



LOCAL PENSION COMMITTEE – 18TH NOVEMBER 2022

REPORT OF THE DIRECTOR OF CORPORATE RESOURCES

AEGON – BOND MARKET UPDATE

Purpose of the Report

1. The purpose of this report is to provide the Local Pension Committee with background information on the Leicestershire Pension Funds (Fund) investments held with Aegon asset management and the performance of bonds generally.
2. This report will be supplemented by a PowerPoint presentation which will be presented at the meeting by representatives from Aegon.

Background

2. At the January 2022 Local Pension Committee meeting, the 2022 strategic asset allocation (SAA) was approved. This included allocations to bond investments; 4.5% to inflation linked bonds (IL), 4.0% to global multi asset credit, 2.5% to investment grade credit, 2.5% to emerging market debt (EMD) and 0.5% to short dated investment grade (SDIG). The Aegon fund has recently changed its name to the Aegon Short Dated Climate Transition Fund with the addition of a target to hold bonds with a 30% lower carbon intensity than the broader credit market index.
3. The Fund holds two bond investments with Aegon, IL bonds (target allocation 4.5%) and SDIG credit (target allocation 0.5%).
4. In March 2022 a decision was made by the Director of Corporate Resources using delegated powers to invest £60m excess cash into the SDIG fund. The investment was reported to the Pension Committee at its meeting on 10 June 2022.
5. As at 30 June the actual value of the two investments totalled £284m or 5.1% of total fund assets.

What are index linked bonds

6. An index-linked bond is a bond where payment of interest income on the amount invested is related to a specific price index, for example the Consumer Price Index (CPI). As a result, the bond's cash flows are adjusted to ensure that the holder of the bond receives a known real rate of return.
7. An index-linked bond is also known as a Treasury Inflation-Protected Securities (TIPS) in the U.S, and a linker in the U.K. The Fund has held index linked bonds within the Aegon index linked mandate and Ruffer (one of the three targeted return managers) are known to hold these bonds as part of their strategy.

What are short dated investment grade bonds

8. Short dated bonds are defined within the Aegon mandate as having less than four years to maturity, the point at which the capital is returned. The investment grade element relates to the issuers credit rating (these are issued by one of the big three agencies, S&P, Moody's and Fitch), with a rating better than BBB (on the S&P scale) meaning the issuer is of investment grade. Investment grade generally means that these issuers of credit are of higher quality and therefore more able to satisfy the terms of the agreement.
9. Short dated bonds have stronger capital preservation characteristics than longer dated bonds all other things being equal and the Fund recognised the need for a short dated product within the 2021 SAA.
10. The Aegon product with a shorter 'modified duration' (all other risks equal) will have a lower price volatility than the LGPS Central Investment Grade bond fund in which the Fund is also invested in. Simply, as maturity time of a bond increases so does duration and the bond becomes more volatile.

Summary performance of mandates

11. Aegon index linked bonds performance amongst other things will be covered in their presentation, a summary of performance is included below alongside benchmark performance. The benchmark is the FTSE all stock index linked total return.

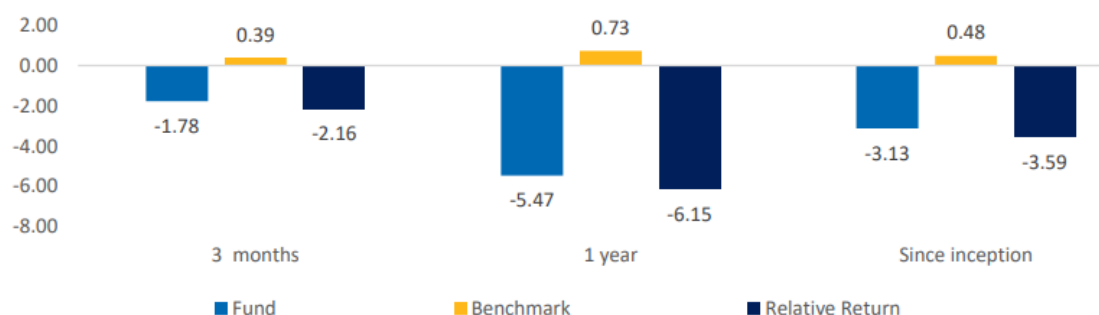
Fund Performance (% return)

Strategy	Q3 2022	YTD	Financial YTD	3 years [^]	Since inception
Index Linked	-8.91	-29.13	-25.02	-9.05	4.47
Benchmark /neutral	-9.33	-29.34	-25.23	-9.23	4.67
Geometric relative	0.46	0.30	0.28	0.19	-0.19

Performance based on mid-price valuations. Source: AAM UK as at 30 September 2022

12. Aegon's short dated product was launched in April 2021 and as such has a shorter history. The benchmark for this product is cash + 1.25% gross of fees over a rolling 3-year period.

Performance summary (%) to 30 September 2022



Recommendation

13. The Committee is recommended note the report

Equality and Human Rights Implications

14. None

Appendices

15. None

Background Papers

16. None

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