London Borough of Barnet Pension Fund
Funding Strategy Statement covering the period 1 April 2023 to 31 March 2026

This preface to our Funding Strategy Statement covering the period 1 April 2023 to 31 March 2026 sets out the specifics of the London Borough of Barnet Pension Fund and the key areas we have considered to inform our Funding Strategy. The preface is supported by a more detailed document prepared in collaboration with our advisors, which also includes links to important Fund policies.

1. What is our overall objective?

1.1 Our overall objective is to ensure there are sufficient resources to meet pension benefits as they fall due.

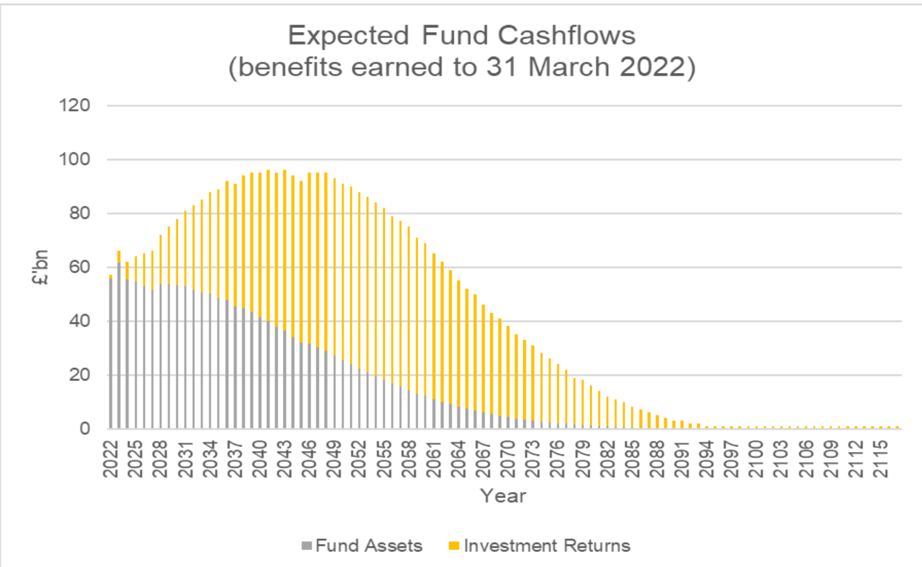
1.2 Our resources are:
- the assets we hold within the Pension Fund
- the return we may get on those assets in the future; and
- the ability for us to ask for contributions from our employer base in the future

1.3 A secondary condition is that we take risk in a measured way to ensure the overall efficiency and cost effectiveness of funding. Because we are taking risk, we need to manage those risks.

2. How are we doing against our objectives?

2.1 At 31 March 2022, and at a "Whole of Fund" level, we had c£1.5bn of assets. The nominal (i.e. not discounted) value of the benefit payments promised to that date, based on Hyman's central view on long-term inflation, was c£4bn. This leaves c£2.5bn to be funded via investment returns or additional contributions.

2.2 The balance between how benefits earned to date are expected to be met through current assets and investment returns on those assets is illustrated below – as can be seen, the majority of benefits are expected to be met through investment returns (orange area), which is why focusing on investment returns is so important.



2.3 Our actuary has calculated that we would need to achieve an annual return of at least 4.7% to meet these payments without requiring further contributions from our employers. Our actuaries assess that the probability of achieving this level of return over the long-term is around 70%.

2.4 This implies that, whilst there is a positive likelihood that further money isn't required to fund benefits built up, there is a material probability that the current assets are not sufficient to cover the benefits already promised and that further contributions may be required. This indicates the level of risk being taken to fund our pension obligations.

2.5 After considering the provisional results of the 31 March 2022 valuation and experience over the inter-valuation period, we are currently comfortable with our funding progress and the level of overall risk we are taking at a "Whole of Fund" level. However, the position for employer groups is more nuanced.

2.6 An important consideration when thinking about our employer groups and overall risk appetite is the ability to request contributions in the future.

3. Ability to request further contributions in the future

3.1 The ability for us to request contributions from employers in the future is a very important part of our overall risk management framework and funding strategy. This ability is constrained by the following two factors:

- The ability of the employer to flex its operating costs to allocate more resources towards the pension scheme if required - *For the majority of our employers this is limited without due notice (possibly a number of years). We also do not wish to negatively impact public service delivery because of increasing pension contributions*

- How confident we can be that the employer will be around in the very long-term to support the pension scheme - *For the majority of our employers we can be very confident about this, but for some employers, such as universities and colleges, we may need to take a more cautious view – not because we have any specific concerns around those employers within the Fund, but more reflecting the general uncertainty of any organisation who cannot guarantee future revenue streams*

4. Taking investment risk

4.1 In general, we are required to invest in assets that do not provide a guaranteed return. This means that there is a risk that the asset performance is lower than that assumed by our actuaries to determining funding contributions.

4.2 A key part of our funding strategy is how we might manage periods where assets do underperform relative to our assumptions. In this situation, further contributions may be required.

4.3 There are two broad ways asset under performance can be managed:

- We use time to smooth out periods of underperformance. This approach assumes underperformance is followed by a 'reversion' to a norm through overperformance. This is risky because the position may not revert

- We set a higher funding target to reduce the probability of underfunding. This approach reduces our risk but is potentially inefficient as it may lead to too much capital being tied up in the pension scheme or the pension scheme becoming over funded. Depending on the time frame used to reach such a funding target, contribution requirements to get there may be, in themselves, unaffordable

4.4 For our tax raising bodies and for those with an underlying government guarantee and / or bond we would generally seek to use a mixture of time and controllable increases to cash contributions to manage periods of underperformance. This may be achieved by taking less prudence in the Funding Target and / or allowing a longer timeframe to recover deficits.

4.5 For our non-tax raising bodies it may not be appropriate to take less prudence and / or increase the time to recover deficits. From a risk management perspective, we therefore may want to reduce the likelihood of underperformance by seeking to move to a higher funding target gradually over time. We will be looking to consult with employers over the period until the 31 March 2025 valuation to consider how best to achieve this.

4.6 For completeness, we may also keep back additional reserves when performance has been better than expected to provide a further cushion against periods of underperformance and we will consider whether it would be appropriate to reduce cash on case-by-case basis.

5. Can an LGPS request security?

5.1 Yes, to protect against the risk of an employer not being there in the future we may explore how additional security can allow us to adopt a less prudent funding target. However, additional security may help reduce an employer's cash contributions, but it does not, in itself, reduce an employer's risk unless the security embeds increased commercial certainty and / or is combined with a change in investment strategy.

6. Experience since 31 March 2019

6.1 Our Funding Strategy will evolve over time and our experience over the last three years has, of course, informed our Funding Strategy for the period 1 April 2023 to 31 March 2026.

6.2 In terms of overall commentary, it is no understatement to say that the world has experienced significant change since the last valuation assessment at 31 March 2019. Covid-19 has had a dramatic impact on mortality rates as well as global markets, but we have also seen:

- the formalisation of Brexit, which has changed the UK's trading relationships which has caused some market uncertainty;
- a significant rise in interest rates as Central Banks try to control increasing inflation; and

- the emergence of a conflict in Ukraine and the shock to energy supplies that has followed

6.3 As a Pension Fund investing in risky assets, we are not immune to the impact of these factors: the one certainty we be sure of is that we are now facing greater uncertainty. We will be undertaking a full investment review in the Spring of 2023 and we are also evolving our Responsible Investment strategy and overall investment procedures to consider how we can be more nimble and flexible in our decision making.

6.4 Against this backdrop, the experience over the period 1 April 2019 to 31 March 2022 for Investment Returns, Inflation, Longevity and Data is summarised below:

Item	Experience	Commentary
Investment Returns	8.9% p.a. on average), compared to required return of 4.4% p.a.	Favourable investment returns have contributed to around £100m improvement in funding position over the valuation period. In context, over the inter valuation period, there was substantial support for capital markets via Central Banks quantitative easing programmes which, given the levels of inflation, is unlikely to continue. This could put pressure on capital values more generally from 2023 and is something we need to be mindful of as we conduct our investment review.
Inflation	5.4% over the period compared to 7.1% assumed	Inflation over the valuation period was around 2% lower than what was assumed at 31 March 2019. This has contributed to around a £30m gain in the overall funding position. However, the future outlook for inflation is very uncertain, with CPI increasing significantly since the 31 March 2022 valuation date. Looking forward, Hymans central estimate for future inflation is that CPI will average around 4% to 5% overr the next 5 years, then gradually reverting to the Bank of England's long-term target for inflation of c2%. Markets are pricing in a higher level of long-term inflation (at around 3.0% to 3.5%, so significantly higher than the Bank of England target). This difference is indicative of the level of future risk we face in relation to inflation. Allowing Hymans central estimate for future inflation increases liabilities by around £100m relative to the assumptions adopted in 2019. Allowing for market pricing for inflation would increase liabilities by a further c30% (£450m LBB analysis) relative to the assumptions adopted in 2019.

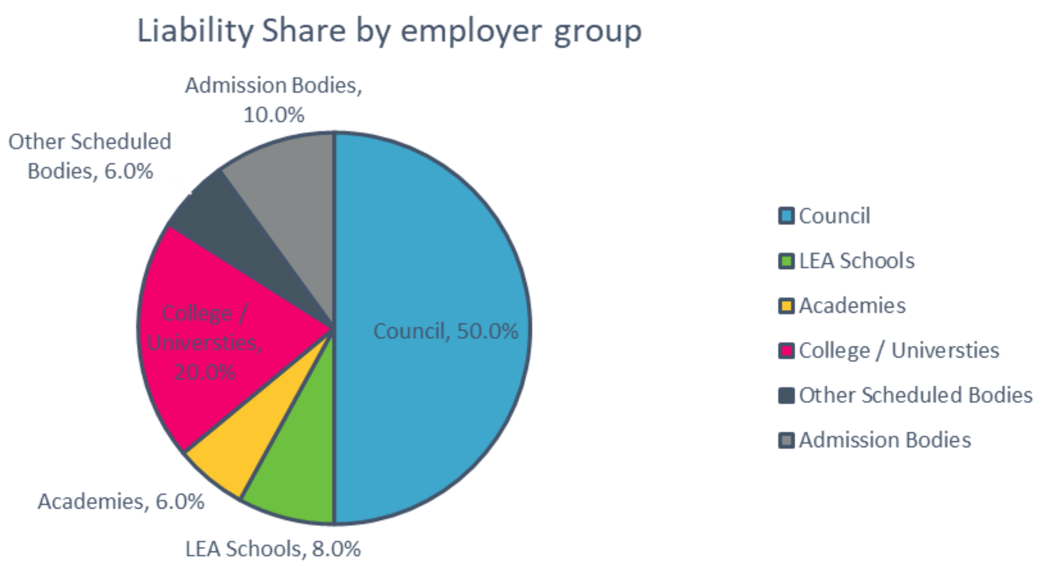
Item	Experience	Commentary
Mortality	Not analysed	Whilst the number of excess deaths increased dramatically in 2020 and 2021 due to the impact of Covid, these deaths were predominantly at older ages (80 years plus) and so, from a Pension Fund perspective, the financial impact has not been as material as some of the other issues discussed here, such as investment returns and inflation. The longer-term impact due to Covid is not known. On advice from our Actuary, we have actually marginally strengthened our longevity assumptions but will keep the position under review fort the 31 March 2025 valuation.
Data	£50m impact	There has been a process of rectifying data records since the last valuation after it was found that the overall level of record keeping was poor. There is a significant 'true-up' number of £50m to reflect the more up-to-date data used. Given the significance of this item we will be analysing the differences between the 2019 and 2022 data to understand where the main areas of differences are.

Areas of focus for 31 March 2022

7. Employer Groups

7.1 The Barnet Pension Fund has a diverse range of employers, and a higher overall allocation to non-taxing raising bodies relative to most other LGPS funds.

7.2 A summary of the different employer groups at 31 March 2022 is provided below:



7.3 The average level of exposure to non-tax raising bodies for the LGPS in general is around 10% based on information provided in Aon's 2018 report on non-tax raising bodies. This means the Pension Fund has over double the level of exposure than that experienced more generally.

8. Implications of maturing scheme

8.1 When the flow of new entrants towards a pension scheme slows it means that, overall, the average age of pension scheme members starts to increase and the 'duration' (i.e. time frame) of future cashflows starts to reduce.

8.2 A consequence of this is that the time horizon that risk can be comfortably taken reduces. This position is compounded if the Pension Fund cannot be 100% confidence in the ability of the employer to make contributions in the future – i.e. when there is a situation where the time horizon for paying benefit starts to shrink and the visibility for being able to rely on future pension contributions is limited, the sensible risk mitigating strategy is to plan to take less risk in the future.

8.3 This is reflected in the Fund's general policy of funding 'cessation' liabilities (i.e. liabilities without employer backing) on a "least risk" actuarial basis.

8.4 For the Council's obligations, this is not a concern, indeed the inflow of new members that are expected to arise out of the in-sourcing of certain contracts may increase the duration of obligations overall for Council – that said, depending on the contribution agreement following the 31 March 2022 valuation discussions, the Fund may switch to being a net dis-investor of assets as benefit outgo starts to exceed income.

9. The Council

A summary of the approach funding approach adopted for each employer group in 31 March 2019 is provided below, together with a high-level summary of any proposed changes from 31 March 2023.

2019 approach

Funding Consideration	Comment
Funding target	Ultimate target consistent with probability of success of at least 75% based on long-term investment strategy (based on Hymans; proprietary ESS model)
Financial position relative to Funding Target	78%
Timeframe proposed to reach funding target	17 Years (assumes at least 70% probability of success)

Overall comment on Council Funding approach

9.1 Based on provisional results, the funding for the Council's share of obligations has progressed well. We are not seeking to amend the funding approach for the Council, apart from adjusting the timeframe for meeting the Funding Target to ensure overall stability of contribution rates.

10. Other Scheduled Bodies (Tax Raising or wholly owned by the Council)

10.1 Funding approach was consistent with the Council's. Aggregate Funding for this group was 81% of target at 31 March 2019.

10.2 Based on provisional results, funding for other Scheduled Bodies has progressed well. We are not seeking to amend the funding approach for other Scheduled Bodies, apart from adjusting the timeframe for meeting the Funding Target to ensure overall stability of contribution rates.

11. Academies

11.1 Funding approach was consistent with the Council's. Funding was 78% of target at 31 March 2019 across all academies. Academies obligations are ultimately underwritten by DfE which means we are comfortable taking a relatively long-term view for this employer group. That said, we still need to be mindful of stability, because it is responsible to do so and a requirement of the regulations.

11.2 Based on provisional results, funding for academies has progressed well. We are not seeking to amend the funding approach for academies at an aggregate level, however, note comment below which may impact individual academy contribution rates from 31 March 2023.

11.3 In 2019 contribution rates were set as the average across all academies. Whilst contributions were set as a common rate, asset and liabilities were not pooled. This means that some academies may have been over / under paying relative to their true cost. We believe this approach, whilst easier to administer, introduces risk of systematic under or over funding for some academies.

11.4 We will therefore be amending the approach so that each academy pays the contribution rate consistent with the liabilities and asset share. We will enter into discussions with academies where the change in contribution rate is more than 2% to discuss whether smoothing would be appropriate.

12. Admitted Bodies

12.1 We take a range of approaches for Admitted Bodies, and these are documented within the respective admission agreements and other contractual documentation associated with each employer. Overall, Funding for Admitted Bodies has progressed well and we are not proposing a change to the overall approach. We are also not envisaging a significant change to contribution rates.

12.2 We have a number of relatively “small” employers joining the scheme with a handful of members (e.g. to service contracts for schools around catering) and the admission process is complex. Over the period to 2025 we will review the admission process to see whether it can be made simpler without prejudicing the overall security of the scheme materially.

12.3 The Council is looking to in-source a number of contracts over the next few years. All things being equal, this will increase our overall membership and pace at which the Fund grows. Whilst it may increase the overall duration of the Scheme, which is potentially positive from the perspective of us being able to take a long-term view on investments, it also potentially increases risk as the Pension Fund increases in size relative to the employer base.

13. Universities / Colleges

2019 approach

Funding Consideration	Comment
Funding target	Ultimate target consistent with probability of success of 75% based on long-term investment strategy (based on Hymans; proprietary ESS model).
Financial position relative to Funding Target	94%
Timeframe proposed to reach funding target	15 Years (assumes 70% probability of success)

13.1 We note that the approach taken in 2019 for Universities and Colleges was not significantly different to the approach adopted for the Council (with the core difference being the timeframe to reach target set as 15 years rather than 17 years).

13.2 Given that the Universities / Colleges do not have the same level of long-term covenant visibility as the Council, the level of risk we are taking is, relatively, much higher. This is compounded given our relatively high exposure to these types of employers as a percentage of the overall Fund.

13.3 Of potential concern for the 2022 valuation is the level of long-term inflation risk we are exposed to, particularly given our advisors central view on long-term inflation, which is broadly in line with Bank of England long-term targets, but significantly different to that implied by market indicators.

13.4 We are also aware that steps have been taken by Middlesex University to provide alternative pension provision. This will significantly reduce the flow of new entrants into the Fund. Whilst this will slow the build-up of liabilities for this employer, which is positive from a risk management perspective, it does potentially accelerate the point at which we may need to start planning for cessation and accelerates the maturation of the Middlesex University section of the Fund.

13.5 As noted in Section 8. above, where the maturation of obligations happens, it is sensible to start to plan to take less risk. This is compounded when there is also a limited level of covenant visibility associated with the employer.

13.6 Because of this we will be seeking to switch the Funding Target for Middlesex University to a Least Risk funding basis. The timeframe and probability of success will depend on affordability, but provisionally we believe it would be appropriate to target a 15-year time horizon with at least a 60% probability of success.

13.7 For Barnet & Southgate College we will not be amending the Funding Approach for the 31 March 2022 valuation, but we will keep the situation under review pending the outcome of the Government's review of whether to provide an underlying government guarantee to Further Education pension liabilities.

14. Supplementary Information

14.1 The attached document prepared in conjunction with our advisors sets out further details of:

- How employer contributions are calculated
- How assets and liabilities are calculated
- What happens when an employer joins the fund
- What happens when an employer leaves the fund
- What the statutory reporting requirements are

The document also provides further information on the:

- The regulatory framework around setting a Funding Strategy Statement
- Roles and responsibilities
- General risks and controls
- Actuarial assumptions