SOUTH YORKSHIRE PENSIONS AUTHORITY

Medium Term Financial Strategy

2023/24 to 2025/26

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1. Foreword

1.1 Foreword to the Medium-Term Financial Strategy 2023/24 to 2025/26

1.1.1 This Medium-Term Financial Strategy (MTFS) has been produced by the South Yorkshire Pensions Authority to cover the period from April 2023 to March 2026. This period will see the continued emphasis on supporting the overall Corporate Strategy in building on the continuing improvement journey for the organisation, as well as continuing the transition of the Authority's remaining investment assets into the pooling structures provided by the Border to Coast Pensions Partnership.

1.1.2 The strategy covers both the costs of running the Authority's operations and the income and expenditure of the pension fund, although this is significantly more difficult to forecast than routine running costs such as staff salaries.

1.1.3 Any financial strategy is based on a series of key assumptions and throughout this document these assumptions are identified and are subject to ongoing review as part of the process of regular budget monitoring and producing updates to this strategy.

1.1.4 The financial strategy (and the budget which is the annual expression of the strategy) is, put simply, the financial expression of the policy position set out in the corporate strategy. Hence this strategy is updated each year as the Corporate Strategy is updated to reflect changed circumstances.

1.1.5 While SYPA is less exposed to the wider constraints on the public sector financial environment than our colleagues in the major employing organisations within the Pension Fund, we still have a responsibility to manage the resources for which we are responsible in such a way that our expenditure does not negatively impact on the overall performance of the Pension Fund. This strategy sets out how we aim to achieve this in as transparent a way as possible.

2. Setting the context for the medium term financial strategy

2.1 Public Sector Finance

2.1.1 The public sector financial environment is probably the most significant factor defining the context in which this strategy is developed. Key issues, like the level of pay awards, have an impact both on some aspects of the Fund's liabilities as well as upon elements of the Authority's cost base.

2.1.2 The main factors which normally affect the Authority and the Fund are concerned with local government finance. In general terms, growth in local government spending tends to lag growth in the generality of government spending, although pay tends to mirror the headline change in public sector pay.

2.1.3 The effects of the global COVID-19 pandemic, inflation and other demand pressures remain hugely significant issues for Local Government. The financial settlement includes funding for Councils for costs arising from this, as well as additional funding for social care. However, a substantial proportion of this additional funding is dependent on increases to council tax, and it remains the case that the overall context is that local government finances are under increasing pressure.

2.1.4 The national pay award for 2022/23 was agreed in November 2022 at a level of £1,925.00 added to each scale point. This increase is significantly larger than recent previous pay awards, and has lead to further pressure on Local Government Budgets. However, based on the information available it does not appear that this trend of higher pay awards is set to continue.

2.1.5 Despite the previous pay award being proportionally greater than prior increases, for the time being, our assessment of what this means for the Authority and the Fund is that it is likely that headline pay increases in the medium term will be at around, or quite possibly below, the level of 2%, and that major employers (and probably schools and colleges as well) will continue to need to identify significant year on year savings. This has wider effects on a number of areas, including the affordability of contribution rates, the balance of membership between active, deferred and pensioner members, and the number of early retirements on grounds of redundancy. These factors will influence the value of benefits in payment, the average lifetime in retirement and the value of lump sum “strain” payments into the Fund. All of these factors will need to be reflected in forecasts of income and expenditure and in the debate over contribution rates at each valuation.

2.2 The Pensions Sector

2.2.1 What is happening in the wider pensions sector impacts the Authority and the Fund in a less direct way, although no less significantly. For example, a significant change in the funding level of the remaining private sector defined benefit schemes could change the value of certain assets classes used to address the results of the change (e.g., a search for index linked gilts if funding levels increased). This could impact on the potential rate of growth in the value of the Fund or could make it harder to deploy capital into specific types of asset if other funds take up the supply of assets.

2.2.2 In addition, trends in the wider pensions sector tend, over time, to influence developments within LGPS and in the public sector pensions' space. These trends may arise from regulatory emphasis, such as the continuing focus on data quality, or from changes in technology such as the growing emphasis on various forms of e-communication, and methods of engaging with scheme members.

2.3 The Economic Environment

2.3.1 The wider economic environment impacts the Fund in terms of both its assets and its liabilities. Clearly the underlying economic environment impacts the performance of investments in the financial markets while key metrics such as inflation and interest rates feed into the actuarial calculations which determine the Fund's liabilities.

2.3.2 It remains incredibly difficult to forecast the movements in key economic indicators therefore it makes sense for this strategy to use assumptions based on key factors already reflected in the financial framework such as the assumed level of investment return included in the actuarial valuation. This is not a protection against any forecast being wrong – it almost certainly will be – but it means that the strategy is based on an underlying set of assumptions that have been subject to a more rigorous set of testing than it would be possible to achieve internally.

2.4 The Starting Point

2.4.1 The starting point has a significant impact on any strategy. In this case, the starting point is reflected in the current cost base for the Authority's operations and its fund management arrangements and the level of funding within the scheme which, based on the 2022 valuation results, reflects a significant improvement on the previous 2019 position.

2.4.2 In some senses the starting point is possibly more influential than other aspects of the context, for example achieving full funding, or close to full funding leads to an alteration to the strategic asset allocation moving funds out of equities into less volatile, preferably income generating assets. Unfortunately, these tend to be more expensive assets to manage thus a change in the cost base is almost inevitable. Whether the focus is on net of fees return or gross fees is irrelevant because both will ultimately have the same impact on the value of and performance of the Fund.

2.4.3 For the South Yorkshire Pension Fund, the starting point is, based on the 2022 valuation results, full funding. This impacted employers' deficit recovery contributions, which in many cases are now a surplus position. The current valuation position will inform the review of the Investment Strategy Statement, due to be produced in March 2023.

3. Financial objectives

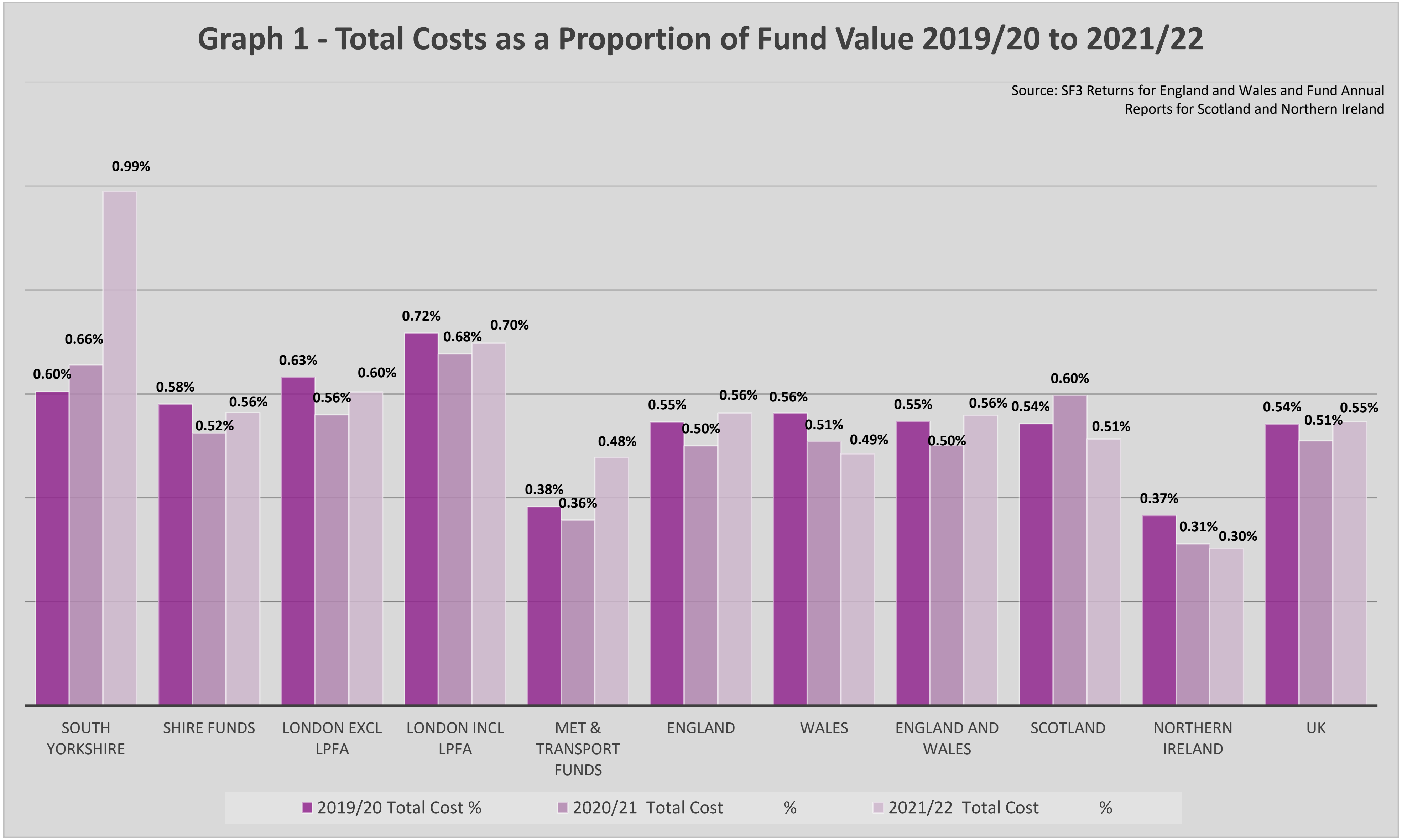
3.1 Financial Objectives

3.1.1 For any strategy it is important to understand what you are aiming to achieve. This is no less true of this MTFS, and this section sets out objectives in relation to the control of costs in the overall context of the Fund. In order to set these objectives, we need to understand how SYPA's costs compare to the rest of the LGPS funds.

3.2 Comparative Costs

3.2.1 The only real source of data to compare SYPA with other LGPS funds is the annual SF3 return completed by all English and Welsh funds and submitted to MHCLG. Similar data for the Scottish and Northern Irish funds can be added to this from fund annual reports to give a UK wide comparison. There are flaws with this data, particularly regarding the disclosure of non-invoiced investment costs, which are gradually, but very slowly, being worked out of the system. However, it is the only comprehensive data set available and does give a broad indication of how SYPA compares with other LGPS funds.

3.2.2 Chart 1 below shows how SYPA's total costs compare with those of both the totality of other LGPS funds and of particular types of fund, for the last three financial years from 2019/20 to 2021/22.


Graph 1 - Total Costs as a Proportion of Fund Value 2019/20 to 2021/22
Source: SF3 Returns for England and Wales and Fund Annual Reports for Scotland and Northern Ireland
0.60%
0.66%
0.99%
0.58%
0.52%
0.56%
0.63%
0.56%
0.60%
0.72%
0.68%
0.70%
0.38%
0.36%
0.48%
0.55%
0.50%
0.56%
0.56%
0.51%
0.49%
0.55%
0.50%
0.56%
0.54%
0.60%
0.51%
0.37%
0.31%
0.30%
0.54%
0.51%
0.55%
SOUTH YORKSHIRE
SHIRE FUNDS
LONDON EXCL LPFA
LONDON INCL LPFA
MET & TRANSPORT FUNDS
ENGLAND
WALES
ENGLAND AND WALES
SCOTLAND
NORTHERN IRELAND
UK
2019/20 Total Cost %
2020/21 Total Cost %
2021/22 Total Cost %

3.2.3 This appears to show that South Yorkshire's costs as a proportion of Fund value now represent the highest cost Fund in this comparison, and a significant increase compared to the previous year.

3.2.4 The primary driver for the significant increase in the SYPA costs for 2021/22, relates to investment costs, specifically performance fees on the alternative assets we invest in. Alternative assets have performed well during 2021/22, and the performance fees account for c50% of our investment management costs. Due to the fees being generally higher with alternative assets, the combination of this and strong performance account for the significant increase in the chart.

3.2.5 Adidtionally, it is important to consider the SYPA costs compared to other Funds in the context of the drive to greater cost transparency and improved reporting of investment management expenses that are not invoiced but deducted at source from Net Asset Value (NAV). Since 2018/19 SYPA, with the aid of Border to Coast, has made significant progress in this regard, that so far is outpacing the progress of other Funds. It should also be noted that unlike other LGPS funds, SYPA is not able to fully recover VAT resulting in a tax drag, which in 2021/22 amounted to £0.14m, and was c.£0.21m in the two years before that.

3.2.6 Whilst our progress on cost transparency appears to have started earlier and moved more quickly, it is evident that a similar impact is now starting to be seen within some of the other Funds' costs for 2020/21 to 2021/22; and it is anticipated this will continue, making these comparisons more useful going forward as they will be on a more 'like-for-like' basis.

3.2.7 The following table presents more detail of the investment costs and this demonstrates the impact since 2018/19 of the enhanced reporting of these external management costs that are deducted at source.

Investment Management Expenses - Breakdown	**2018/19** **£0**	**2019/20** **£0**	**2020/21** **£0**	**2021/22** **£0**	**Movement 2018/19 to 2021/22** **£0**
Pooling Costs - Invoiced	1,935	2,066	3,891	4,345	2,410
Internal Management Costs	672	596	539	583	-89
External Management Costs - Invoiced	5,335	3,529	2,528	2,824	-2,511
External Management Costs - Deducted at Source	40,254	37,790	52,431	92,383	52,129
Irrecoverable VAT Liability	516	497	211	144	-372
Total Investment Management Expenses	**48,712**	**44,478**	**59,600**	**100,279**	**51,567**
Fund Value at 31 March: £000	**8,439,965**	**8,170,401**	**9,862,073**	**10,673,562**	**1,691,672**
Investment Costs as Percentage of Fund Value %	**0.58%**	**0.54%**	**0.60%**	**0.94%**	

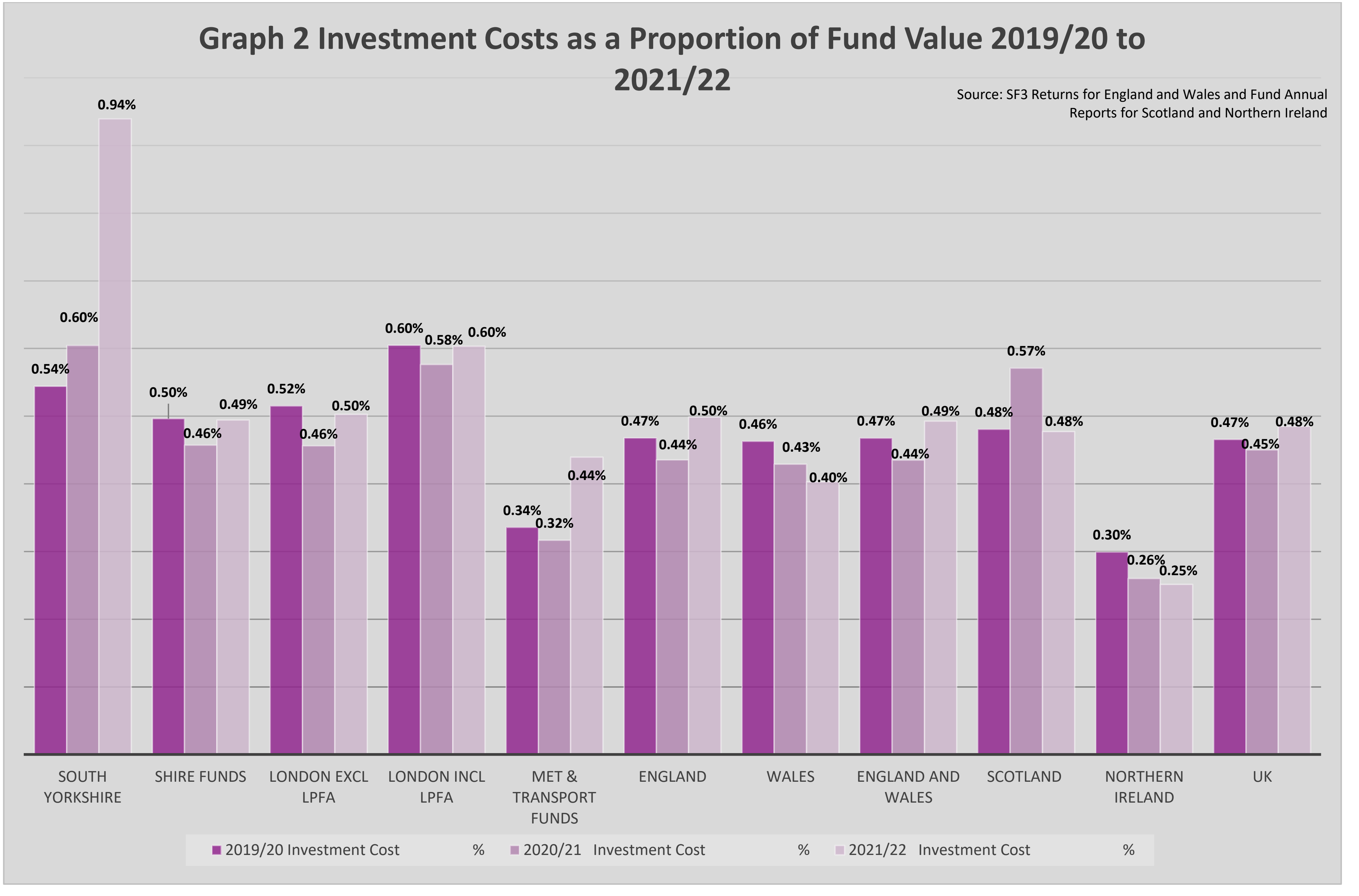
3.2.8 The Authority is confident that our performance in controlling actual costs overall remains strong; but there is no room for complacency, and we continue to closely monitor this area in light of the following factors that are driving cost increases:

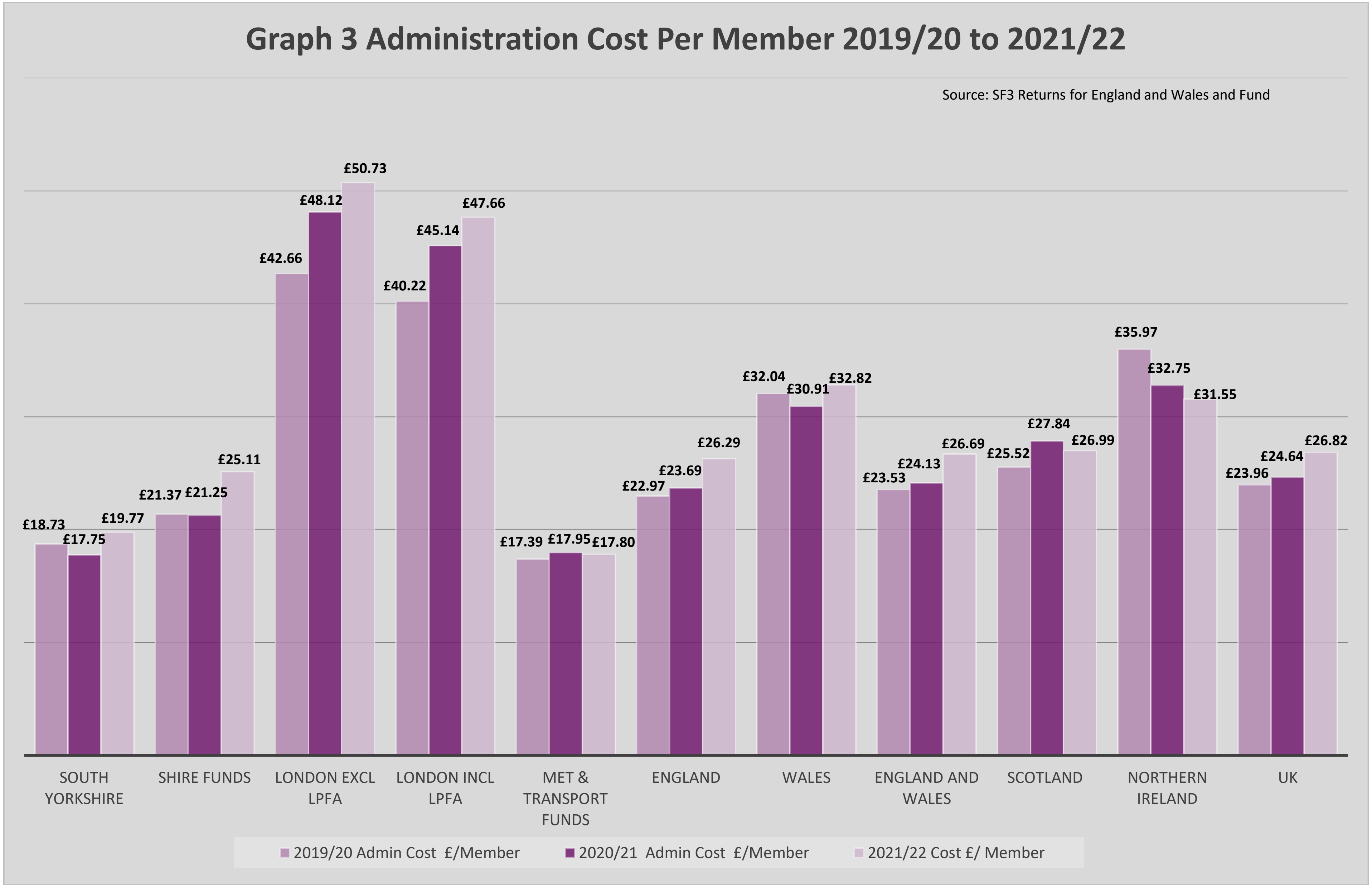
- The Fund's strategic asset allocation continues to move more of the portfolio into unlisted assets such as private equity and infrastructure which in general tend to be more expensive to manage. The impact of this investment strategy is evidenced in Chart 1 and referenced at 3.2.4.

- The Government's pooling initiative results in SYPA's listed assets in future being managed within pooled structures provided by Border to Coast which, while cheap in comparison to external managers, are more expensive than the previous, admittedly unsustainable, in-house arrangements.

3.2.9 There are specific factors which might be expected to give rise to SYPA having a higher-than-average cost base, in particular the fact that it is a stand-alone pension organisation bearing its own corporate overheads, rather than sharing them with a council. This has not been borne out by the data in recent years but will be kept under review as part of the budget process going forward, particularly as the Authority continues to invest in the development of the organisation and governance.

3.2.10 The total cost shown in Chart 1 can be analysed in more detail by looking at the following two charts which separate out SYPA's Investment and Administration costs and how these compare with the rest of the Local Government Pension Scheme across the UK.


Graph 2 Investment Costs as a Proportion of Fund Value 2019/20 to 2021/22
Source: SF3 Returns for England and Wales and Fund Annual Reports for Scotland and Northern Ireland
0.54% 0.60% 0.94%
0.50% 0.46% 0.49%
0.52% 0.46% 0.50%
0.60% 0.58% 0.60%
0.34% 0.32% 0.44%
0.47% 0.44% 0.50%
0.46% 0.43% 0.40%
0.47% 0.44% 0.49%
0.48% 0.57% 0.48%
0.30% 0.26% 0.25%
0.47% 0.45% 0.48%
SOUTH YORKSHIRE
SHIRE FUNDS
LONDON EXCL LPFA
LONDON INCL LPFA
MET & TRANSPORT FUNDS
ENGLAND
WALES
ENGLAND AND WALES
SCOTLAND
NORTHERN IRELAND
UK
2019/20 Investment Cost %
2020/21 Investment Cost %
2021/22 Investment Cost %


Graph 3 Administration Cost Per Member 2019/20 to 2021/22
Source: SF3 Returns for England and Wales and Fund
£18.73
£17.75
£19.77
£21.37
£21.25
£25.11
£42.66
£48.12
£50.73
£40.22
£45.14
£47.66
£17.39
£17.95
£17.80
£22.97
£23.69
£26.29
£32.04
£30.91
£32.82
£23.53
£24.13
£26.69
£25.52
£27.84
£26.99
£35.97
£32.75
£31.55
£23.96
£24.64
£26.82
SOUTH YORKSHIRE
SHIRE FUNDS
LONDON EXCL LPFA
LONDON INCL LPFA
MET & TRANSPORT FUNDS
ENGLAND
WALES
ENGLAND AND WALES
SCOTLAND
NORTHERN IRELAND
UK
2019/20 Admin Cost £/Member
2020/21 Admin Cost £/Member
2021/22 Cost £/ Member

3.2.10 It is evident from Chart 3 that Administration costs for the Authority remain at the lower end of the spectrum of costs.

3.2.11 When comparing the two charts it is clear that the main driver of the increased fund costs come from the investment costs, and in particular the performance costs, referenced at 3.2.4.

3.2.12 In regard to Administration, SYPA is benefitting from the economy of scale that comes from serving a large fund, while the much smaller London funds clearly see the diseconomies which arise from servicing much smaller funds.

3.2.13 In order to see the value for money picture we plan to participate in CEM and CIPFA benchmarking exercises through 2023/24, which should hopefully provide further insight into the Authority's services.

3.3 Financial Objectives

3.3.1 The Authority needs to set financial objectives which focus on the key streams of activity within its operations, administration and investment while bringing these together to focus on total cost. These objectives will mirror the financial constraint imposed on the district councils by the grant system, thus ensuring that SYPA is taking no more from the pension fund for its running costs than is necessary.

3.3.2 At the same time the Authority must be careful, as a small organisation, not to "shoot itself in the foot" by setting unachievable financial objectives which generate relatively large-scale savings targets, which could not be delivered without impacting the customer experience.

3.3.3 For Pensions Administration, the financial objective may be framed as follows:

"The annual increase in the budgeted cost per member for administration functions will be limited to an index made up of 70% local government pay and 30% September CPI."

3.3.4 This limits the rate of increase in costs while allowing the benefits of any increase in productivity to be re-invested in the quality of the service provided to members, which is broadly in line with the Authority's overall objectives. Such an approach also provides some buoyancy in the level of resources available in order to address the rising number of members and employers within the Fund. A similarly expressed objective could be placed on the Authority's overall operating budget, which would place a helpful constraint on corporate costs. These two objectives are illustrated in the table below.

Cash Limits for Operating Budget	2023/24 Baseline £ / Member	2024/25 Cash Limit[2] £ / Member	2025/26 Cash Limit[2] £ / Member
Administration Service[1]	£25.59	£26.72	£27.90
Authority Operational Budget[1]	£38.11	£39.79	£41.54

Notes

1. The cost per member is based on the relevant totals included within the Authority's operational budget as presented for approval at the Authority's February 2023 meeting. The equivalent figures for SF3 reporting purposes will be slightly higher because they additionally include non-recoverable VAT which is not part of the Authority's total operating budget.

2. The future years' cash limits are calculated by applying an inflationary increase of 4.4% which comprises 2.0% Local Government Pay Inflation and 10.1% CPI Inflation, weighted in accordance with the financial objective set out above.

3. Membership is assumed to increase at 1.5% per year in line with recent trends.

3.3.5 Given that, broadly, investment costs have a relationship to the value of invested assets, it would be sensible to have an objective which recognises this, but also recognises the fact that the Authority's investment strategy is to move out of listed into unlisted and more expensive assets, and also that the Authority's overall objective is to achieve the best possible net of fees risk-adjusted returns meeting the actuarial return objective (currently c. 4.45%pa). This means that any financial objective around investment costs should not place an artificial constraint which prevents the Authority from making the right investment decisions.

3.3.6 Given the information set out above, framing an objective in relation to investment costs is quite difficult. However, something along the following lines could be appropriate:

"In any financial year, the Authority will seek to limit investment management expenses to a level less than the median in the CEM benchmarking comparator group."

3.3.7 Given the limitations to an LGPS comparator set out above this metric provides a more realistic target which is based on a much wider international peer group and reflects full cost transparency for all participants, thus there will be a like for like comparison. Using the CEM measure also means that the Authority will have access to data which will allow it to understand how and why its costs differ from others within the peer group.

3.3.8 The targets set out in these financial objectives will be reviewed each year in the context of their impact on the Authority's overall financial position and their impact on the ability of the Authority to deliver its corporate objectives, while still driving improvements in efficiency. In addition to these objectives which can easily be measured in budget setting and which in effect place cash limits on the Authority's budget, a number of financial performance measures related to comparative costs will be part of the suite of Corporate Strategy measures.

4. Financial forecasts

4.1 Forecast Assumptions

4.1.1 Any financial forecast is based on a series of assumptions. The key assumptions are set out below:

- **Pay –** Pay awards have been assumed to average 2% over the period, which is in line with the average of headline increases from the most recent local government pay awards.
- **Prices -** CPI inflation will be 10.1% for 2023 per the September 2022 CPI rate. With the current CPI volatility, the future rates for the remainder of the medium term have been based on estimates specific to the area being projected.
- **Contribution Income and Benefits Payments–** The forecast is produced by the actuary for both income and expenditure, based on the latest valuation results.
- Investment returns are assumed to be in line with actuarial assumptions.
- External investment management costs have been separately analysed in order to produce the forecast based on experience to date, plus known changes and estimated changes as a result of continued transition to Pooling.

4.1.2 Based on current knowledge, these assumptions are reasonable. We will continue to develop and refine our forecasting techniques over the period to provide a robust basis for resource planning.

4.2 Operational Budget Forecast

4.2.1 The forecast for the operational budget is summarised in the table below:

Operating Budget	2022/23 Forecast Outturn	2023/24 Budget	2024/25 Estimate	2025/26 Estimate
	£	£	£	£
Employees	3,858,846	4,741,827	4,975,550	5,075,060
Running Costs	1,863,503	2,150,003	2,245,760	2,317,165
Subtotal: Gross Expenditure	**5,722,349**	**6,891,830**	**7,221,310**	**7,392,225**
Income	(135,929)	(156,260)	(162,510)	(165,755)
Subtotal: Net Expenditure	**5,586,420**	**6,735,570**	**7,058,800**	**7,226,470**
Capital Expenditure	64,720	72,000	0	0
Contribution to / (from) Reserves	178,860	(150,000)	(80,000)	70,000
Total Charge to Pension Fund	**5,830,000**	**6,657,570**	**6,978,800**	**7,296,470**
Membership	172,952	174,680	176,430	178,190
Cost Per Member	**£33.71**	**£38.11**	**£39.56**	**£40.95**

4.2.2 The budget setting and medium-term financial strategy (MTFS) preparation for 2023/24 to 2025/26 has taken place in the context of a number of drivers for growth in cost that are explained in further detail in the Budget report presented alongside this Strategy.

4.2.3 The budget for the 2023/24 year ahead reflects continued emphasis on equipping the organisation for meeting the challenges expected in the next three years as detailed in the Corporate Strategy elsewhere on the agenda. Additional resources are included for twelve new posts to be established to support various specific areas of the planned work, as previously approved by the Staffing, Appointment and Appeals Committee in October 2022. These additional resources should ensure the organisation is well equipped, resilient and with a sustainable base for this medium term period.

4.2.4 The estimates for the remainder of the Medium Term set out above are based on projecting the 2023/24 budget forward, removing the one-off items from that year, and adding inflationary increases as necessary.

4.2.5 The key risks and uncertainties in relation to this forecast are as follows:

- Pay settlements and inflation running at a higher level than assumed in the forecast. This is clearly a risk, although the current wider local government and public sector finance context has been heavily impacted by the global pandemic and a range of pressures including social care demand, and the UK's exit from the EU. The 2022/23 pay settlement was agreed at a higher level than estimated, however based on the information available we expect this to return to 2% in 2023/24. An additional measure taken to mitigate against risks arising from the uncertainty and volatility in regards to pay and wider costs inflation is that in 2022/23 we are proposing to create a Pay and Benefits reserve equivalent to c4% of the pay budget, and we will also retain a small corporate contingency budget. This is in addition to the usual process of budgetary control whereby in the event of higher costs than forecast, managers will seek to absorb the in-year impact through the management of vacancies and seeking to either defer one off expenditure or avoid aspects of running cost expenditure. It is considered that these measures will be adequate to address the risk of cost increases.

- Deterioration in budgetary control. Budgetary controls and processes were strengthened during the 2019/20 - 2020/21 period and are now well embedded. The implementation of the new finance system that took place in 2022 will allow us to increase our levels of budgetary control with more detailed and comprehensive reports, to be developed during the coming financial year. There is therefore no indication of any likelihood of deterioration. The controls in this regard are also subject to internal audit review on a regular basis, which provides assurance on both their adequacy and their application.
- Loss of external income. This is mitigated through prudent budgeting, for example not including any assumptions around additional software sales which tend to be sporadic, and through securing longer term agreements with customers with staggered end dates so that not all agreements come to an end at the same time.

4.2.6 The operational budget is relatively low risk and is relatively simple in comparison to the Fund Forecast, being many times smaller and much less volatile. Consequently, while it understandably receives specific scrutiny as a cost that, in effect, has to be borne by participants in the Fund, variations are unlikely to have a material impact on the overall standing of the Fund.

4.3 Pension Fund Forecast

4.3.1 The table below presents a summary of the forecast for the Pension Fund for the current and coming three years.

South Yorkshire Pension Fund Financial Forecast	Actual 2021/22 £m	Forecast 2022/23 £m	Forecast 2023/24 £m	Forecast 2024/25 £m	Forecast 2025/26 £m
Dealings with members, employers and others directly involved in the scheme:					
Contributions receivable & transfers in from other pension funds	-211	-215	-256	-266	-277
Benefits payable and payments to or on account of leavers	338	361	358	345	355
Net (additions) / withdrawals from dealings with members	**127**	**146**	**102**	**79**	**78**
Management expenses	106	81	87	90	93
Net returns on investments	-1,045	-643	-682	-685	-709
Net (increase)/decrease in the Fund during the year	**-812**	**374**	**-493**	**-516**	**-538**
Net Assets of the Fund at 1 April	-9,862	-10,674	-10,300	-10,793	-11,309
Net Assets of the Fund at 31-Mar	**-10,674**	**-10,300**	**-10,793**	**-11,309**	**-11,847**
Management Expenses as Percentage of Average Net Assets	0.99%	0.79%	0.81%	0.80%	0.79%

4.3.2 In the first year of the forecast, investment costs (including those within the operational budget) are at 79 bps and are expected to remain at 79 bps by 2025/26. The forecast costs have reduced from the 2021/22 actual costs, due to the higher performance fees discussed earlier, which are forecast to stabilise at a lower level. It should also be borne in mind that this forecast is produced on a fully transparent basis and therefore comparisons with other funds will not necessarily be valid. These forecasts will be reviewed against benchmark data when available.

4.3.3 The forecast for the Pension Fund is much more susceptible to forecast error than that for the operational budget. In particular, while there is some consistency in terms of data from previous years the Authority cannot control the numbers of members retiring in any year or the decisions which they make in relation to commutation of pension to lump sum. Similarly, the numbers of deaths amongst the membership of the Fund and the numbers of members transferring either into or out of the Fund are changeable and outside the control of the Authority. While the forecasts are based on the best information available using the actuarial results and historic information, as adjusted for known one off events, and inflation where appropriate, there is a significant amount of variability from year to year which it is extremely difficult to forecast.

4.3.4 The forecast Fund value at the end of the current year reflects the challenging external investment environment we have experienced through 2022/23. These factors include, but are not limited to, the volatile inflationary environment, the war in Ukraine and the ongoing impacts of COVID.

4.3.5 The important message in the above forecast is the anticipated net withdrawal from the Fund in each year for dealings with members, this results in a significant increase in the requirement for the harvesting of investment income. This trend will be an ongoing challenge for the fund now that we have matured, and it is not anticipated that this scenario will reverse.

4.3.6 The key risks and uncertainties in the Fund Forecast include the following:

- Financial market volatility, which will impact on both the asset value of the Fund and on the level of investment income and large swings in asset value will result in significant variation from the forecast. This is a constant risk for pension funds. Steps have been taken, through the broad asset allocation, to reduce the potential volatility in the Fund but the risk of events which might cause significant market dislocation remains and, if anything, is at the current time heightened as a result of continuing tensions around international trade, the economic impact of the COVID-19 pandemic and the war in Ukraine.
- A further significant wave of service reductions across major employers resulting in workforce reductions, which have the effect of reducing the number of active members contributing and further increase the imbalance between contributions received and benefits paid. Other than changes in the Strategic Asset Allocation to focus on income generation and delivering investment returns above actuarial assumptions to build resilience into the Fund, there are limited options available to the Fund in this area.
- Failure of pooling to contain investment costs. While SYPA is not expecting to make any significant savings as a result of pooling, in the short to medium term the expectation is that the process of pooling will contain costs. However, should the Pool fail to achieve its objectives in this area there will be an impact on net of fees returns. To date, the evidence is that in this respect Border to Coast are delivering in line with their plan and, should the initial moves of partner funds into the range of internally managed funds continue or increase, there may well be the opportunity for costs in relation to listed assets to reduce towards the pre-pooling levels, although they are very unlikely to reach those artificially low levels. If the Pool were to fail to deliver cost savings as anticipated, then further mitigation will come through the collective action of the 11 partner funds to address any underperformance.

4.3.7 This forward forecast indicates a challenging position when viewed in the context of market conditions and uncertainty as at the time of writing. All economic forecasts indicate that we are moving away from the high inflationary environment, combined with lower returns for a protracted period, which is reflected in the actuarial assumptions used in producing the forecast. This results in the need for the Fund and the Pool to focus on securing good assets and sustained income streams within its revised strategic asset allocation.

5. Policy on reserves

5.1 Reserves

5.1.1 Reserves are funds that are set aside for two main reasons:

- A ‘just in case’ risk materialises that requires additional resources; or
- To save up for a particular project.

5.1.2 All of SYPA’s costs are met by the Pension Fund therefore, unlike a local authority, the first contingency argument for holding reserves does not hold as costs incurred, for example, as a result of a building fire, would simply fall to the Pension Fund which is about 1,500 times the size of the Authority’s budget and such costs are therefore unlikely to be material.

5.1.3 The argument for holding reserves to save up for things does, though hold. In order to save up in this way, managers will have had to underspend their budgets and thus the ability to use money thus saved acts as an incentive to manage within the available resources.

5.1.4 However, there is a balance to be struck as reserves could be allowed to accumulate to a level where they became significant in the context of the Authority’s budget at which point, they would in effect be depriving the Fund of cash to invest. Consequently, some limitation on the level of reserves is necessary to maintain this balance. For the previous iterations of this strategy, a limit of 7.5% of the operating budget has been applied. However the current external environment is extremely volatile, and as such it is considered that an increase to this limit would be appropriate in order to provide a suitable degree of flexibility for maintaining reserves at a level that will enable us to manage risk as needed. It is therefore proposed to increase the limit to 10% of the operating budget. This results in the following policy on reserves:

“The Authority will maintain its operational revenue reserves at a level equivalent to no more than 10% of its operational budget, the establishment of new reserves will be approved by the Authority on the recommendation of the Treasurer, and the level of reserves will be reviewed by the Treasurer each year as part of their report on the final accounts of the Authority.”

5.1.5 During the 2021/22 financial year, the reserves were put towards financing major capital projects that needed to be resourced. These projects included the Oakwell House long-term office accommodation project, replacement of business systems and the implementation of a new contract for pensions administration software. The forecast outturn for 2022/23 sees the Authority returning to a budget underspend position. The primary reason for the 2022/23 underspend would be due to challenges filling vacancies, leading to staffing underspend.

5.1.6 The 2022/23 projected underspend includes an amount that was included in the budget for the outcomes of the pay and benefits review. Whilst the review has been carried out and reported upon, the work to plan actions to address the findings and to cost these, has slipped, resulting in a need to carry forward the budget amount set aside for this. It is therefore proposed that we create a “Pay and Benefits Reserve” in 202/23 for this purpose – which will be used in 2023/24. Adding this new reserve, in addition to the other 2022/23 forecast reserve movements, will take the total revenue reserves to 9.4% of the 2022/23 operational budget.

5.1.7 At the current time the new reserve is anticipated to be used for particular outcomes of the review, however due to the challenging recruitment and retention environment, the reserve will be reviewed periodically to allow the Authority some flexibility.

5.1.8 The forecast level of reserves for the medium term are as shown in the following table.

South Yorkshire Pensions Authority Earmarked Reserves	Forecast Balance at 31 March 2023 £	Forecast Balance at 31 March 2024 £	Forecast Balance at 31 March 2025 £	Forecast Balance at 31 March 2026 £
Operational Revenue Reserves:				
Corporate Strategy Reserve	147,270	107,270	72,770	122,770
ICT Reserve	201,160	126,160	95,660	115,660
Pay and Benefits Reserve[1]	200,000	200,000	200,000	200,000
Subtotal - Revenue Reserves	**548,430**	**433,430**	**368,430**	**438,430**
Revenue Reserves as % of Budget	*9.4%*	*6.5%*	*5.3%*	*6.1%*
Capital Projects Reserve	119,330	84,330	69,330	69,330
Total Reserves	**667,760**	**517,760**	**437,760**	**507,760**

Notes

1. The 'Pay and Benefits' reserve is planned to be used in 2023/24 to contribute to costs required for implementation of any changes arising from the pay and benefits review undertaken in 2022/23. At this stage, it is not possible to provide a reasonable estimate for this, which is why no movements on this reserve can be shown here at this time.

5.1.9 The above table illustrates that the current plans and forecasts involve drawing down from the revenue reserves in 2023/24, followed by a further drawdown in 2024/25 and a net contribution into the reserves in 2025/26. The earmarked reserves will continue to be kept under review and transfers to and from each reserve will be reported to the Authority for approval based on a recommendation from the Treasurer as required, through the quarterly reporting of management accounts and financial forecasts.