at 2:00pm and concluded at 2:30pm.

Agenda Item 5

MEETING:	PENSIONS COMMITTEE
DATE:	8 NOVEMBER 2018
TITLE:	INVESTMENT STRATEGY STATEMENT
PURPOSE:	TO ASK THE PENSIONS COMMITTEE TO ADOPT THE AMENDED STATEMENT
RECOMMENDATION:	APPROVE THE AMENDED STATEMENT
AUTHOR:	CAROLINE ROBERTS, INVESTMENT MANAGER

1. INTRODUCTION

The Pensions Committee adopted the Investment Strategy Statement (ISS) in March 2017 in accordance with the new legislation. The ISS replaced the Statement of Investment Principles (SIP).

2. RESPONSIBLE INVESTMENT

Following a session with Fund Advisors regarding Environmental, Social and Governance (ESG) for members of the Pensions Committee and the Pension Board, the Investment Panel discussed a paper from Hymans Robertson on investment principles.

The Committee and the Board agreed on the following principles which have been included in the ISS at **Appendix A**.

- 2.1 In accordance with the Committee's fiduciary duty, financial considerations should carry more weight than non-financial considerations when making investment decisions, even though environmental, social, and governance ('ESG') matters can materially affect risk and returns. Therefore, 'ESG' factors should be embedded in the investment processes and in the decision-making processes of the managers appointed by the Fund.
- 2.2 The Fund's Committee will seek to invest in sustainable assets, including investing within the Wales area when non-financial investments can derive from this, on condition that they satisfy the requirements of the fiduciary duty.
- 2.3 The Committee accepts that it has a duty to be a responsible investor. It is expected that consulting with companies, rather than avoiding investing, will be more effective in changing corporate behaviour and reducing risk. Wherever possible, collaborative action provides the most successful route to influence outputs.

- 2.4 As a long-term investor, the Fund is vulnerable to systemic risks such as climate change and the expectation of a transfer to a low carbon economy. Financial outcomes can be improved through managing how open to such risks the fund is.
- 2.5 Share-holder comprehension and outcomes can be improved through providing transparency at each step of the value-adding chain.

3. RECOMMENDATION

- 3.1 The Committee is asked to approve the amended Investment Strategy Statement which is attached at Appendix A.

Investment Strategy Statement

1. Introduction and background

This is the Investment Strategy Statement (“ISS”) of the Gwynedd Pension Fund (“the Fund”), which is administered by Gwynedd Council, (“the Administering Authority”). The ISS is made in accordance with Regulation 7 of the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016 (“the Regulations”).

The ISS has been prepared by the Fund’s Pension Committee (“the Committee”) having taken advice from the Fund’s investment adviser, Hymans Robertson LLP. The Committee acts on the delegated authority of the Administering Authority.

The ISS, which will be approved by the Committee on 16 March 2017, is subject to periodic review at least every three years and without delay after any significant change in investment policy. The Committee has consulted on the contents of the Fund’s investment strategy with such persons it considers appropriate.

The Committee seeks to invest in accordance with the ISS, any Fund money that is not needed immediately to make payments from the Fund. The ISS should be read in conjunction with the Fund’s Funding Strategy Statement (which is currently being reviewed).

2. The suitability of particular investments and types of investments

The primary objective of the Fund is to provide pension and lump sum benefits for members on their retirement and/or benefits on death, before or after retirement, for their dependants, on a defined benefits basis. This funding position will be reviewed at each triennial actuarial valuation, or more frequently as required.

The Committee aims to fund the Fund in such a manner that, in normal market conditions, all accrued benefits are fully covered by the value of the Fund’s assets and that an appropriate level of contributions is agreed by the employer to meet the cost of future benefits accruing. For employee members, benefits will be based on service completed but will take account of future salary and/or inflation increases.

The Committee has translated its objectives into a suitable strategic asset allocation benchmark for the Fund. This benchmark is consistent with the Committee’s views on the appropriate balance between generating a satisfactory long-term return on investments whilst taking account of market volatility and risk and the nature of the Fund’s liabilities.

It is intended that the Fund’s investment strategy will be reviewed at least every three years following actuarial valuations of the Fund.

The fund carried out an asset liability modelling exercise in conjunction with the 2016 actuarial valuation. A number of different contribution and investment strategies were modelled and the future evolution of the Fund considered under a wide range of

different scenarios. The Committee set a target of having a minimum 67% chance of achieving their long term funding target – returning to a fully funded position within the next 20 years. They also considered the level of downside risk in the various strategies by identifying the low funding levels which might emerge in the event of poor outcomes.

This approach helps to ensure that the investment strategy takes due account of the maturity profile of the Fund (in terms of the relative proportions of liabilities in respect of pensioners, deferred and active members), together with the level of disclosed surplus or deficit (relative to the funding bases used).

In addition, the Committee monitors investment strategy on an ongoing basis, focusing on factors including, but not limited to:

- Suitability given the Fund's level of funding and liability profile
- The level of expected risk
- Outlook for asset returns

The Committee also monitors the Fund's actual allocation on a regular basis to ensure it does not notably deviate from the target allocation.

The long term asset class returns assumed within the modelling exercise were as follows:

Asset Class	Median expected return 10 years (%pa)	Median expected return 20 years (%pa)
UK equities	5.0	5.9
Overseas equities	4.6	5.6
Private equity	5.9	7.0
UK Property	2.8	3.7
Absolute Return Bonds	2.6	3.6

3. Investment of money in a wide variety of investments

Asset classes

The Fund may invest in quoted and unquoted securities of UK and overseas markets including equities and fixed interest and index linked bonds, cash, property and commodities either directly or through pooled funds. The Fund may also make use of contracts for differences and other derivatives either directly or in pooled funds investing in these products for the purpose of efficient portfolio management or to hedge specific risks.

The Committee reviews the nature of Fund investments on a regular basis, with particular reference to suitability and diversification. The Committee seeks and considers written advice from a suitably qualified person in undertaking such a review. If, at any time, investment in a security or product not previously known to the Committee is proposed, appropriate advice is sought and considered to ensure its suitability and diversification.

The Fund's target investment strategy is set out below. In line with the Regulations, the authority's investment strategy does not permit more than 5% of the total value of all investments of fund money to be invested in entities which are connected with that authority within the meaning of section 212 of the Local Government and Public Involvement in Health Act 2007".

Table 1: Fund allocation

Asset class	Target allocation %
UK equities	19.5
Overseas equities	53.0
Total equities	72.5
Property	10.0
Bonds	15.0
Infrastructure	2.5
Total	100.0

Managers

The Committee has appointed a number of investment managers all of whom are authorised under the Financial Services and Markets Act 2000 to undertake investment business.

The Committee, after seeking appropriate investment advice, has agreed specific benchmarks with each manager so that, in aggregate, they are consistent with the overall asset allocation for the Fund. The Fund's investment managers will hold a mix of investments which reflects their views relative to their respective benchmarks. Within each major market and asset class, the managers will maintain diversified portfolios through direct investment or pooled vehicles. The manager of the passive funds in which the Fund invests holds a mix of investments within each pooled fund that reflects that of their respective benchmark indices.

4. The approach to risk, including the ways in which risks are to be measured and managed

The Committee is aware that the Fund has a need to take risk (e.g. investing in growth assets) to help it achieve its funding objectives. It has an active risk management programme in place that aims to help it identify the risks being taken and put in place processes to manage, measure, monitor and (where possible) mitigate the risks being taken. One of the Committee's overarching beliefs is to only to take as much investment risk as is necessary.

The principal risks affecting the Fund are set out below, we also discuss the Fund's approach to managing these risks and the contingency plans that are in place:

Funding risks

- Financial mismatch – The risk that Fund assets fail to grow in line with the developing cost of meeting the liabilities.
- Changing demographics – The risk that longevity improves and other demographic factors change, increasing the cost of Fund benefits.
- Systemic risk - The possibility of an interlinked and simultaneous failure of several asset classes and/or investment managers, possibly compounded by financial 'contagion', resulting in an increase in the cost of meeting the Fund's liabilities.

The Committee measures and manages financial mismatch in two ways. As indicated above, the Committee has set a strategic asset allocation benchmark for the Fund. This benchmark was set taking into account asset liability modelling which focused on probability of success and level of downside risk. The results from the 2016 analysis highlighted that the Fund has a 77% probability of achieving full funding over the period to 2037 and a downside risk measure equivalent to a funding level of 38% at that date in the average of the worst 5% of outcomes. This analysis will be revisited as part of the 2016 valuation process. The Committee assesses risk relative to the strategic benchmark by monitoring the Fund's asset allocation and investment returns relative to the benchmark. The Committee also assesses risk relative to liabilities by monitoring the delivery of benchmark returns relative to liabilities.

The Committee also seeks to understand the assumptions used in any analysis and modelling so they can be compared to their own views and the level of risks associated with these assumptions to be assessed.

The Committee seeks to mitigate systemic risk through a diversified portfolio but it is not possible to make specific provision for all possible eventualities that may arise under this heading.

Asset risks

- Concentration - The risk that a significant allocation to any single asset category and its underperformance relative to expectation would result in difficulties in achieving funding objectives.
- Illiquidity - The risk that the Fund cannot meet its immediate liabilities because it has insufficient liquid assets.
- Currency risk – The risk that the currency of the Fund's assets underperforms relative to Sterling (i.e. the currency of the liabilities).
- Environmental, social and governance ("ESG") – The risk that ESG related factors reduce the Fund's ability to generate the long-term returns.
- Manager underperformance - The failure by the fund managers to achieve the rate of investment return assumed in setting their mandates.

The Committee measures and manages asset risks as follows.

The Fund's strategic asset allocation benchmark invests in a diversified range of asset classes. The Committee has put in place rebalancing arrangements to ensure the Fund's "actual allocation" does not deviate substantially from its target. The Fund invests in a range of investment mandates each of which has a defined objective, performance benchmark and manager process which, taken in aggregate, help reduce the Fund's asset concentration risk. By investing across a range of assets, including liquid quoted equities and bonds, as well as property, the Committee has recognised the need for access to liquidity in the short term.

The Fund invests in a range of overseas markets which provides a diversified approach to currency markets; the Committee also assess the Fund's currency risk during their risk analysis. Details of the Fund's approach to managing ESG risks are set out later in this document.

The Committee has considered the risk of underperformance by any single investment manager and have attempted to reduce this risk by appointing more than one manager and having a significant proportion of the Scheme's assets managed on a passive basis. The Committee assess the Fund's managers' performance on a regular basis, and will take steps, including potentially replacing one or more of their managers, if underperformance persists.

Other provider risk

- Transition risk - The risk of incurring unexpected costs in relation to the transition of assets among managers. When carrying out significant transitions, the Committee seeks suitable professional advice.
- Custody risk - The risk of losing economic rights to Fund assets, when held in custody or when being traded.
- Credit default - The possibility of default of a counterparty in meeting its obligations.
- Stock-lending – The possibility of default and loss of economic rights to Fund assets.

The Committee monitors and manages risks in these areas through a process of regular scrutiny of its providers, and audit of the operations it conducts for the Fund, or has delegated such monitoring and management of risk to the appointed investment managers as appropriate (e.g. custody risk in relation to pooled funds). The Committee has the power to replace a provider should serious concerns exist.

A separate schedule of risks that the Fund monitors is set out in the Fund's Funding Strategy Statement.

5. The approach to pooling investments, including the use of collective investment vehicles and shared services

The Fund is a participating scheme in the WALES Pool. The proposed structure and basis on which the WALES Pool will operate was set out in the July 2016 submission to Government.

Assets to be invested in the Pool

The Fund's intention is to invest its assets through the WALES Pool as and when suitable Pool investment solutions become available. An indicative timetable for investing through the Pool was set out in the July 2016 submission to Government. The key criteria for assessment of Pool solutions will be as follows:

- 1 That the Pool enables access to an appropriate solution that meets the objectives and benchmark criteria set by the Fund
- 2 That there is a clear financial benefit to the Fund in investing in the solution offered by the Pool, should a change of provider be necessary.

At the time of preparing this statement the Fund has already invested the following assets via the WALES Pool:

Asset class	Manager	% of Fund assets	Benchmark and performance objective
Passive Equity	BlackRock	22.5	FTSE All-Share and FTSE All-World Indices Benchmark Return

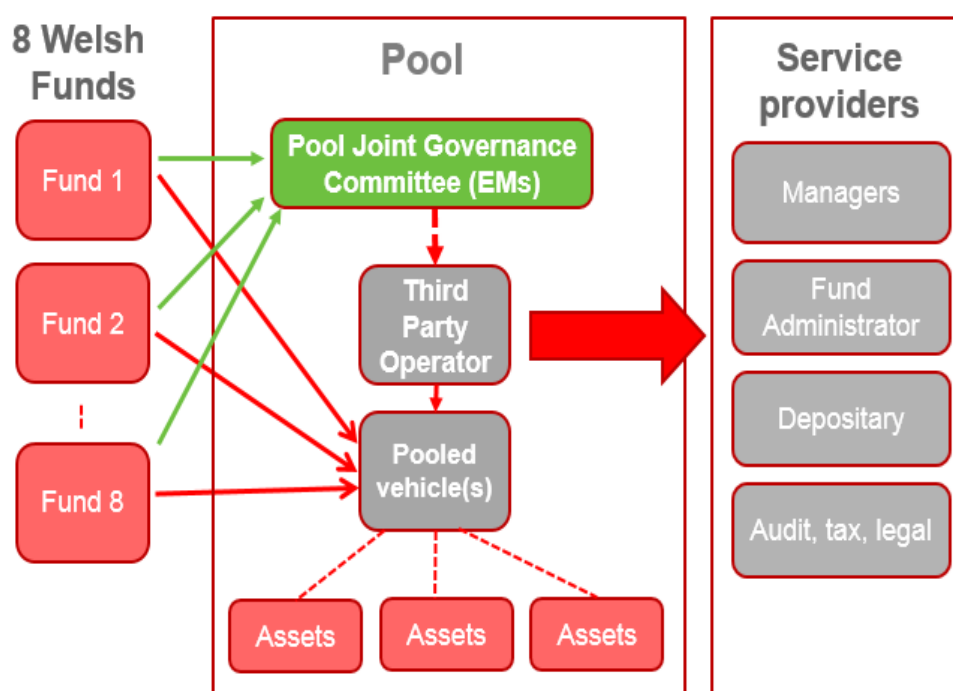
At the time of preparing this statement the Fund has elected not to invest the following assets via the WALES Pool:

Asset class	Manager	% of Fund assets	Benchmark and performance objectives	Reason for not investing via the WALES Pool
Private Equity	Partners	5.0	MSCI World Benchmark + 5% per annum	Existing contractual commitments in funds which have a finite life.
Infrastructure	Partners	2.5	MSCI World Benchmark + 5% per annum	Existing contractual commitments in funds which have a finite life.

Any assets not currently invested in the Pool will be reviewed at least every three years to determine whether the rationale remains appropriate, and whether it continues to demonstrate value for money. The next such review will take place no later than 2020.

Structure and governance of the WALES Pool

The Pool will appoint a third party operator authorised by the FCA to provide a series of investment sub-funds in which the assets of the participating funds will be invested.



A Joint Governance Committee (JGC) will be established to oversee the operator. The Committee will comprise elected members – one from each of the eight participating funds. It is anticipated that this is likely to be the Chairs of the respective Pensions Committees though administering authorities may choose to nominate alternative members if appropriate. This arrangement will provide accountability for the operator back to individual administering authorities.

The Joint Governance Committee (JGC) will be set up formally as a Joint Committee between the participating administering authorities. Each fund will have one elected member on the Committee. It will operate on the basis of ‘One Fund, One Vote’, though the intention is that any decisions are reached by consensus wherever possible. A formal Terms of Reference for the Committee will be drawn up.

The Committee will be responsible for ensuring where practical that there are an appropriate range of sub-funds available to allow administering authorities to implement their own desired asset allocation. The JGC will be in regular discussions

with the operator as to the specific sub-funds which should be set up within the Pool, both at the outset and on an ongoing basis.

Officers from each administering authority will attend JGC meetings (in a non-voting capacity). The officers already work together as the Pensions Sub Group of the SWT (Society of Welsh Treasurers). The formal terms of reference of this officer group will be revised in light of the new pooling arrangements. The officers will advise the JGC on the establishment and monitoring of the various sub-funds as well as liaise directly with the operator on any day-to-day investment matters.

In the first instance, it is anticipated that the fund representatives on the JGC will report back to their respective individual funds' Pensions committees who will be responsible for satisfying themselves as to the effectiveness of the pooling arrangements overall and the operation of the JGC. However, the local Pensions Boards may also seek reassurance on aspects of the management of the funds' investments.

External scrutiny and formal due diligence of the operator and depositary will also be carried out by the FCA in their role as regulator.

The operator will be responsible for selecting and contracting with investment managers for each of the sub-funds as well as appointing other service providers such as depositary asset servicer, and an external valuer as necessary.

We anticipate at this stage that listed bonds and equities are likely to be invested through a UK based Authorised Contractual Scheme (ACS) in order to benefit from the tax transparent nature of the vehicle, though we will discuss this issue with the appointed operator. It may be that alternative vehicles are more appropriate for some other asset classes. As well as considering the options with the operator, we will also take external advice on the final proposed approach from a tax efficiency and legal compliance basis.

Under the proposed structure, the depositary will hold legal title to the assets of the Pool. The operator will be responsible for managing and operating the Pool, including entering into the legal contracts with the investment managers.

The appointed operator will provide and operate a range of investment vehicles to allow collective investment by the participating funds.

The operator will be responsible for selecting and contracting with investment managers for the management of the underlying assets. They will also be responsible for administration in relation to the vehicles in terms of unit pricing, valuation, handling cash flows in and out of the various sub-funds, trade processing and reporting on performance.

They will be responsible for due diligence from an audit, legal and tax perspective for the respective sub-funds and also for electing a depositary to the Pool.

The Pool will also procure independent external legal and tax advice as necessary to support them in their relationship with the operator.

6. How social, environmental or corporate governance considerations are taken into account in the selection, non-selection, retention and realisation of investments

In accordance with the Committee's fiduciary duty, financial considerations should carry more weight than non-financial considerations when making investment decisions, even though environmental, social, and governance ('ESG') matters can materially affect risk and returns. Therefore, 'ESG' factors should be embedded in the investment processes and in the decision-making processes of managers appointed by the Fund.

The Fund's Committee will seek to invest in sustainable assets, including investing within the Wales area when non-financial investments can derive from this, on condition that they satisfy the requirements of the fiduciary duty.

The Committee accepts that it has a duty to be a responsible investor. It is expected that consulting with companies, rather than avoiding investing, will be more effective in changing corporate behaviour and reducing risk. Wherever possible, collaborative action provides the most successful route to influence outputs.

As a long-term investor, the Fund is vulnerable to systemic risks such as climate change and the expectation of a transfer to a low carbon economy. Financial outcomes can be improved through managing how open to such risks the fund is.

Share-holder comprehension and outcomes can be improved through providing transparency at each step of the value-adding chain.

MEETING:	PENSIONS COMMITTEE
DATE:	8 NOVEMBER 2018
TITLE:	TREASURY MANAGEMENT 2018/19 – MID YEAR REVIEW
PURPOSE:	CIPFA's Code of Practice recommends that a report on the Council's actual Treasury Management during the current financial year is produced.
RECOMMENDATION:	RECEIVE THE REPORT FOR INFORMATION
AUTHOR:	DAFYDD L EDWARDS, HEAD OF FINANCE

EXECUTIVE SUMMARY

During the six month period between 1 April and 30 September 2018, the Council's borrowing remained well within the limits originally set. There were no new defaults by banks in which the Council deposited money.

1. INTRODUCTION

The Chartered Institute of Public Finance and Accountancy's Treasury Management Code (CIPFA's TM Code) requires that Authorities report on the performance of the treasury management function at least twice yearly (mid-year and at year end). This report provides a mid-year update.

The Council's Treasury Management Strategy for 2018/19 was approved by full Council on 8 March 2018 which can be accessed on <https://democratiaeth.cyngor.gwynedd.gov.uk/documents/s16298/Rheolaeth%20Trysorllys.pdf?LLL=1>

The Council has borrowed and invested substantial sums of money and is therefore exposed to financial risks including the loss of invested funds and the revenue effect of changing interest rates. The successful identification, monitoring and control of risk are therefore central to the Council's treasury management strategy.

Following consultation in 2017, CIPFA published new versions of the Prudential Code for Capital Finance in Local Authorities (Prudential Code) and the Treasury Management Code of Practice but has yet to publish the local authority specific Guidance Notes to the latter.

The updated Prudential Code includes a new requirement for local authorities to provide a Capital Strategy, which is to be a summary document approved by full Council covering capital expenditure and financing, treasury management and non-treasury investments. This report covers treasury activity and the associated monitoring and control of risk. The Council will be producing its Capital Strategy later in 2018-19 for approval by full Council.

The Welsh Government (WG) asked for comments on changes to its Guidance on Minimum Revenue Provision (MRP). These include clarification or changes to terminology and the calculation of MRP.

2. EXTERNAL CONTEXT

Economic background: Oil prices rose by 23% over the six months to around \$82/barrel. UK Consumer Price Inflation (CPI) for August rose to 2.7% year/year, above the consensus forecast and that of the Bank of England's in its August *Inflation Report*, as the effects of sterling's large depreciation in 2016 began to fade. The most recent labour market data for July 2018 showed the unemployment rate at 4%, its lowest since 1975. The 3-month average annual growth rate for regular pay, i.e. excluding bonuses, was 2.9% providing some evidence that a shortage of workers is providing support to wages. However real wages (i.e. adjusted for inflation) grew only by 0.2%, a marginal increase unlikely to have had much effect on households.

The rebound in quarterly GDP growth in Q2 to 0.4% appeared to overturn the weakness in Q1 which was largely due to weather-related factors. However, the detail showed much of Q2 GDP growth was attributed to an increase in inventories. Year/year GDP growth at 1.2% also remains below trend. The Bank of England made no change to monetary policy at its meetings in May and June, however hawkish minutes and a 6-3 vote to maintain rates was followed by a unanimous decision for a rate rise of 0.25% in August, taking Bank Rate to 0.75%.

Having raised rates in March, the US Federal Reserve again increased its target range of official interest rates in each of June and September by 0.25% to the current 2%-2.25%. Markets now expect one further rise in 2018.

The escalating trade war between the US and China as tariffs announced by the Trump administration appeared to become an entrenched dispute, damaging not just to China but also other Asian economies in the supply chain. The fallout, combined with tighter monetary policy, risks contributing to a slowdown in global economic activity and growth in 2019.

The EU Withdrawal Bill, which repeals the European Communities Act 1972 that took the UK into the EU and enables EU law to be transferred into UK law, narrowly made it through Parliament. With just six months to go when Article 50 expires on 29th March 2019, neither the Withdrawal Agreement between the UK and the EU which will be legally binding on separation issues and the financial settlement, nor its annex which will outline the shape of their future relationship, have been finalised, extending the period of economic uncertainty.

Financial markets: Gilt yields displayed marked volatility during the period, particularly following Italy's political crisis in late May when government bond yields saw sharp moves akin to those at the height of the European financial crisis with falls in yield in safe-haven UK, German and US government bonds. Over the period, despite the volatility, the net change in gilt yields was small. The 5-year benchmark gilt only rose marginally from 1.13% to 1.16%. There was a larger increase in 10-year gilt yields from 1.37% to 1.57% and in the 20-year gilt yield from 1.74% to 1.89%. The increase in Bank Rate resulted in higher money markets rates. 1-month, 3-month and 12-month LIBID rates averaged 0.56%, 0.70% and 0.95% respectively over the period.

Credit background: Reflecting its perceived higher risk, the Credit Default Swap (CDS) spread for non-ringfenced bank NatWest Markets plc rose relatively sharply over the period to around 96bps. The CDS for the ringfenced entity, National Westminster Bank plc, has held steady below 40bps. Although the CDS of other UK banks rose marginally over the period, they continue to remain low compared to historic averages.

The ringfencing of the big four UK banks - Barclays, Bank of Scotland/Lloyds, HSBC and RBS/Natwest Bank plc – is complete, the transfer of their business lines into retail (ringfenced) and investment banking (non-ringfenced) is progressing and will need to be completed by the end of 2018.

There were a few credit rating changes during the period. Moody's downgraded Barclays Bank plc's long-term rating to A2 from A1 and NatWest Markets plc to Baa2 from A3 on its view of the credit metrics of the entities post ringfencing. Upgrades to long-term ratings included those for Royal Bank of Scotland plc, NatWest Bank and Ulster Bank to A2 from A3 by Moody's and to A- from BBB+ by both Fitch and Standard & Poor's (S&P). Lloyds Bank plc and Bank of Scotland plc were upgraded to A+ from A by S&P and to Aa3 from A1 by Moody's.

Our treasury advisor Arlingclose will henceforth provide ratings which are specific to wholesale deposits including certificates of deposit, rather than provide general issuer credit ratings. Non-preferred senior unsecured debt and senior bonds are at higher risk of bail-in than deposit products, either through contractual terms, national law, or resolution authorities' flexibility during bail-in. Arlingclose's creditworthiness advice will continue to include unsecured bank deposits and CDs but not senior unsecured bonds issued by commercial banks.

3. INVESTMENT ACTIVITY

The Council holds invested funds, representing income received in advance of expenditure plus balances and reserves held.

The Welsh Government's Investment Guidance gives priority to security and liquidity and the Council's aim is to achieve a yield commensurate with these principles.

The Council holds invested funds, representing income received in advance of expenditure plus balances and reserves held. During the 6 months, the Council's investment balance ranged between £79.4 and £31.4 million due to timing differences between income and expenditure. The investment position during the period is shown in the table below.

	31.3.18 Balance £m	6 month Movement £m	30.9.18 Balance £m
Banks & building societies (unsecured)	11.1	3.8	14.9
Covered bonds (secured)	2.1	(1.0)	1.1
Government (incl. local authorities)	25.0	(7.0)	18.0
Money Market Funds	9.3	(0.4)	8.9
Total investments	47.5	(4.6)	42.9

Both the CIPFA Code and government guidance require the Council to invest its funds prudently, and to have regard to the security and liquidity of its treasury investments before seeking the optimum rate of return, or yield. The Authority's objective when investing money is to strike an appropriate balance between risk and return, minimising the risk of incurring losses from defaults and the risk of receiving unsuitably low investment income.

Security of capital has remained the Council's main investment objective. This has been maintained by following the Council's counterparty policy as set out in its Treasury Management Strategy Statement for 2018/19.

Counterparty credit quality was assessed and monitored with reference to credit ratings (the Council's minimum long-term counterparty rating for institutions defined as having "high credit quality" is A- across rating agencies Fitch, S&P and Moody's); credit default swap prices, financial statements, information on potential government support and reports in the quality financial press.

Performance Report

The progression of risk and return metrics are shown in the extracts from Arlingclose's quarterly investment benchmarking in the table below.

	Credit Score	Credit Rating	Bail-in Exposure	Weighted Average Maturity (days)	Rate of Return %
31.03.2018	3.96	AA-	43%	48	0.55
30.06.2018	3.85	AA-	42%	52	0.69
30.09.2018					
Similar LAs	5.78	A	58%	248	0.75
All LAs	4.21	AA-	62%	42	0.65

Investments were made with banks and building societies and included call accounts, fixed-rate term deposits and certificates of deposit, Money Market Funds and covered bonds.

The average cash balances were £48.7m during the six months. Following a UK Bank Rate of 0.25% since August 2016 the rate was increased to 0.5% in October 2017 and then increased again in July 2018 to 0.75%.

The Council's budgeted investment income for the year is estimated at £0.17m based on an investment outturn of 0.5% for the whole year.

Compliance Report

I can confirm compliance with the Prudential Indicators for 2018/19, which were set in March 2018 as part of the Council's Treasury Management Strategy Statement.

4. Investment Training

During the period officers have attended investment training with Arlingclose and CIPFA relevant to their roles.

5. Outlook for the remainder of 2018/19

Having raised policy rates in August 2018 to 0.75%, the Bank of England's Monetary Policy Committee (MPC) has maintained expectations of a slow rise in interest rates over the forecast horizon.

The MPC has a definite bias towards tighter monetary policy but is reluctant to push interest rate expectations too strongly. While policymakers are wary of domestic inflationary pressures over the next two years, it is believed that the MPC members consider both that (a) ultra-low interest rates result in other economic problems, and that (b) higher Bank Rate will be a more effective weapon should downside Brexit risks crystallise and cuts are required.

Arlingclose's central case is for Bank Rate to rise twice in 2019. The risks are weighted to the downside. The UK economic environment is relatively soft, despite seemingly strong labour market data. GDP growth recovered somewhat in Q2 2018, but the annual growth rate of 1.2% remains well below the long term average.

	Sep-18	Dec-18	Mar-19	Jun-19	Sep-19	Dec-19	Mar-20	Jun-20	Sep-20	Dec-20	Mar-21	Jun-21	Sep-21
Official Bank Rate													
Upside risk	0.00	0.00	0.00	0.00	0.00	0.00	0.25	0.25	0.25	0.25	0.25	0.25	0.25
Arlingclose Central Ca	0.75	0.75	1.00	1.00	1.25	1.25	1.25	1.25	1.25	1.25	1.25	1.25	1.25
Downside risk	0.00	0.00	0.50	0.50	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.75

The view is that the UK economy still faces a challenging outlook as the minority government continues to negotiate the country's exit from the European Union. Central bank actions and geopolitical risks, such as prospective trade wars, have and will continue to produce significant volatility in financial markets, including bond markets.

Agenda Item 7

MEETING	Pensions Committee
DATE	8 November 2018
TITLE	GMP (Guaranteed Minimum Pension) Reconciliation
PURPOSE OF THE REPORT	Update the Committee about the reconciliation work as the process nears completion
AUTHOR	Nicholas Hopkins – Pensions Manager
RECOMMENDATION	For information only

1. BACKGROUND

- 1.1 Committee members will be aware that a three person team was established in January 2016 to deal with GMP (Guaranteed Minimum Pension) reconciliation. Progress reports were submitted to Committee meetings held in November 2016 and 2017.

2. UPDATE

- 2.1 The temporary member of staff (appointed to the team from June 2016) obtained a permanent post as of the end of July 2018. As most of the work had been completed, with queries sent to HMRC, it was decided that for the short time remaining on the project, a replacement would not be sought.
- 2.2 As of October 2018, there were 134 queries awaiting reply from HMRC. Gwynedd Pension Fund (GPF) maintains that 30 of these are 'not in scheme' due to refunds having been paid, and therefore there should be no GMPs in the Fund. In such cases a Contribution Equivalent Premium would be due to HMRC. GPF maintain that these payments have been made and is therefore challenging HMRC about the facts.
- 2.3 Of particular concern are those where GPF and HMRC disagree about their contracted out circumstances. These are referred to as 'stalemate cases' and vary from cases where benefits have been transferred out (including the GMP) to other schemes, but HMRC maintain that GPF retain liability, to dependant pensioners where GPF pays a widow/widower GMP but HMRC maintain there is no widow/widower entitlement.
- 2.4 GPF currently has 119 widow/widower cases designated as 'stalemate'. Although entitlement under pension regulations has been confirmed by double checking marriage and birth certificates, HMRC still insist there is no entitlement.

- 2.5 'Stalemate' issues have been raised with the Westminster Government's Ministry of Housing, Communities and Local Government (MHCLG), who in turn raised it with Treasury. A letter dated 25 September 2018 from Paul Kirk (Head of Public Service Pensions at Treasury) to Sophie Broadfield (Minister of Housing and Local Government) stated that such cases should be resolved between schemes and HMRC on an individual scheme basis. This remains an issue requiring further investigation.

3. CONCLUSIONS

- 3.1 I am pleased to be able to inform members that GPF are in a comparatively good position as regards the GMP reconciliation project. The two person team will finish on 31 December 2018 as the team leader retires and the seconded Pensions Officer returns to the Pension Section having gained valuable experience.
- 3.2 Any outstanding issues will transfer to the main Pension Section's day to day work.