

Report title	Quarterly Investment Report to 31 December 2020 and Investment Strategy Statement 2021	
Originating service	Pension Services	
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Recommendation for decision:

The Pensions Committee is recommended to:

1. Approve the completion of the annual review of the WMPF's Investment Strategy Statement (ISS), with only very minor changes proposed.

Recommendations for noting:

The Pensions Committee is asked to note:

1. The global market and investment update paper prepared by the Fund's Investment Consultant, Redington.
2. Asset Allocation and Performance Reporting for the West Midlands Pension Fund (WMPF), Main Fund and Admitted Body Sub Funds.

1.0 Purpose

- 1.1 The investment report covers developments in investment markets, asset allocation and investment performance over the latest quarter in relation to the West Midlands Pension Fund (Main Fund and Admitted Body Sub Funds). Supporting responsible investment activities are covered in a separate paper.

2.0 Background

- 2.1 This paper aims to bring together routine investment matters relevant to the management and implementation of the Fund's investment strategy and related policies:
- I. The economic and market background environment in which the Fund operates and the outlook for different asset classes.
 - II. WMPF's investment strategy is outlined in the Investment Strategy Statement (ISS) and set in conjunction with the Funding Strategy Statement (FSS) to target a return over the long term to deliver the asset values required to meet benefit payments due to members. The Strategic Investment Allocation Benchmark (SIAB) forms part of the ISS and includes the target asset allocation and the levels of returns investment policies will be benchmarked against.
 - III. This report provides separate commentary on the Main Fund and Admitted Body Sub Funds (ABSF), established for former employers of the West Midlands Integrated Transport Authority Pension Fund, West Midlands Transport Limited (WMTL) and Preston Bus (PB).
 - IV. This report refers to Fund positioning against 2019 ISS and SIAB policy targets. These were refreshed as part of the 2020 ISS review as approved by the Pensions Committee in March 2020. Implementation of the 2020 ISS updates is underway and will see the Fund transition to new strategic policy targets, designed to better meet the future needs of the WMPF.
 - V. An interim review of the ISS has been completed and only very minor changes are proposed. The investment strategy formulated as part of the 2020 update remains appropriate to deliver against long term objectives.

3.0 Executive Summary

- 3.1 As at 31 December 2020, the West Midlands Pension Fund's market value was £18.4 billion (incl. WMTL and PB ABSF). Investment markets generally rose in the quarter continuing the recovery from lows seen earlier in the year.
- 3.2 The Main Fund increased by 6.0% over the quarter trailing the return of its benchmark. The Fund's growth assets (largely equities) delivered strong positive returns in the quarter. Income and stabilising assets performed less well with Infrastructure the largest

detractor. The Fund's returns are below that of its benchmark for 1, 3 and 5 years but are marginally ahead over 10 years.

- 3.3 The Admitted Body Sub Funds outperformed in the 3 months to 31 December but remain marginally behind over 1 year and longer time periods. For WMTL, positive relative performance for the quarter was driven by a rebound in Multi-Asset Credit and Diversified Growth Funds. For both ABSF Multi-Asset Credit contributed positively to deliver excess return over the quarter but was a drag for 1 year relative performance.

4.0 Markets and Investment Background

- 4.1 The Fund's Investment Consultant, Redington provides a quarterly update on the market background and market performance over the quarter. The report for the quarter to 31 December 2020, which further sets out the outlook for the Fund's key asset classes over the coming months, can be found in Appendix A.

- 4.2 Returns for the major asset classes for the period are shown below:

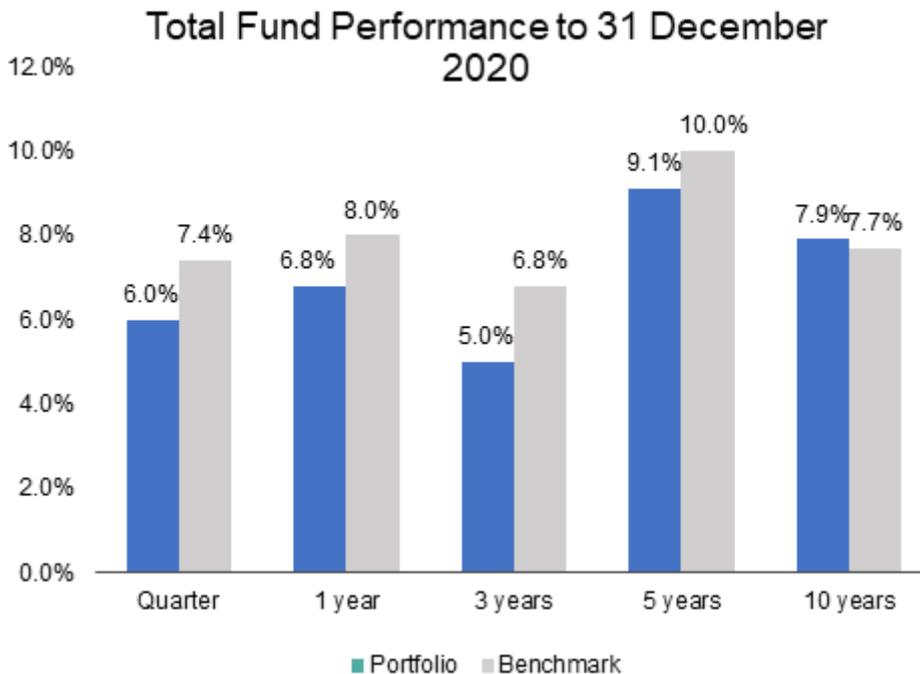
Asset Class Returns (£)	3 months (%)	12 months (%)
FTSE All World ex UK	8.4	14.3
UK Equity (FTSE All Share)	12.6	-9.8
Europe (ex UK) Equity	9.2	8.6
North America Equity (S&P 500)	6.1	14.7
Emerging Market Equity	13.2	14.7
UK Gilts (All Maturities)	0.6	8.3
Index Linked Gilts	1.2	11.0
Corporate Bonds	3.1	7.8

- 4.3 The last quarter of 2020 saw strong returns from all primary asset classes except for government bonds. Equity performance again varied by region with particularly strong performance seen from areas of the market which had lagged in the earlier quarters of the year. Uncertainty remains in commercial UK property markets with low transaction levels and ongoing rent deferrals.

5.0 West Midlands Pension Fund

Main Fund Performance Summary

- 5.1 The Main Fund delivered a return of 6.0% over the quarter against a benchmark return of 7.4%. The Fund's relative return remains negative over 1, 3 and 5 years.



- 5.2 Underperformance over the quarter was driven by an overweight allocation to the lower returning stabilising assets (including cash) and underperformance from the Private Equity portfolio (versus a strong performance from its listed equity benchmark).
- 5.3 Over 1 year, these same assets detracted from relative performance. The Infrastructure and Real Assets portfolio (benchmarked against an 'inflation plus' target return level) also underperformed over this period. Over 3 years the main detractors remain Private Equity, Infrastructure and Insurance Linked Securities.
- 5.4 The asset allocation of the Main Fund as at the quarter end, compared to strategic targets is set out overleaf. Note that this table and accompanying commentary refers to previous policy targets. The revised Strategic Investment Allocation Benchmark within the 2020 Investment Strategy Statement will be adopted as new strategies are implemented and meaningful allocation changes are made. New target weights are shown for reference.
- 5.5 The Fund remained overweight in stabilising assets versus previous policy targets, as a result of the higher than normal levels of cash held and an overweight position in corporate bonds reflecting the revised target weighting (note corporate bonds have been reclassified as an 'income' asset, as reflected overleaf).

- 5.6 The Fund's attention is focused on implementing the Strategic Asset Allocation (SAA) changes as agreed as part of the 2020 Investment Strategy review. Efforts are focused on fixed income assets, with steps being taken to move towards new target weights in multi-asset credit and illiquid credit in particular and cash holdings expected to be deployed over the coming quarters.

Asset class	Value (£m)	Fund allocation %	Current Benchmark %	Difference %	Change from previous quarter %
Growth					
Quoted equities	9,592	52.9	48.0	4.9	0.9
Private equity	1,217	6.7	10.0	-3.3	-1.6
Special opportunities	354	2.0	5.0	-3.0	-0.2
Total growth assets	11,163	61.5	63.0	-1.5	-0.9
Stabilising					
UK gilts	459	2.5	2.0	0.5	-0.3
Index linked gilts	1,233	6.8	5.0	1.8	-0.2
Cash & Cash Equivalents	932	5.1	2.0	3.1	2.7
Corporate bonds	700	3.9	2.0	1.9	-0.2
Cashflow matching fixed interest	318	1.8	3.0	-1.2	-0.1
Total stabilising assets	3,642	20.1	14.0	6.1	1.9
Income assets					
Specialist fixed interest	451	2.5	3.5	-1.0	-0.2
Emerging market debt	793	4.4	3.5	0.9	0.0
Property	1,318	7.3	10.0	-2.7	-1.4
Real assets and infrastructure	752	4.1	6.0	-1.9	-0.8
Total income assets	3,314	18.3	23.0	-4.7	-2.4
TOTAL	18,121	100.0	100.0	-	-

6.0 West Midlands Pension Fund

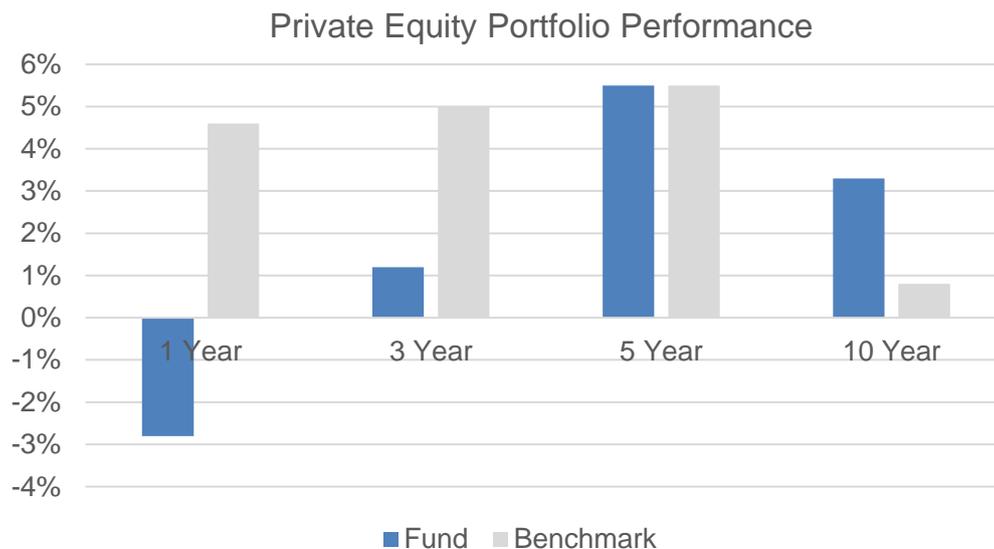
Detailed Performance Commentary

Growth Assets

- 6.1 The total Combined Equity Fund delivered strong absolute performance during the last three months of 2020 but underperformed the benchmark level of return. This can be attributable to holdings such as the LGPSC Climate Multi-Factor fund underperforming the broad equity market as other areas of the stock market performed very strongly (largely those which had underperformed during the rest of the year).
- 6.2 The Main Fund's passive equity assets are now almost exclusively managed by the investment pool company, LGPS Central Ltd with a large proportion of these assets held in an LGPS Central Ltd ACS Global Equity passive fund. All passive funds performed broadly in line with the respective benchmarks during the quarter but with significant divergence between region and strategy as shown below.

	Q4 2020	Full Year 2020
LGPSC UK (FTSE All Share)	12.6%	-9.8%
LGPSC Global ex UK	9.9%	12.6%
LGPSC Dividend Growth (Blended)	4.7%	1.4%
FTSE Climate Multi-Factor	5.3%	11.6%

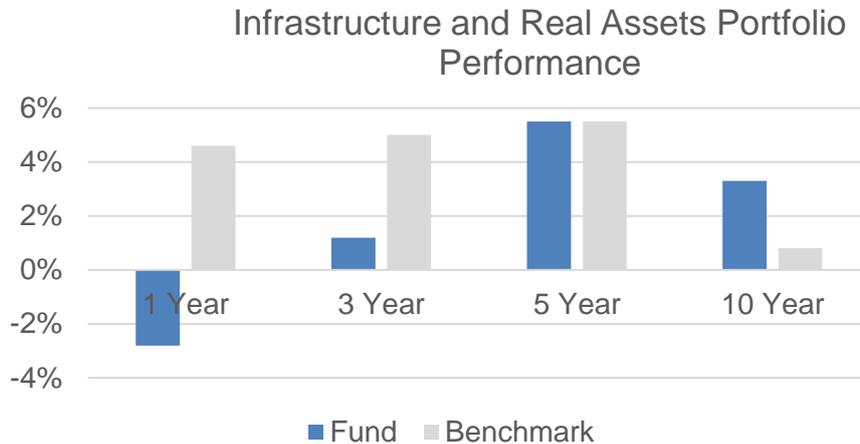
- 6.3 Over the quarter, the Fund's actively managed global equities comprised the LGPS Central Ltd (LGPSC) Active Equity fund, an allocation to sustainable equity managers and a basket of global equity futures.
- 6.4 For the quarter, the LGPSC Global Active Equity Fund returned 10.9% outperforming by 2.4%. The fund also ended the full year ahead of the benchmark. The LGPSC Global Active Equity Fund is a blended multi-manager portfolio consisting of three portfolios.
- 6.5 Emerging Markets delivered strong returns in Q4 and the Fund's portfolio outperformed its benchmark. All three managers outperformed during the quarter but were behind over 1 year. A review of these managers is being undertaken prior to effecting the increase in allocation set within the 2020 ISS.
- 6.6 The Private Equity portfolio significantly underperformed during the 3-month period ending 31 December 2020. The benchmark used for this asset class comprises listed equities plus an outperformance target. As such, during volatile periods (such as last year) the relative performance should be interpreted with caution. Over longer time periods the portfolio has met expectations and achieved benchmark level returns.



Income Assets

- 6.7 The Income pool outperformed its respective benchmark over the quarter. The aggregate property portfolio had a very strong period and continues to outperform on a longer-term basis. The Direct portfolio performed particularly well (significantly ahead of IPD/MSCI indices) due to resilient performance from sectors such as industrial, supermarket and offices. As previously highlighted, valuation uncertainty persists, and future rental levels remain unclear. The Indirect portfolio declined by 1.30% over 2020 and lagged both the Direct portfolio and its return target.

6.8 The infrastructure portfolio had a positive quarter but delivered a negative return over the course of the year. The portfolio has significantly underperformed its target return (CPI +4%) over 3 years but has done better on a longer-term basis. The Fund's UK assets have struggled during the pandemic, and the US portfolio has also fared poorly.



6.9 The major elements of the fixed income portfolio performed relatively well in the final quarter of the year as credit markets continued to rally. The Emerging Market Debt (EMD) allocation performed strongly and in particular, the dedicated hard currency (referring to USD or Euro denominated debt) EMD fund. The Multi-Asset Credit allocation outperformed in Q4 benefitting from its short interest rate duration positioning but underperformed its benchmark by 1.6% for the full year 2020. The Fund's sterling credit allocations also outperformed.

Fixed Income Relative Performance

	Quarter	1 year	3 years
Emerging Market Debt	2.3%	4.8%	0.5%
Corporate Bonds	1.1%	3.0%	1.6%
Multi Asset Credit	0.4%	-1.6%	N/A
LGPS Central Corporate Bond Fund	0.5%	N/A	N/A

Stabilising Assets

6.10 Stabilising Fixed Income: The stabilising portfolio comprises the Fund's exposure to government bonds and index linked securities, high-grade corporate bonds and cash. The stabilising component of the fixed interest portfolio delivered marginally positive returns.

6.11 Over the 1 and 3 year timeframes the stabilising portfolio has outperformed its benchmark.

Currency

6.12 The Fund changed its hedge ratios from 50% EUR and 25% USD to 25% EUR effective 16 September 2020. The hedge has had a positive impact on performance over the course of 2020. It has however, had a larger impact on the performance of the benchmark (which reflect higher hedge ratio) so has damaged relative returns (i.e. versus benchmark).

7.0 Admitted Body Sub Funds (ABSFs)

7.1 The current allocation for the two ABSFs is shown below.

WMTL asset allocation (excluding buy-in policy):

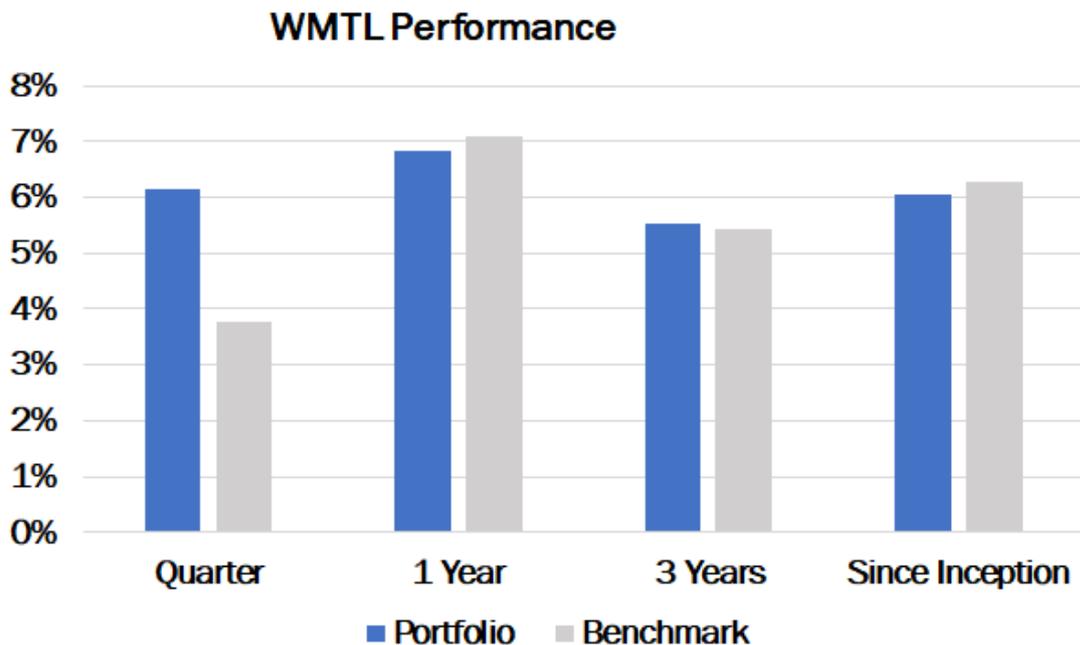
Asset Class	Value (£)	Fund allocation %
Equities	83,021,148	29.8%
Diversified Growth Funds (DGF's)	106,808,407	38.3%
Total Growth	189,829,555	68.1%
Fixed interest	38,354,588	13.8%
Multi Asset Credit	50,006,623	17.9%
LDI	0	0.0%
Cash	417,599	0.1%
Total Defensive	88,778,810	31.9%
TOTAL	278,608,365	

WMPB asset allocation:

Asset Class	Value (£)	Fund allocation %
Equities	3,319,294	16.7%
Total Growth	3,319,294	16.7%
Fixed interest	11,081,495	55.6%
Multi Asset Credit	5,473,397	27.5%
LDI	0	0.0%
Cash	43,396	0.2%
Total Defensive	16,598,288	83.3%
TOTAL	19,917,582	100.0%

WMTL performance

7.2 Outperformance in the quarter has not been enough to recover 1 year performance but the Fund is now marginally ahead of its benchmark for 3 years. Relative performance driven by the Multi-Asset Credit holding which underperformed its 'base rate plus' performance target.



7.3 WMTL 1 year performance summary by asset class is shown below with both Equities and the DGFs outperforming:

	Portfolio Return	Benchmark Return
Equities	11.0%	10.5%
Diversified Growth Funds	4.9%	4.0%
Bonds	5.4%	6.8%

Fixed Income

7.4 Alongside the Multi-Asset Credit holding in the bond portfolio, there are passive Index Linked Gilts and actively managed Corporate Bonds. The Corporate Bond mandate is performing well, ahead of benchmark over the 1-year period.

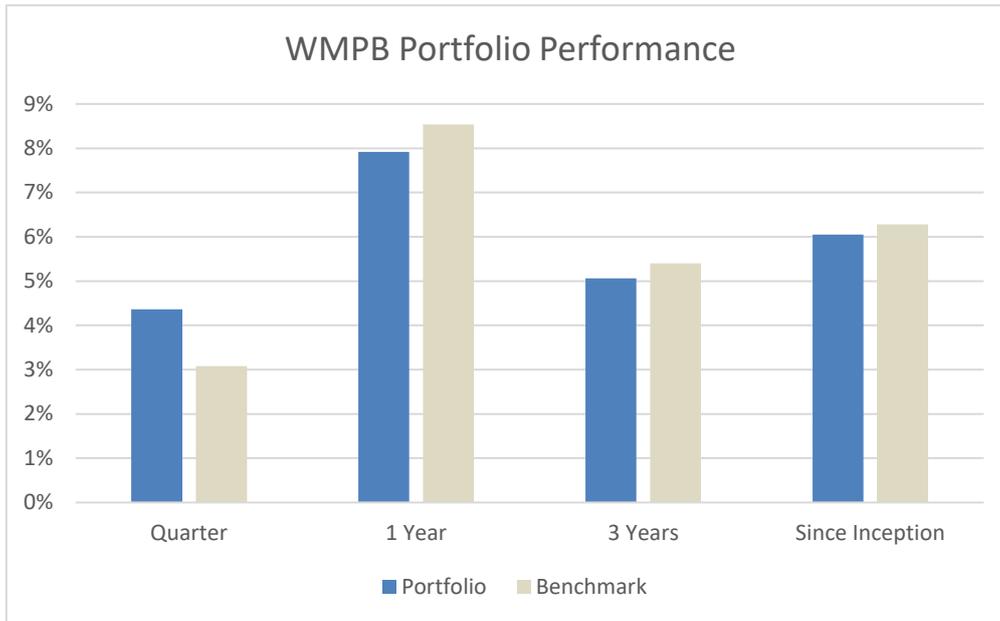
7.5 Multi-Asset Credit was introduced in Q3 2018. The fund continued its recovery in Q4 and ended the year with a positive return of 1.99% (but behind its benchmark). As mentioned, underperformance from this strategy has been a detractor for 1 year total relative returns, in part driven by benchmarking performance for this asset against target returns (LIBOR+4.5%).

Diversified Growth Funds

7.6 Both Diversified Growth Fund holdings delivered positive absolute and relative performance for the quarter and 1 year performance is now ahead of target. In both cases, equities were the largest contributor to quarterly gains. More defensive holdings held back performance for both funds.

WM PB Performance Summary

7.7 WMPB performance is summarised below. Outperformance in the quarter has not been enough to recover 1 year or 3 year performance. Relative performance for PB is almost entirely driven by the Multi-Asset Credit allocation, for the same reasons as those described above (for WMTL).



7.8 WMPB 1 year performance Summary by Asset Class is show below.

	Portfolio Return	Benchmark Return
Equities	10.5%	10.7%
Bonds	7.4%	8.0%

7.9 WMPB’s holding in Passive Equities, Index-Linked Gilts, Multi-Asset Credit and Corporate Bonds are the same as those held by WMTL, with performance outlined above.

8.0 Investment Pooling Update – LGPS Central Ltd

8.1 The Fund continues to work closely with its investment pool company LGPS Central Ltd (LGPSC) and Partner Funds to look for opportunities to transition assets where it can see value add from doing so including the opportunity to make cost savings. In Q4 2020 assets were transitioned to the LGPSC Emerging Market Debt fund (at its launch).

8.2 Work has taken place alongside input from the Fund and other Partner Funds to establish a Multi-Asset Credit (MAC) sub-fund for which managers have been selected. The fund is expected early in the second quarter of this year. In addition, the Fund has been working with a number of Partner Funds and LGPSC to develop a Private Debt offering.

9.0 Investment Strategy Statement (annual review)

- 9.1 In defining the implementation of the Fund's investment strategy, the ISS sets out the Strategic Investment Allocation benchmark (SIAB) including the permitted ranges for each asset type.
- 9.2 A full in-depth review of the Fund's ISS is completed every 3 years in conjunction with the triannual funding and valuation process. In addition, interim annual reviews are also completed to complement this cycle.
- 9.3 The Fund completed a full review of its investment strategy over 2019/2020 resulting in significant changes to the Funds SIAB being approved in March 2020. Implementation of these strategy changes is underway as communicated separately to this Committee.
- 9.4 The interim review referenced here confirms these strategy changes remain appropriate for the Fund to meet its longer-term objectives. The Fund's Investment Consultant, Redington, who advised the Fund during the 2019/2020 review have provided the following confirmation statement:

"In our view, the broad strategy changes remain appropriate from the detailed review that we conducted in 2020. We will continue to undertake analysis within each asset class category as we move through implementing the agreed changes, which will inform the specific implementation routes that are most appropriate for the Fund within each asset class".

- 9.5 Whilst the longer-term strategy remains the focus and is unchanged, Fund Officers are alive to the significant changes to the investment and economic landscape that occurred in 2020 and the potential impact of these on the outlook for Fund investment. These will be considered as we move through strategy implementation.
- 9.6 The only proposed change to an investment allocation/strategy is within the Liability Driven Investments being implemented for WMTL. Here it is proposed to reduce the stated target hedge ratio for interest rate movements to 60% (from 70%) to better reflect the hedging that is possible within the risk management controls (leverage levels) in place for this strategy.
- 9.7 Additionally, some minor, largely presentational changes are proposed to the ISS document. These changes are intended to improve clarity of message rather than altering the stated beliefs, Fund objectives or overarching investment strategy. These small changes include:
- improving the description of delegated responsibilities to Fund Officers.
 - expanding the description of the operational risks that the Fund faces and how these are managed.
 - rewording and condensing of some investment beliefs.
 - changing references to specific Fund Officer job titles, where these are no longer relevant.

- formatting changes to the SIAB targets and ranges table in appendix B (the stated targets and ranges will not change).

9.8 The updated Investment Strategy Statement 2021, incorporating the revisions and clarifications above is set out in Appendix B for Committee approval.

10.0 Financial implications

10.1 The financial implications are set out throughout the report.

11.0 Legal implications

11.1 The report contains no direct legal implications.

12.0 Equalities implications

12.1 The report contains no direct equal opportunities implications.

13.0 Environmental implications

13.1 The report contains no direct environmental implications.

14.0 Human resources implications

14.1 The report contains no direct human resources implications.

15.0 Corporate landlord implications

15.1 The report contains no direct corporate landlord implications.

16.0 Schedule of background papers

16.1 Investment Strategy Statement 2020 -
<https://www.wmpfonline.com/CHttpHandler.ashx?id=16022&p=0>

16.2 Funding Strategy Statement 2020 -
<https://www.wmpfonline.com/CHttpHandler.ashx?id=12481&p=0>

17.0 Schedule of appendices

17.1 Appendix A – Redington Economic and Market Update Q4 2020.

17.2 Appendix B – Investment Strategy Statement 2021 (To follow).