Leicestershire County Council

Minutes of a meeting of the Local Pension Committee held at County Hall, Glenfield on Friday, 26 January 2024.

PRESENT:

Leicestershire County Council

Mr. T. Barkley CC (Chairman)
Mr. D. C. Bill MBE CC
Mr. D. J. Grimley CC
Mr. P. King CC
Mr. C. A. Smith CC

Leicester City Council

Cllr Adam Clarke

District Council Representative

Cllr. Martin Cartwright and Cllr. Roy Denney

University Representative

Mr. Zubair Limbada

Staff Representatives

Mr N. Booth
Mr V. Bechar

Independent Advisers in Attendance

Mr Phillip Pearson	Hymans Robertson
Mr Russel Oades	Hymans Robertson

112. Minutes.

The minutes of the meeting held on 1st December 2023 were taken as read, confirmed and signed subject to an amendment being made to record that prior to consideration of the Climate Risk Management Report 2023 (minute 84 refers) the meeting had been adjourned for a short period.

113. Question Time.

The Chief Executive reported that no questions had been received under Standing Order 34.

114. Questions asked by members under Standing Order 7(3) and 7(5).

The Chief Executive reported that no questions had been received under Standing Order 7(3) and 7(5).

115. Urgent Items.

There were no urgent items for consideration.

116. Declarations of interest.

The Chairman invited members who wished to do so to declare any interest in respect of items on the agenda for the meeting.

There were no declarations made.

117. Overview of the Current Asset Strategy and Proposed 2024 Asset Strategy.

The Committee considered a report of the Director of Corporate Resources, the purpose of which was to inform the Committee of the outcome of the annual review of the Leicestershire Pension Fund's (the Fund) strategic investment allocation and structure. The report also provided advice regarding the Fund's current investment strategy relating to fossil fuel exposure and provided advice, as requested by the Committee at its last meeting in December 2023, on the proposal put forward to 'require LGPS Central to establish a fossil fuel free fund.' A copy of the report marked 'Agenda Item 6' is filed with these minutes.

The Chairman welcomed to the meeting Mr. Philip Pearson and Mr. Russel Oades from Hymans Robertson, who supplemented the report with a presentation. A copy of the presentation slides is filed with these minutes.

At the request of the Chairman and in response to questions raised, the Head of Law advised the Committee that the report properly addressed the proposal put forward by Cllr Cartwright in the context of the motion unanimously agreed at its last meeting and referred Members to the relevant paragraphs (paragraphs 2, 9, 20 to 46 and the recommendation at paragraph 48(d)).

The Chairman reminded members of the legal advice the Committee had received about its duties and responsibilities, emphasising that the Committee's power of investment must be exercised with care, skill, prudence and diligence and that its predominant focus should be what was best for the financial position of the fund (balancing risk and return). The primary objective of the Committee was to ensure sufficient funding in the long term so that retirement benefits that employers promised to members under scheme rules could be paid when they fell due. Provided the risk of significant financial detriment to the fund remained low, the Committee's choice of investment might be influenced by wider social, ethical or environmental considerations where views on investment are likely to be widely shared by scheme employers and members.

Arising from the discussion and questions, the following points were made:

Annual Review of Investment Strategy

(i) Based on current figures the expected median return for the 2024 strategic asset allocation (SAA) of 8.7%pa, was considered achievable. The figures were based on yields on government bonds which were relatively high. It was noted, however, that as this was just a median estimate there was a 50 percent chance the returns could be higher or lower. Therefore, when establishing the funding position for the Fund a more prudent and conservative view would be taken.

(ii) A member questioned how the investment strategy took account of the recent announcement by the Department for Levelling Up, Housing and Communities (DLUHC) which suggested that funds might be required to invest up to 5% in assets to support levelling up in the UK. Mr Pearson advised that investing in projects that would contribute to levelling up would not be new for the Fund. The Funds investment in infrastructure assets were a good example of this, which included a significant allocation to the UK. Members noted that investment managers were in the process of assessing where the Fund's existing investments were already contributing to levelling up objectives, following which they would consider whether anything else needed to be done. However, the Fund already likely met the 5% target.

(iii) A Member raised concerns that some large-scale government projects aimed at levelling up had been cancelled, such as HS2 phase 2b, and questioned, given that government policy could change, if this increased the level of risk for the Fund. Mr Pearson reassured members that investment managers would not invest predominantly or primarily to help the levelling up agenda from a political perspective. This would not be appropriate as their professional role was to seek out and prioritise investments that would generate a good financial return for the Fund. They would, however, seek to take advantage of those opportunities that offered both an attractive financial return and had good positive economic and social impacts that could contribute to the Government's levelling up agenda.

(iv) Most of the Fund's mandates were global mandates which gave investment managers the widest possible opportunity to consider the best investments available. Of those in the UK, some could relate to Leicestershire. Members noted that unfortunately, original, good infrastructure investment opportunities were limited, despite the UK having a proportionately good share of the global investable infrastructure market.

(v) A Member questioned whether LGPS Central helped to inform the market of the sort of projects it would be interested in. Mr Pearson confirmed that all infrastructure managers, as well as LGPS Central, did this on a regular basis, particularly as infrastructure managers were now more proactive in dealing with the issue of a lack of supply. Members noted that infrastructure managers had moved into developing projects themselves, identifying infrastructure needs, taking them through the planning process, raising the finance needed and thereafter managing projects through to construction.

(vi) Investment managers were sensitive to a wide range of risks, including climate change and geopolitics. Whilst steps were taken to avoid such risks this was not always possible; recent events in the Red Sea being a good example, given its importance as a trade route. Members were reassured that the Funds exposure to BRICS (emerging market countries including Brazil, India, China and South Africa and others) was relatively small (less than 10%). Risks were also managed through good diversification both in terms of asset type and geography.

(vii) A Member questioned to what degree consideration was given to how other funds and pools chose to invest, how they performed, and whether the Fund was benchmarked against them. Mr Pearson advised that whilst other funds activities were considered, managers would not be influenced by them, as every fund was different, particularly in areas such as funding position, risk appetite, the ability of sponsoring employers to flex their contribution rates up and/or down. It was important that the funding strategy and the investment strategy reflected the needs of individual Funds, not the LGPS average.

(viii) The Committee noted that Boarder to Coast had created a fund that was dedicated to climate opportunities. This was different to the approach taken by LGPS Central which had chosen to invest in decarbonisation opportunities across a number of different funds. Whilst two different approaches, it looked like both, in terms of the sorts of assets they invested in, were similar. However, Mr Pearson advised that LGPS Central could demonstrate better progress on meeting its climate change targets.

(ix) As part of the SAA review investments in protection assets had been considered to control investment risk and mitigate the Fund's liabilities. However, as both were linked to interest rates and inflation both moved in the same direction. Whilst the rise in inflation had resulted in a material fall in the value of the Fund's protection assets by around 8%, the Fund's liabilities had also fallen by the same percentage. In monetary terms, however, its liabilities had fallen a lot further and so overall the Fund's position had improved from the last valuation point. Consequently, whilst an increase in the Fund's allocation to protection assets might appear justifiable, Mr Pearson advised that a more detailed assessment would be needed before considering such approach. Hymans Robertson would undertake more detailed modelling in the first quarter of 2024 and an update would be provided to the Investment Sub Committee in April.

Proposal to establish a fossil fuel free fund

The Chairman advised members that the Committee could not 'require' LGPS Central to set up a fossil free fund, as had been originally proposed by Cllr Cartwright at the previous meeting in December. It could only 'request' this. To avoid confusion, and before commencing the discussion on this item, the Chairman sought and obtained the consent of the Committee to alter the wording of the recommendation set out in paragraph 48(d), to replace the word 'require' with 'request'.

At the invitation of the Chairman, Cllr Cartwright confirmed that he had no objection to the change in terminology. He commented that he wished to seek to add a fund that allowed for investments to be made which were specifically fossil fuel free. The request was simply to allow the Fund to have choice and clarity and specifically did not seek to change current investments.

Arising from discussion and questions on this section of the report, the following points were made:

(i) The approach currently adopted by the Fund was based on the core principle that it was better for the Fund, the wider economy and the climate, to remain invested in companies that had high emissions, or fossil fuel reserves, so it could engage very firmly with those companies to decommission those reserves and reduce emissions. Three different mechanisms were adopted to achieve this: (a) managers met regularly with companies to make sure they had sensible decarbonisation plans in place and were delivering on them; (b) use a 'tilted index approach' where a sub-fund reduced the weight to those companies that had high emissions or high exposure to fossil fuel reserves; (c) managers made decisions on individual stocks, taking into account a variety of criteria including exposure to climate risk, prioritising those companies that offered good investment returns but had a responsible approach to managing climate risk. Members commented that more information was needed to better understand what outcomes these approaches achieved. It was noted that Hymans Robertson had recommended that the Fund improve reporting in this area to provide officers and the Committee with greater insight.

(ii) Members noted the Fund was on target to achieve its Net Zero objectives. Its greenhouse gas emissions and exposure to fossil fuels had fallen faster than was needed to meet these targets, and current levels of both emissions and fossil fuels were well below the asset markets that the Fund invested in. Mr Pearson commented that this was one of the reasons why Hymans Robertson had not recommended changing the Fund’s current investment approach as this was working very well.

(iii) A Member questioned whether fossil fuel free funds were producing better outcomes. Mr Pearson advised that whilst there were several such funds on the market, these currently appeared to have higher greenhouse gas emissions than those which the Leicestershire Pension Fund currently invested in. At the request of a member, the Director undertook to provide the data that showed LGPS Central was performing better than the Border to Coast fund.

(iv) A Member raised concerns that whilst the comments now made were compelling, this had not been supported by evidence within the report. The Director of Corporate Resources emphasised that officers had been asked to provide advice on the Fund’s current investment strategy and the merits of the concept of requesting LGPS to introduce a fossil fuel free fund. Comparisons on the rate of decarbonisation with other funds had not therefore been included though this could form part of the annual report on performance against the Fund’s Net Zero Climate Strategy.

(v) Members raised questions regarding the practicalities of establishing a fossil fuel free fund. It was noted that the LGPS Central pool was managed as a whole, in line with a single investment strategy agreed by the partners. Partner funds were currently aligned on the approach to address climate risk. Members were advised that LGPS Central would be hesitant to develop a new fossil fuel free product without funds first being committed to invest within this given the cost implications for all the administering bodies. Officers confirmed that the cost of developing a fossil fuel free fund would not be insignificant and would have to be shared under the cost sharing agreement signed by all eight-pension fund administering authorities within LGPS Central.

(vi) The Fund was not structured to offer choice to individuals. The Fund combined all the assets and liabilities across the employers to share risks. Mr Pearson advised that offering a fossil fuel free investment strategy choice alongside a normal investment strategy choice would essentially create two funds which would result in the splitting of liabilities and losing some of the benefits of sharing risk, including those not related to climate change. This was not therefore recommended.

(vii) Members noted that, given the legal and shareholder agreements put in place for individual pools, investing in another partnership pooled fund that had already established a fossil fuel free fund would be complex and give rise to added cost and risk. By way of example, the transition costs to move £0.8 billion from LGIM to LGPS Central’s climate multifactor fund had been in the region of £18m. The longer such transitions took, the greater the risk and the higher the potential cost.

(viii) The Director of Corporate Resources reminded the Committee that this was a defined benefit contribution scheme. The choice around investments were made by the trustees of the scheme which was this Committee (and the Investment Sub Committee). Whilst the Committee should be cognisant of individual members views, individual scheme members did not have a choice as to how the Fund would be invested. It was incumbent on the Committee to make those decisions and to ensure pensions could be paid now and in the future, noting that responsibility ultimately fell back onto the employers, such as the County, City and district councils, who underwrote the scheme.

(ix) A Member questioned if a scheme member could choose to opt out of the LGPS if they felt strongly about the way it was being invested. The Director confirmed that employers were obliged to offer the LGPS and did not have to offer a different defined contribution scheme. A member could therefore opt out as membership was not mandated. However, they would not then receive the employer contributions.

(x) There was a general consensus that the Committee was concerned about climate change and wished to identify ways in which it could be addressed. However, there were varying views on the best approach to take. Some members had concerns that requesting the establishment of a fossil free fund could be costly and would not necessarily achieve a better result than the current approach. These members felt that the safest, most responsible approach would be to continue with the current investment strategy, particularly as scheme members had been consulted on the Net Zero Strategy just two years ago and were supportive of the strategic direction the Fund was taking on carbon reduction. As performance and outcomes were monitored this would be kept under review. The Director confirmed that from the outset it had been agreed that the Net Zero Climate Strategy would be reviewed every three years and so would be due for review in 2026.

(xi) It was noted that partner funds in the pool could discuss whether they would like to apply a selective exclusion on thermal coal from funds that are run by LGPS Central. However, it was more complicated for LGIM as they invested for and with an enormous number of investors. Members noted that the Fund was already invested in an LGIM fund called the Low Carbon Transition Index Fund (LCTIF) where the stocks were weighted towards companies with low emissions and low fossil fuel reserves which already excluded thermal coal. Consideration could be given to progressively investing more in this fund.

(xii) Mr Pearson commented that key concern with establishing a new fossil free fund would be that in doing this, efforts would be displaced from what is currently being done by LGPS Central to address climate change, which was proving to be very successful. Hymans Robertson's recommendation was to remain invested and to continue to focus on engaging with those companies that needed to decarbonise, but to approach this more rigorously, instead of creating expensive parallel fund structures that might not be as effective. Members noted that Hymans Robertson had made some recommendations to strengthen the current engagement approach on a variety of ESG issues, but particularly climate change

At the invitation of the Chairman, Cllr Cartwright commented that he accepted the advice now provided and welcomed the healthy debate that had taken place in light of the motion he had originally put forward. It was clear, that whilst not considered appropriate now, this would be something that might be reconsidered in the future, which he thought partners who each had like minded aspirations regarding climate change, would support. Members commented that if LGPS Central were in the future to develop a fossil fuel free product it would be appropriate for the Committee to reconsider its approach.

Cllr Cartwright then moved an additional recommendation, seconded by Cllr Clarke, that greater clarity be provided regarding individual companies detailing those which were fossil fuel free and those that were not. This would ensure transparency to Members and scheme members on where the Fund was invested and help address some of the concerns now raised regarding transparency.

The Chairman invited officers to comment on the proposed additional recommendation before a vote took place. The Committee was advised that companies could not yet easily be identified as either fossil fuel free or otherwise as this was not one of the international standard classifications currently used by investors. However, the annual report to the Committee setting out performance against delivery of the Net Zero Climate Strategy did set out the Fund’s overall fossil fuel exposure and consideration could be given to breaking this data down into more detail on a company-by-company basis. Members noted, however that LGPS Central invested in thousands of different companies and some limitation on the data to be provided was therefore needed.

The Director also advised that consideration was being given to the measures available to assess outcomes and performance against the Net Zero Strategy, with a view to increasing the breadth of those currently reported to the Committee. He suggested that a report on the outcome of this work could be presented to the Committee in September to allow Members to also input into that process and to advise where they felt the identified measures still fell short of expectation. Member feedback would then help shape the annual report on the Net Zero Climate Strategy which was due to be presented in November.

In the light of the advice now received, Cllr Cartwright withdrew his amendment and confirmed he was satisfied with the approach suggested by officers. However, he sought assurance that the planned reports, both the report on the outcome of work to review the measures available to assess outcomes and performance against the Net Zero Strategy planned for September, and the annual report on delivery of the Net Zero Climate Strategy planned for November, would firmly address the concerns now raised regarding the lack of clarity and data provided in relation to where the Fund was currently invested with specific regard to fossil fuel. The Director agreed to circulate copies of reports considered by the Committee in 2023 to enable Members to provide initial feedback on where they considered more detail was needed. This would aid officers in preparing the report in line with Members expectations. The Director further confirmed that any Member of the Committee was welcome to contact him directly in advance of the meeting in September regarding what information they though was needed.

RESOLVED:

(a) That the maintenance of the target SAA allocation as described at paragraph 19 of this report be agreed;

(b) That the Director of Corporate Resources be authorised to make benchmark changes as per the guidance given at paragraph 11 of the report and the appendix to the report, with such changes to be delivered quarterly through the year, commencing for the June Local Pension Committee meeting;

(c) That the following two reviews be undertaken and presented to the ISC for consideration:

- A protection assets review as described at paragraph 12 of this report, with the final detailed scope of the review to be agreed between officers and Hymans Robertson.
- A review to maintain exposure to two asset classes which will be returning capital over the coming years (bank risk share investments and Timberland). The final scope of the review to be agreed between officers and Hymans Robertson.

(d) That the advice now provided by the Fund's investment advisor, Hymans Robertson, regarding the proposal to request LGPS Central to establish a fossil fuel free fund be noted and that it be agreed not to proceed with that proposal at the current time.

(e) That the Director be requested to:

(i) circulate copies of reports considered by the Committee in 2023 to enable Members to provide initial feedback on where they considered more information and data was needed to address the concerns now raised regarding the need for greater clarity and transparency around where the Fund was currently invested with regards fossil fuel;

(ii) present a report to the Committee in September, having regard to the feedback provided on (i) above, on the review of measures to be used to demonstrate the outcomes achieved and performance made against the Fund's Net Zero Climate Strategy to allow Members further input into that process and to advise where these still fell short of expectation;

(iii) present the annual report on the Net Zero Climate Strategy to the Committee in November taking account of Member feedback under (i) and (ii) above.

(iv) provide to Members after the meeting the data that showed LGPS Central was performing better than the Border to Coast fund with regard to its green house gas emission levels;

(f) That the recommendations put forward by Hymans Robertson, as detailed in paragraph 43 of the report, to be implemented as part of the Fund's Net Zero Climate Strategy be agreed.

118. <u>Draft Responsible Investment Plan 2024</u>

The Committee considered a report of the Director of Corporate Resources, the purpose of which was to seek the Committee's approval of the Leicestershire Pension Fund's Responsible Investment Plan 2024 to enable the Fund to further improve the management of responsible investment risks. A copy of the report marked 'Agenda Item 7' is filed with these minutes.

RESOLVED:

That Responsible Investment Plan 2024 attached to the report as Appendix A, be approved.

119. Pension Fund Training Needs Self Assessment.

The Committee considered a report of the Director of Corporate Resources, the purpose of which was to provide an update on the Training Needs Self Assessments undertaken, to identify training Members of the Committee were expected to complete to demonstrate a suitable level of knowledge and understanding and to set out options for the Committee to consider as part of the planned review of the current Training Policy. A copy of the report marked 'Agenda Item 8' is filed with these minutes.

Arising from discussion, the following points were made:

(i) The Chairman commented that, whilst training was not currently mandatory, this did appear to be the Government's intended direction of travel to make sure members of local pension committees had a good level of knowledge and understanding relevant to their role.

(ii) A Member commented that the Hymans Robertson on-line Aspire training modules provided a good, 'nuts and bolts' overview and members were encouraged to complete this. The modules were not time consuming and very manageable.

(iii) Members welcomed the suggestion of providing for different training requirements (such as starter, interim and advanced courses), taking account of the different levels of experience of Committee Members. It was suggested that this would provide a more flexible and targeted approach.

(iv) It was suggested that training events held in person were more beneficial as much was learnt from the questions raised by other members and from the informal discussions held with officers.

(v) A Member commented that a new Code of Practice from the Pensions Regulator had been introduced and which would come into force in March 2024. Members queried what the implications of this would for the Committee. The Director undertook to provide an update as part of a future regulatory update to the Committee.

RESOLVED:

a) That the report on the Pension Fund Training Needs Self-Assessment be noted;

b) That all members be encouraged to complete the training needs assessment, if not yet done, and to return this to officers by 14 February 2024;

c) That Members be encouraged to commit to progressing with completion of the Hymans Aspire training modules, noting that a record would be taken as at 31 March 2024 for the Fund's Annual report;

d) That Members feedback any further views on the current approach to the Fund's Training Policy as part of the review;

e) That the Director be requested to provide an update on the Code of Practice from the Pensions Regulator as part of a future regulatory update.

120. Date of next meeting.

RESOLVED:

That it be noted that the date of the next meeting would be 8 March 2024, at 9.30am.

9.30am – 12.30pm CHAIRMAN
26 January 2024