

Pension Fund Committee

Meeting to be held on Friday, 18 June 2021

Electoral Division affected: None;

Lancashire County Pension Fund - 2020/21 budget monitoring report

Appendix 'A' refers

Contact for further information:

Sean Greene, 01772 530877, Head of Fund, sean.greene@lancashire.gov.uk

Executive Summary

Details of the financial performance of the Fund for the year ended 31 March 2021, with a comparison to budget and prior year results, are set out at Appendix 'A'. The data included in the Appendix forms the basis of the year end statutory financial statements.

Recommendation

The Committee is asked to review the financial performance of the Fund for the year ended 31 March 2021 and make comments on the variances outlined in the report.

Background and Advice

The budget for the financial year ending 31 March 2021 was approved by the Pension Fund Committee on the 6th March 2020.

Budgeted net income to the Fund for the year was estimated at £219.1m before accounting for changes in the market value of investments during the year. This would be available for investment.

Appendix 'A' sets out an adverse variance of £73.8m against budget for the financial year – an additional £59.3m on the forecast reported to the committee on 12th March 2021. The key variances from budget are set out below. Please refer to Appendix 'A' for a more detailed breakdown of income and expenditure.

Contributions income

Actual £416.3m (Budget £373.1m, forecast at Q3 £417.0m)

Up-front payments for future service and deficit funding contributions were made by a number of employers within the Fund to cover amounts due for the 3 years to 31 March 2023. These prepayments amounted to £262.2m and were received by the Fund in April and May 2020. Accounting practice requires that these contributions be recognised on receipt rather than be allocated across the 3 financial years to

which they relate. The actual income received in the year was higher than budget due to increased uptake of the prepayment option following the budget being set. Other factors include the above budget pay award granted to public sector employees in the financial year.

There was a reduction in the amount of contributions income received compared to the last forecast (Q3 2021). This has arisen mainly as an employer going into administration and exiting the fund had a surplus of £0.5m. The resultant repayment of a surplus has been offset against employer contributions.

Transfers In

Actual £10.8m (Budget £12.5m, forecast at Q3 £10.0m)

Income from transfers is dependent on the number and timing of new members joining the Fund and is not an item that can be predicted with great accuracy. The actual is within the anticipated range.

Investment income

Actual £146.7m (Budget £214.5m, forecast at Q3 £174.3m)

Investment income consists mainly of income from the pooled investment funds (85% of the budget). Also included are direct property rental income, interest, foreign exchange differences and tax refunds. Over the year investment income received has been below budget by £67.8m.

As referenced in the budget monitoring paper presented to the Committee in March 2021, this has been primarily due to the economic impact of the pandemic. When making the last forecast the expected under recovery of investment income was £40.2m and there was some recovery in global equity distributions expected in the final quarter. However, this was not the case and the actual is £27.6m lower than previously forecast, due to:

- a significant proportion of this is the result of a delay in the distribution for the LPPI Infrastructure Fund which has fallen into the next financial year. Accounting practice is to recognise income on receipt so this will be reported in the next budget monitoring update; and
- Q4 distribution for the LPPI Global Equities Fund was lower than in previous periods, as a result of some companies within the GEF decreasing dividend payments due to the pandemic as well as a slight change in the composition of the portfolio which saw lower-dividend paying companies added.

Total benefits payable

Actual £291.8m (Budget £289.5m, forecast at Q3 £291.8m)

The forecast for the year is broadly in line with budget, with an overall adverse variance due to lump sum benefits being in excess of budget.

Transfers out

Actual £16.5m (Budget £15.5m, forecast at Q3 £16.2m)

The cost of transfers out of the Fund is dependent on the number and timing of members transferring their benefits to other funds. The actual is broadly in line with expectations

Investment management expenses

Actual £114.2m (Budget £70m, forecast at Q3 £82.8m)

The majority (90%) of the budget was for fees on the pooled investments. These costs are not directly invoiced to the fund but are charged to the pools. However, in line with CIPFA guidance on the reporting of management expenses an accounting adjustment is made to reflect the costs in the accounts. These costs are calculated on the basis of fair value of the pooled investments, with a performance element also payable on some investment manager mandates. The fee information is collected from underlying fund managers in arrears – with some managers reporting only half yearly or annually. As a result, the 'actual' costs for the year include estimates based on previously reported information.

At the last monitoring – presented to the Committee in March 2021 - it was forecast that actual spend (for investment management fees on pooled investments) would be above budget for 2020/21 with an adverse variance of £15.5m. At the year end, actual spend has now risen by £31.4m resulting in a variance of £46.9m - this variance against budget is due to the following factors:

- Investment management costs are calculated on the basis of fair value of the pooled investments, with a performance element also payable on some investment manager mandates. During the year the value of the Fund's assets has increased from £8.4 billion to £9.5 billion and this increase will result in an increase in fees;
- There was a very strong market rally resulting in a number of the Fund's Private Equity investments making substantial gains which also resulted in an increase in performance-related fees above the level anticipated in 2020. Additionally a high proportion of the Private Equity investments are mature, resulting in a higher level of distributions (and therefore performance related fees, which are often calculated on the distributions of realised investments);
- It should also be noted that some performance fees are paid once a threshold has been met then all the accrued fees to date are paid in that one period which can cover a number of years; and
- in the original budget set in 2020, there was some estimate of performance fees included. However, not all performance fees could be estimated and, as reported in last monitoring report, "It is the Fund's policy to not estimate performance fees

since they are difficult to predict and can either be an expense or, less often, a reduced cost where negative performance is reflected in a mandate." Therefore, although the variation in the quarter is large it is not totally unexpected.

Other expenses within this heading include LPP and other investment managers directly invoiced management fees which is showing a spend below budget for the year of £1.2m. The LPP direct costs are calculated on the basis of the market value of non-pooled assets, which is lower than budgeted. Reduction in market value of the non-pooled assets such as direct property holdings also reduces the non-pooled asset fees.

Fund administration and oversight and governance fees

Actual £5.1m (Budget £5.1m, forecast at Q3 £5.1m)

These cover the cost for administration expenses payable to Local Pensions Partnership Administration comprises core administration services, charged on a cost per member basis in addition to employer risk services and costs such as legal and actuarial fees incurred in running the fund.

Consultations

Local Pensions Partnership Investments Limited has been consulted for investment management fee and investment income analysis.

Implications:

This item has the following implications, as indicated:

Risk management

The full year financial performance is included in the Fund's annual report and statement of accounts for the year ended 31 March 2021. Regular budget monitoring is a key control for the Fund and assists in the financial management of the Fund, providing an indication of significant variances from expectations and informing future budgets.

Local Government (Access to Information) Act 1985

List of Background Papers

Paper	Date	Contact/Tel
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Reason for inclusion in Part II, if appropriate		
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