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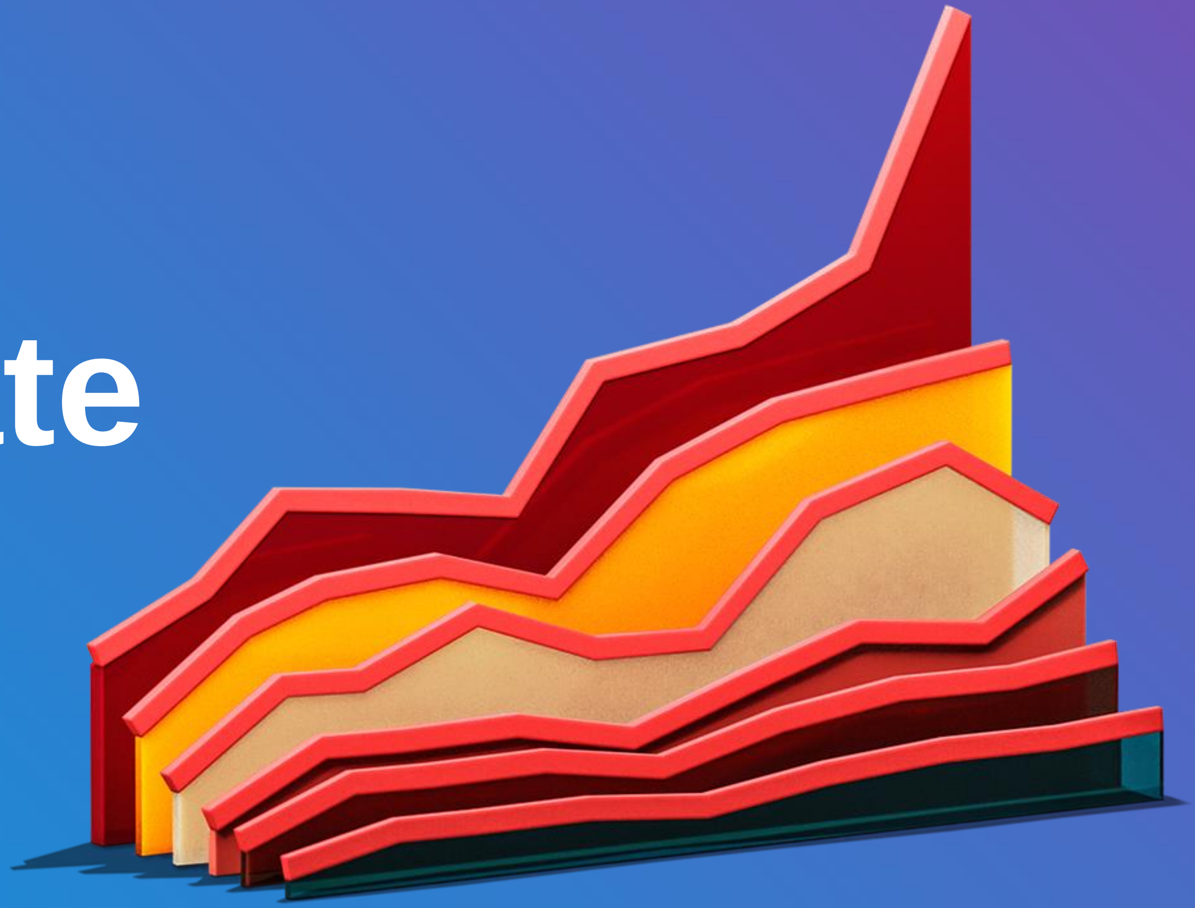
30 June 2024 Funding Update

Islington Council Pension Fund

August 2024



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Funding Update – 30 June 2024
Whole Fund

Headlines

2022 valuation funding level 96% deficit £79m

"Like for like" funding level 91% deficit £189m

Updated discount rate / mortality assumption funding level 99% deficit £17m

	31 March 2022 Valuation	30 June 2024 Update (Like for Like)	30 June 2024 Update (Discount rate sensitivity / Mortality)
Assets	£1,787m	£1,993m	£1,993m
Liabilities	£1,866m	£2,182m	£2,010m
Funding Level	96%	91%	99%
Surplus / Deficit	-£79m	-£189m	-£17m
Primary Contribution Rate	18.4%	18.4%	18.2%
Real Discount Rate - Past Service	CPI+1.55%	CPI+1.55%	CPI+2.00%
Real Discount Rate - Future Service	CPI+2.00%	CPI+2.00%	CPI+2.00%
Life Expectancy Assumption	2022 val baseline CMI 2021 1.75%	2022 val baseline CMI 2021 1.75	2022 val baseline CMI 2022 1.75%

"Like for like" figures - no allowance for the material change in yields since the valuation date .

"Updated discount rate sensitivity/mortality" figures - allow for some *but not all* of the upward movement in yields and other factors that have led to changes in expected returns. Broad allowance has also been made for the impact of the CMI 2023 outcomes (leading to a small reduction in liabilities).

A full reassessment of the expected return outlook / investment strategy changes and stochastic modelling of discount rates will be undertaken as part of the interim review alongside updated mortality trends.

What's happened since 31 March 2022?

Market Conditions

Fund investment returns, as provided by the Fund over the period 31 March 2022 to 30 June 2024, have been c10-11% since 31 March 2022 driven by significant performance of c12% over 2023/24 which offset the negative returns that emerged over 2022/23.

This compares with the long-term required return from the funding strategy of c11% over the period and so overall, returns have been broadly in line with those required despite volatility in the markets over the period.

Inflation

Allowance for a higher 2023 Pension Increase was built into 2022 valuation outcomes, but high inflationary environment continued beyond the valuation date, only "slowing" down over the past 6 months or so and reverting back to levels closer to the long-term assumption.

This funding update allows for the impact of inflation since 31 March 2022, including the 2024 pension increase (c6.7%).

Strategy Updates

Since the valuation, The Fund has carried out a review of its investment strategy.

The proposed changes will slightly increase the best estimate real investment return and provides a marginally higher likelihood of meeting the return requirement for the funding assumptions. However, this comes with a small amount of additional risk/volatility of return also. A full stochastic analysis of expected returns will be carried out as part of planning for the 2025 valuation.

Notes to the calculations

- The 30 June 2024 liability figures are based on an approximate roll-forward of the 31 March 2022 valuation position. They do not reflect the impact of membership experience over the period. They allow for the estimated impact of inflation, interest, benefit accrual, changes in assumptions and benefit cashflows (actual to 31 March 2024 as provided by the Fund and then estimated thereafter).

30 June 2024 Update – What next?

2024 Interim Review

- Interim Review as at 30 September 2024 will be undertaken in the autumn and outcomes reported to Committee at the end of the year.
- Alongside the updated funding position, further consideration will be given to discount rate derivation, national life expectancy changes, data quality and membership profile changes, plus potential outcomes for Council and strategic funding decisions e.g. treatment of surplus etc.
- The interaction with investment strategy will also be considered further.

Demographic Analysis

- In preparation for the 31 March 2025 actuarial valuation next year a full review of demographic assumptions will be undertaken in Q4 2024. Whilst the main focus will be on Fund-specific life expectancy, other assumptions (ill-health retirement, commutation etc.) will also be considered.
- Exercise will reflect local and national experience and trends and will also impact on assumptions for accounting / termination.
- Outcomes to be issued in Q1 2025 and incorporated into initial valuation outcomes to be discussed in Q2.

2025 Valuation

- Broadly speaking the timescales for the 2025 valuation will reflect:

- 31 March – 30 June: Initial discussions on strategy, reflecting outcomes from above exercises and 31 March conditions.

- 30 June – 30 September: Provision of membership data and processing of initial Whole Fund (and Council) positions and drafting Funding Strategy Statement (new guidance expected in early 2025)

- 30 September – 31 December: Agree funding strategy parameters to generate results for all employers and begin funding strategy consultation process

- 31 December – 31 March: Consultation process concludes, liaison with employers on final contribution outcomes and formal actuarial certification of new rates from April 2026

Appendix

2022 Valuation Recap

Key results	Whole Fund	Council
Assets	£1,787m	£1,671m
Liabilities	£1,866m	£1,757m
Funding level	96%	95%
Surplus/(deficit)	-£79m	-£86m
Primary Contribution Rate	18.4%	18.3%
Recovery Period	16 years	16 years
Secondary Contributions - 2023/24 - 2024/25 - 2025/26	Allowing for Prepayments £14.6m £0.4m £0.4m	Allowing for Prepayments £14.3m £0m £0m
Real discount rate – past service	1.55% p.a.	
Probability of attaining discount rate	69%	
Real discount rate – future service	2.00% p.a.	
Probability of attaining discount rate	63%	
Life Expectancy Assumption	2022 Valuation Baseline – CMI 2021 1.75% LT	

Comment

- The Council contribution outcomes took into account the special contribution of £20m paid towards the end of 2022/23 prior to contribution rates being certified.

30 June 2024 Update – Key Considerations

Returns outlook

Gilt yields have risen materially over the last 12 months, which has led to many stochastic models pointing to a significant increase in expected future investment returns, and therefore the valuation discount rate. If such higher discount rates are applied mechanically without adjustment, this results in potentially material funding improvements being recognised at the current time - despite falls in asset values. Such funding improvements for LGPS Funds are being widely reported in the press.

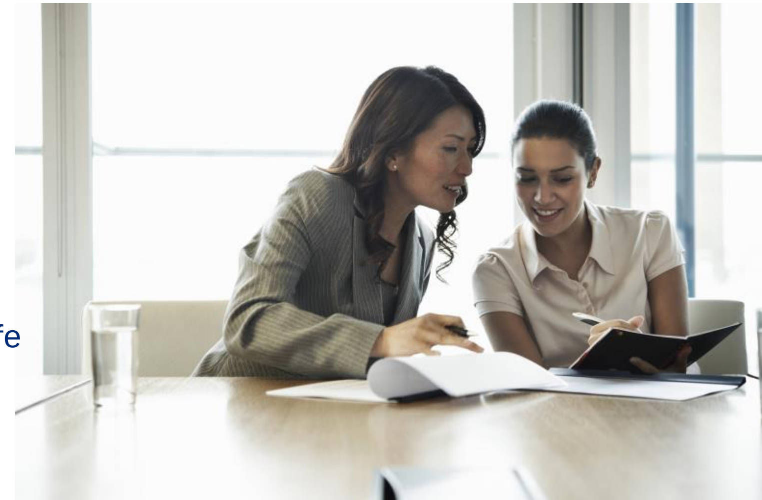
However current conditions are volatile, creating more uncertainty and more “model risk”. This would suggest an increase in prudence margin/likelihood of success is needed when setting discount rates using these models, at least until the outlook begins to look more stable.

As requested by the Fund, we have carried out the funding update showing a sensitivity allowing for some but not all of the upward movement in yields. We have allowed for around 15% of the Fund’s assets to be correlated with gilt yield movements, which takes into account the broad asset strategy adopted. However, the current financial conditions provide much more flexibility in where to position the discount rate.

Further consideration to be given to the range of potential outcomes as part of the funding strategy work in the lead in to the 2025 valuation, taking into account views on economic outlook, contribution affordability and sustainability for employers at that time. We have not sought to pre-empt this work at this stage in the valuation cycle

Investment strategy

2022 Valuation outcomes were based on expected real return outlook as at 31 March 2022 taking into account Fund’s investment strategy. As the change in investment strategy is expected to allow for only a marginal increase in expected return, and alongside it a marginal increase in risk, we are comfortable that detailed review of the impact on the discount rate is not required for this funding update, taking a pragmatic approach. The new strategy will be considered as part of the funding strategy work in the lead in to the 2025 valuation.



Life Expectancy

In June 2023, CMI released outcomes of their 2022 investigation. Relative to the funding assumptions underlying the 2022 valuation calculations, a small reduction in liabilities and future service rate expected as a result. Whilst it is early days and full analysis has yet to be undertaken, indications for the CMI 2023 analysis are for a further fall in projected life expectancy and a further fall in liabilities.

Actuarial Advice

- We have prepared this document for the Administering Authority for the purpose of understanding the development of the funding position of the Fund and factors that have influenced this, for information purposes.
- “Technical Actuarial Standard 100: Principles for Technical Actuarial Work (v2)” and “Technical Actuarial Standard 300: Pensions (v2)” issued by the Financial Reporting Council applies to this presentation and the associated work, and we confirm compliance with this standard. This presentation should be read in conjunction with our report on the actuarial valuation of the Fund as at 31 March 2022.
- Unless otherwise stated, we have relied on the information and 2022 member data plus other data supplied to us in preparing the information, without independent verification. We will not be responsible for any inaccuracy in the advice that is a result of any incorrect information provided to us.
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- This presentation is correct at August 2024. It will not be updated unless requested.