Bath & North East Somerset Council	
MEETING:	**AVON PENSION FUND INVESTMENT PANEL**
MEETING DATE:	**26 November 2024**
TITLE:	**Review of Investment Performance for Periods Ending 30 September 2024**
WARD:	ALL
AN OPEN PUBLIC ITEM	
List of attachments to this report: Appendix 1 – Mercer Performance Monitoring Report Appendix 2 – Brunel Quarterly Performance Report	

1. THE ISSUE

1.1. This paper reports on the performance of the individual portfolios and seeks to update the Panel on routine aspects of the Fund's investments. The report contains performance statistics for periods ending 30 September 2024.

1.2. The Mercer report at Appendix 1 provides strategic level information including total fund level performance, current funding level and an analysis of how the Fund's mandates are performing against expected strategic returns.

1.3. Appendix 2 is the quarterly performance report published by Brunel which includes further details on the performance of the Brunel portfolios and responsible investment activity undertaken on the Fund's behalf.

2. RECOMMENDATION

The Investment Panel:

2.1. **Notes information as set out in the reports.**

2.2. **Identifies any issues to be notified to the Committee.**

3. FINANCIAL IMPLICATIONS

3.1. Returns achieved by the Fund for the three years commencing 1 April 2023 will impact the next triennial valuation which will be calculated as at 31 March 2025. The returns quoted are net of investment management fees.

4. INVESTMENTS UPDATE

A – Fund Performance

4.1. The Fund's assets were £6,034m on 30 September 2024 and delivered a net investment return of 3.5% over the quarter which was 2.2% ahead of its strategic benchmark. Whilst there were some positive absolute performances across many of the Brunel listed equity portfolios, outperformance was largely driven by Brunel's Multi Asset Credit and private market portfolios, reflecting the strengthening backdrop for these assets.

4.2. The estimated funding level stood at 104% at 30 September 2024 (c. £220m surplus).

4.3. The discount rate is reviewed each month with a full review each quarter as per the agreed approach at FRMG. The changes each quarter are based on the expected CPI+ return outlook which is based on the Fund's investment strategy and hedging levels. It considers a combination of Mercer's capital market assumptions and real yield changes based on asset class correlations across the portfolio. The discount rate is sense checked for reasonableness by the Fund actuary taking into account the long-term sustainability of contributions. The September update allows for the updated discount rate of 5.31% p.a. (equivalent to a discount rate of CPI+2.8% p.a. at 30 September 2024).

4.4. Over 1 year to the end of September the Fund returned 14.8% in absolute terms and +2.7% in relative terms. The Brunel listed equity portfolios were positive over this period, although these returns were in line with or behind their respective benchmarks. Positive contributors to overall returns included the BlackRock LDI strategy, Brunel Multi Asset Credit as well as the Brunel private market portfolios.

4.5. Further details relating to performance attribution can be found in section 4 of Appendix 1.

B – Investment Manager Performance

4.6. Brunel reports on the performance of the assets they manage on behalf of the Fund. The report for each Brunel portfolio can be found on pages 19-39 of Appendix 2.

4.7. The third quarter of 2024 ended with healthy returns across most asset classes, despite several bouts of market volatility during the summer months. The long-anticipated start of interest rate cuts in the United States and new stimulus measures in China helped ease investor concerns over weaker US economic data. Developed equity markets generated strong returns, with parts of the stock market that had suffered most from high interest rates generally outperforming. Conversely, growth stocks gave up some of their recent outperformance as value stocks outperformed. Fixed income markets were buoyed by the prospect of lower rates, with government bonds and credit both delivering solid returns. Property has begun to show some tentative shoots of recovery, with investment activity over the quarter at its strongest in nearly two years. Whilst it was a positive quarter for most asset classes, it remains to be seen whether the US central bank has managed to control inflation without engineering a destructive recession.

4.8. In Brunel's listed market portfolios, returns were mixed, however these were offset by strong performances from Multi Asset Credit as well as the private market portfolios.

The Global High Alpha Equity portfolio returned -0.5% over the quarter, underperforming the benchmark (MSCI World) by 0.9%. This was largely driven by the portfolio's tilt to growth and quality, which significantly underperformed value over the quarter. Stock selection detracted, whilst sector allocation was also marginally negative as the benefit of being underweight energy (the poorest-performing sector) was more than offset by the negative impact of not holding utilities (the best-performing sector).

The Global Sustainable Equity portfolio was flat over the quarter with a net return of 0.0%, marginally underperforming its benchmark (MSCI ACWI) by 0.6%. The portfolio's underweight to large-cap technology stocks initially led to some outperformance during the quarter, but as tech stocks rallied following the US rate cut, the portfolio ended the quarter flat in absolute terms.

The PAB Passive Global Equity portfolio returned 0.4% over the quarter, in line with the market capitalisation parent benchmark. The portfolio benefited from limited exposure to the energy sector which was positive for returns. The divergence in performance of the so-called Magnificent Seven stocks had implications for portfolio returns with Apple and Meta making positive contributions, whilst Microsoft, Amazon and Alphabet were the biggest detractors.

The Diversifying Returns Fund (DRF) returned 1.7% over the third quarter, marginally behind the cash benchmark (SONIA 3+%) of 2.1%. Market volatility, combined with currency movements provided headwinds for the underlying constituents and although all managers delivered positive absolute returns, on aggregate these fell short of the index. However, during the sell-off, the portfolio did demonstrate its defensive characteristics, falling far less than the benchmark in one of the short, sharp market corrections.

Multi Asset Credit (MAC) had a positive quarter returning 3.9%, comfortably ahead of its primary cash plus benchmark (SONIA +4%) return of 2.3%. The Fed's 50 basis point rate cut was the catalyst for the outperformance, resulting in favourable returns for fixed rate asset classes. The strong performance was led by Neuberger Berman, who's higher duration exposure (a measure of the sensitivity to changes in interest rates) boosted performance, with the other two managers Oaktree and CQS also posting positive returns.

In private markets, the reduction in interest rates by major central banks across the quarter was generally seen as a positive for infrastructure investments. Many infrastructure assets continue to exhibit strong defensive characteristics and given the diversified nature of the Fund's portfolio (across sectors, geography and business models), performance should be well supported. Global renewables policies also acted as a tailwind, with the new Labour Government committing heavily to increase investment through the newly formed Great British Energy and National Wealth Fund. In private debt, portfolio performance was generally positive. Although M&A activity has been steadily increasingly it remains soft for the year as a whole, resulting in an increase in lending to incumbent borrowers through refinancings.

In Secured Income, the performance of the long lease property sector, which accounts for a large proportion of the portfolio, continues to turn positive after two years of declines. This has largely been driven by sustained rental growth, with distribution yields at historical highs above 5%, and resilient occupational demand, while some sectors are starting to experience capital appreciation. This, coupled with a more benign outlook for inflation and stable borrowing rates provides a positive backdrop for the asset class that should enable continued improvement across sectors.

INVESTMENT STRATEGY AND PORTFOLIO REBALANCING

4.9. **Returns versus Strategic Assumptions:** Returns versus the strategic assumptions used during the 2023 investment review can be found on p15/16 of Appendix 1. Equity and liquid growth assets classes are generally in line with or exceeding expected returns. Property is below its modelled return and the other private market mandates are largely still in build-up phase or do not have a sufficient track record to properly compare against strategic return assumptions.

1.1. **Rebalancing:** Post period-end, the Fund rebalanced its equity overweight by 5% bringing the overall equity allocation down to c. 45%, which is within the rebalancing range set out in the Investment Strategy Statement. This was implemented via the synthetic equity strategy held in within the QIF. Further information relating to this decision is included in Item 11: Risk Management Framework Review.

1.2. **Responsible Investment (RI) Activity**: A summary of portfolio carbon metrics measured by Brunel over the quarter is included on page 10 of Appendix 2. The Fund undertakes in-depth carbon analysis on an annual basis and publishes the results in its Annual Responsible Investment Report, which is cleared by Committee in September.

4.10. **Voting and Engagement Activity:** As a responsible investor, we actively endorse collaborative engagement and seek to use our power as a shareholder to encourage corporate change. Voting and engagement are delegated to the Brunel Pension Partnership for the actively managed equity portfolios and to Legal and General Investment Management (LGIM) for the passive portfolios. On significant issues, Brunel may request that their shares held by LGIM are split out and a different vote made. The voting records of Brunel and LGIM at company meetings held over the last quarter are summarised in the following table:

Votes cast at company meetings in the quarter to 30 September 2024:

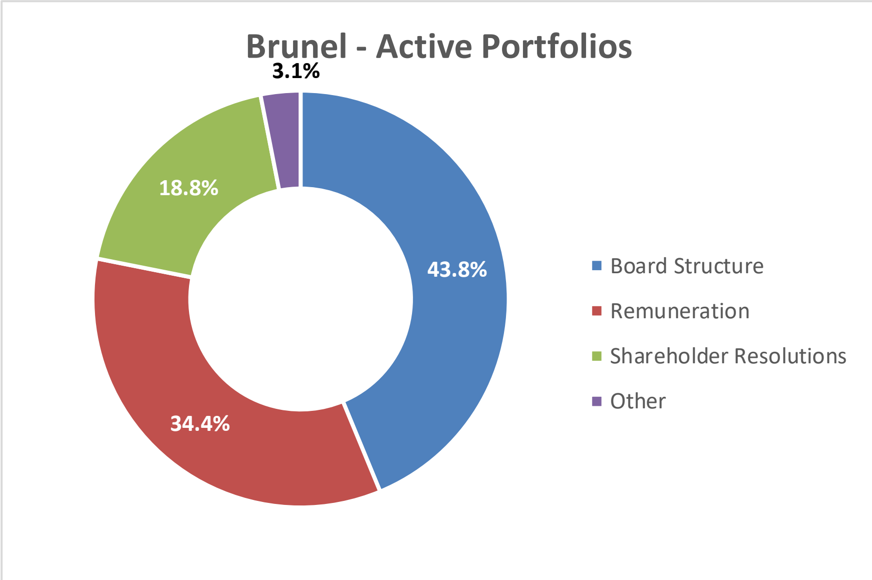
	Quarter to 30 September 2024		
Manager	**Number of Meetings**	**Number of Resolutions**	**Votes against management recommendation**
Brunel/LGIM - Passive Portfolios	63	887	165
Brunel - Active Portfolios	16	241	32

Points to note:

a) Brunel and LGIM actively vote the shares held within their funds on behalf of their client funds, including Avon.

b) The votes against management recommendations will reflect matters where there is concern that the company is not addressing the relevant issue and managing it effectively. The Fund would expect that votes against management should be primarily on the priority areas set out in the Fund’s Investment Strategy Statement. An analysis of the issues where votes have been cast against management recommendations is set out below.

Votes against management recommendation by issue – Quarter to 30 September 2024

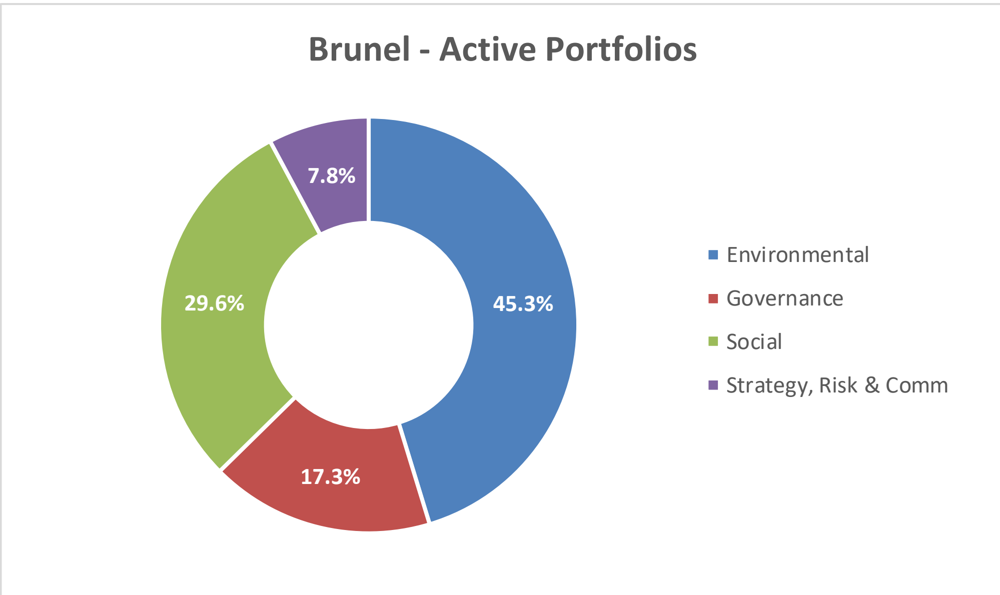


1.1. **Engagement:** Brunel conduct significant engagement with investee companies on behalf of the Fund. A breakdown of the engagement undertaken over the last quarter is summarised as follows:

Company engagement in the quarter to 30 September 2024:

	Quarter to 30 September 2024	
	Number of Companies	Number of Issues
Brunel - Active Portfolios	120	371

Breakdown by issues engaged on:



Further information on Brunel's engagement activity can be found on their website using the following link:

https://www.brunelpensionpartnership.org/library/

5. RISK MANAGEMENT

5.1. An effective governance structure, defining clear responsibilities, and ensuring that the decision-making body has an adequate level of knowledge and access to expert advice, is a key aspect of the risk management process.

6. EQUALITIES

6.1. A proportionate equalities impact assessment has been carried out using corporate guidelines and no significant issues have been identified.

7. CLIMATE CHANGE

7.1. The Fund is implementing a digital strategy across all its operations and communications with stakeholders to reduce its internal carbon footprint in line with the Council's Climate Strategy. The Fund acknowledges the financial risk to its assets from climate change and addresses this through its strategic asset allocation to Paris Aligned Global Equities, Sustainable Equities and renewable energy opportunities. The strategy is monitored and reviewed by the Committee.

8. OTHER OPTIONS CONSIDERED

8.1. None

9. CONSULTATION

9.1. The Head of Pensions has had the opportunity to input to this report and has cleared it for publication.

Contact person	Rebecca Whelan, Senior Investments Officer (Tel. 01225 395355)
Background papers	Data supplied by Mercer, Brunel & State Street Performance Measurement
Please contact the report author if you need to access this report in an alternative format	