

<b>CITY OF WOLVERHAMPTON COUNCIL</b>	<b>Pensions Committee</b> 29 September 2021
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**Report title** Quarterly Investment Report to 30 June 2021

**Originating service** Pension Services

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**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 previously referred 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 ISS changes continues to progress, and this report now adopts an interim benchmark comprising policy targets that reflect partial transition to the strategic targets outlined in the ISS, designed to better meet the future needs of the WMPF.

## **3.0 Executive Summary**

- 3.1 As at 30 June 2021, the West Midlands Pension Fund's market value was £19.9 billion (incl. WMTL and PB ABSF). Investment markets generally rose in the quarter continuing the strong recovery from the sharp falls seen in March 2020.
- 3.2 The Main Fund increased by 4.7%% over the quarter matching the return of its benchmark. The Fund's growth assets (largely equities) delivered strong positive returns in the quarter and for the 12-month period to end June 2021. Income and stabilising assets performed less well. The Fund's returns are ahead of its benchmark for 1 year but have trailed over longer time periods.

3.3 The Admitted Body Sub Funds are ahead of the benchmark return 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's Multi-Asset Credit contributed positively to deliver excess return over the quarter and year.

#### 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 30 June 2021, 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:

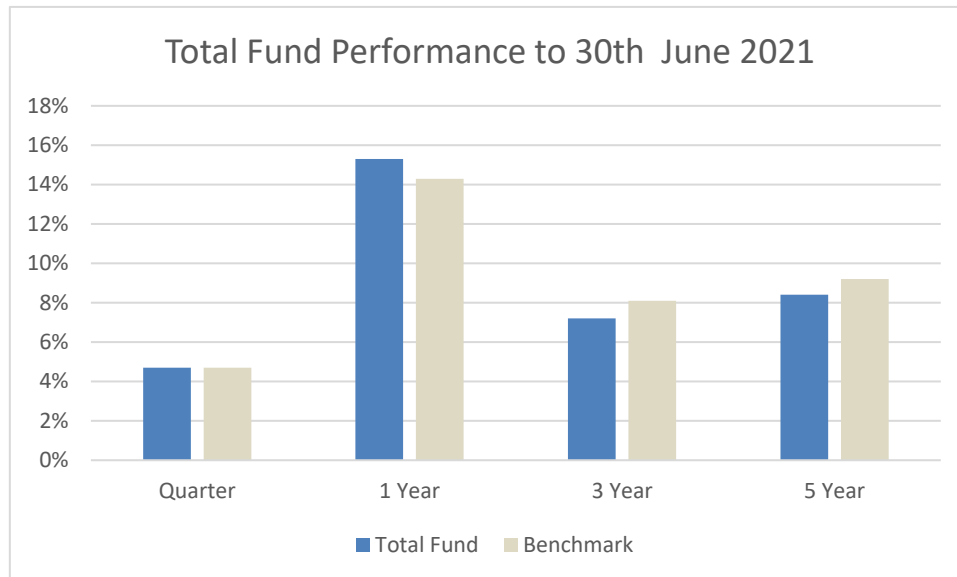
<b>Asset Class Returns (£)</b>	<b>3 months (%)</b>	<b>12 months (%)</b>
US Equity (S&P 500)	8.4%	25.9%
UK Equity (FTSE All Share)	5.6%	21.5%
Emerging Market Equity	4.9%	26.0%
UK Gilts (All Maturities)	1.7%	-6.5%
Corporate Bonds	1.7%	1.8%
Global High Yield Bonds	2.4%	3.4%

4.3 Equities advanced further in the quarter. Government Bond yields fell and Corporate Bonds generally outperformed Government Bonds. 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 4.7% over the quarter matching the benchmark return. The Fund's relative returns versus its benchmark over various time periods are shown below.



- 5.2 The Fund outperformed its benchmark over the 12 months to end June. Private Equity was a large contributor to positive relative performance as strong performance from the portfolio outperformed the listed equity index to which it is compared. A three-month lag has now been introduced to the benchmark for this asset class (effective April 2021 onwards) to make performance comparisons more meaningful.
- 5.3 Infrastructure continues to be a major negative contributor to relative performance. Strong performance from Active Equity and Direct Property portfolio are the main positives.
- 5.4 Over 3 years the main detractors remain Private Equity, Infrastructure and Insurance Linked Securities.
- 5.5 The asset allocation of the Main Fund as at the quarter end is set out overleaf. Interim benchmark weights have been introduced for this quarter to reflect partial transition to the strategic targets outlined in the Fund's ISS. Full adoption of the ISS targets will take some time, especially for illiquid assets such as Infrastructure and Private Debt.
- 5.6 The Fund remained overweight in growth assets versus previous policy targets, as a result of existing equity positions and the strong performance from these asset types.

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	Weight - 30/06/21		Final ISS target		Interim Benchmark Adopted
Developed Market Equity	41.6%		30.0%		40.0%
Emerging Market Equity	7.7%		12.0%		8.0%
<b>Total Equity</b>	<b>54.6%</b>		<b>42.0%</b>		<b>48.0%</b>
Private Equity	7.6%		6.0%		6.0%
Opportunistic	1.6%		2.0%		2.0%
<b>TOTAL GROWTH</b>	<b>63.8%</b>		<b>50%</b>		<b>56.0%</b>
Corporate Bonds	5.1%		4.0%		4.0%
Multi-Asset Credit/Specialist	3.7%		5.5%		5.5%
Emerging Market Debt	4.0%		4.5%		4.5%
Private Debt	0.5%		6.0%		1.0%
Infrastructure	4.2%		9.0%		7.0%
Property	7.0%		9.0%		9.0%
<b>TOTAL INCOME</b>	<b>24.5%</b>		<b>38.0%</b>		<b>31.0%</b>
Gilts	2.2%		2.0%		2.0%
ILG	6.2%		3.0%		5.0%
Low risk strategy (orphan liabilities)	1.6%		5.0%		4.0%
Cash	1.7%		2.0%		2.0%
<b>TOTAL STABILISING (incl. low risk)</b>	<b>11.7%</b>		<b>12.0%</b>		<b>13.0%</b>
<b>TOTAL</b>	<b>100.0%</b>		<b>100.0%</b>		<b>100.0%</b>

- 5.7 The Fund's focus remains on implementing the Strategic Asset Allocation (SAA) changes as agreed as part of the 2020 investment strategy review. Efforts have primarily focused on fixed income assets, with steps being taken to move towards new target weights in Multi-Asset Credit and Private Debt in particular, with Equity holdings will likely to be trimmed over the coming quarter quarters. Options to add to the Fund's Infrastructure investments are also being explored.

## 6.0 West Midlands Pension Fund

### *Detailed Performance Commentary*

#### **Growth Assets**

- 6.1 The total Combined Equity Fund delivered strong absolute performance during the quarter and for the 12 months to 30 June 2021.
- 6.2 The Main Fund's passive equity assets are now almost exclusively managed by the investment pool company, LGPS Central Ltd (LGPSC) with a large proportion of these assets held in an LGPSC 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.

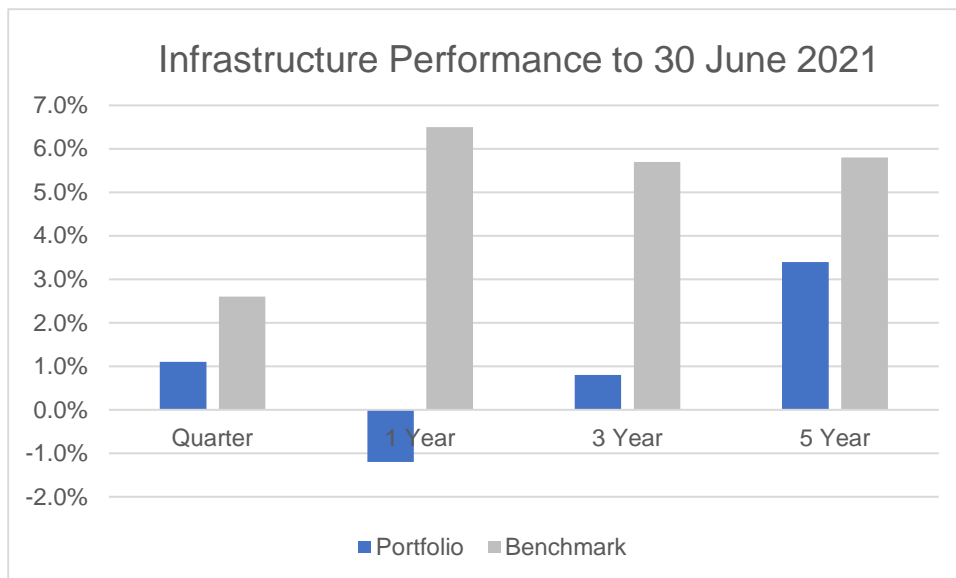
	<b>Quarter</b>	<b>12 months</b>
LGPSC UK (FTSE All Share)	5.4%	20.8%
LGPSC Global ex UK	6.3%	23.3%
LGPSC Dividend Growth (Blended)	6.2%	17.5%
LGPSC Climate Multi-Factor	7.5%	22.2%

- 6.3 Over the quarter, the Fund's actively managed global equities comprised the 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 6.9% underperforming by the benchmark by 0.6%. The fund is comfortably ahead of its benchmark over 1 year (returning 30.6%). The LGPSC Global Active Equity Fund is a blended multi-manager portfolio consisting of 3 underlying portfolios.
- 6.5 Emerging markets lagged developed markets over the quarter and the Fund's Emerging Market Equity portfolio also lagged its benchmark. Performance on a 1-year basis is better. 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 outperformed during the quarter and significantly outperformed over 1 year. The benchmark used for this asset class comprises listed equities plus an outperformance target. As most Private Equity assets experience at least a 3 month 'lag' in being valued periods (such as 18 months) the relative performance (against benchmark) should be interpreted with caution. A 3-month lag to the benchmark return has been introduced from April 2021 onwards. Over longer time periods the portfolio has met expectations.

	<b>Quarter</b>	<b>1 Year</b>	<b>3 year</b>
Private Equity Portfolio	10.2%	36.8%	14.5%
FTSE All World +1% (with lag from April'21)	4.1%	22.1%	13.1%

### Income Assets

- 6.7 The Income segment underperformed its respective benchmark over the quarter and over 12 months. The aggregate property portfolio performed in-line with the benchmark for the 3 month period and continues to outperform on a longer-term basis. The Direct portfolio has 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 performance was weaker.
- 6.8 The infrastructure portfolio delivered a negative return over the course of the year to end June. 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 Fund's Fixed Interest holdings have generally performed well over the year. Both Emerging Market Debt holdings are ahead of benchmark (the LGPS Central fund making a strong start since launch in December 2020). The Fund's Multi Asset Credit investment had a good twelve months (despite underperforming at the onset of the pandemic) as high duration assets such as sovereign and investment grade bonds underperformed high yield. The Fund remains tilted to floating-rate assets. The Fund's Corporate Bond allocations delivered in-line returns over the final quarter but outperformed their benchmarks. Longer-term performance remains strong.

### Fixed Income Performance Highlights

	Quarter		1 Year		3 Year		5 Year	
	Return	Relative	Return	Relative	Return	Relative	Return	Relative
Corporate Bonds	1.7%	0.0%	2.8%	1.1%	5.2%	1.2%	6.4%	0.6%
Multi Asset Credit	1.7%	0.1%	25.0%	2.2%				
Emerging Market Debt	3.9%	0.3%	0.7%	4.9%	5.2%	1.4%		

### ***Stabilising Assets***

- 6.10 Stabilising Fixed Income: The stabilising portfolio comprises the Fund's exposure to government bonds and index linked securities and cash. The stabilising component of the fixed interest portfolio delivered positive returns for the quarter as yields on sovereign debt fell (meaning prices rose). This performance should be expected when risky assets such as equities deliver such strong returns.
- 6.11 Over 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 the last 12 months. It has however, had a larger impact on the performance of the benchmark (which reflect higher hedge ratios for these currency pairs) impacting relative returns (i.e. versus benchmark). The hedge overlay is primarily a risk reduction tool.



## 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):

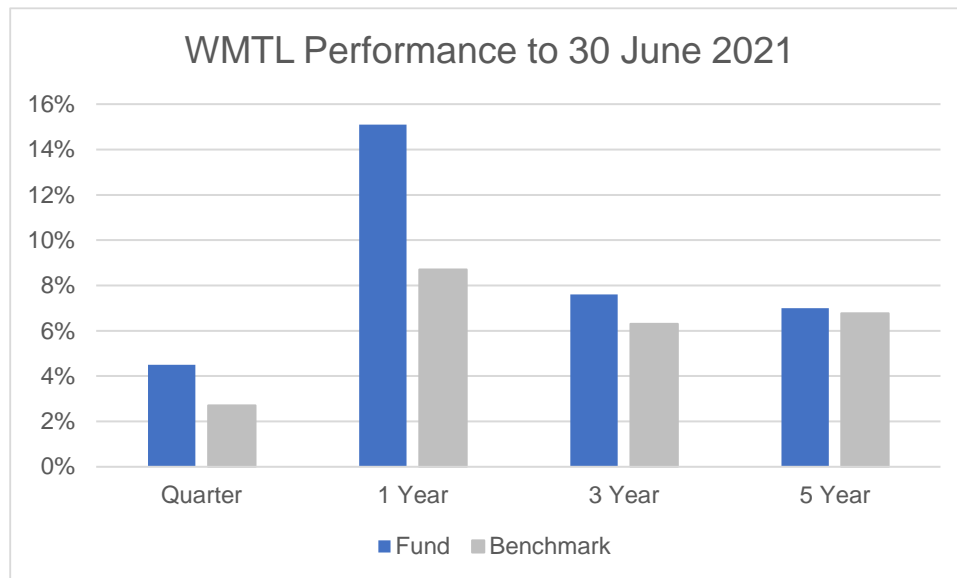
	Value (£000's)	Allocation (%)
Equities	91,533	31%
Diversified Growth Funds	110,893	38%
<b>Total Growth</b>	<b>202,426</b>	<b>69%</b>
Corporate Bonds	10,341	4%
Multi Asset Credit	52,087	18%
LDI/Index Linked Bonds	29,165	10%
Cash	123	0%
<b>Total Defensive</b>	<b>91,716</b>	<b>31%</b>
<b>TOTAL</b>	<b>294,142</b>	<b>100%</b>

PB asset allocation:

	Value (£000's)	Allocation (%)
Equities	3,419	17%
<b>Total Growth</b>	<b>3,419</b>	<b>17%</b>
Corporate Bonds	5,565	28%
Multi Asset Credit	5,701	28%
LDI/Index Linked Bonds	5,355	27%
Cash	59	0%
<b>Total Defensive</b>	<b>16,680</b>	<b>83%</b>
<b>TOTAL</b>	<b>20,099</b>	<b>100%</b>

## WMTL Performance

- 7.2 The Fund outperformed for the quarter and also significantly for 1 year. The Fund is also now marginally ahead of its benchmark for 3 years. Relative performance is driven by the Multi-Asset Credit and Diversified Growth Fund holdings which outperformed 'base rate plus' target performance.



## Fixed Income

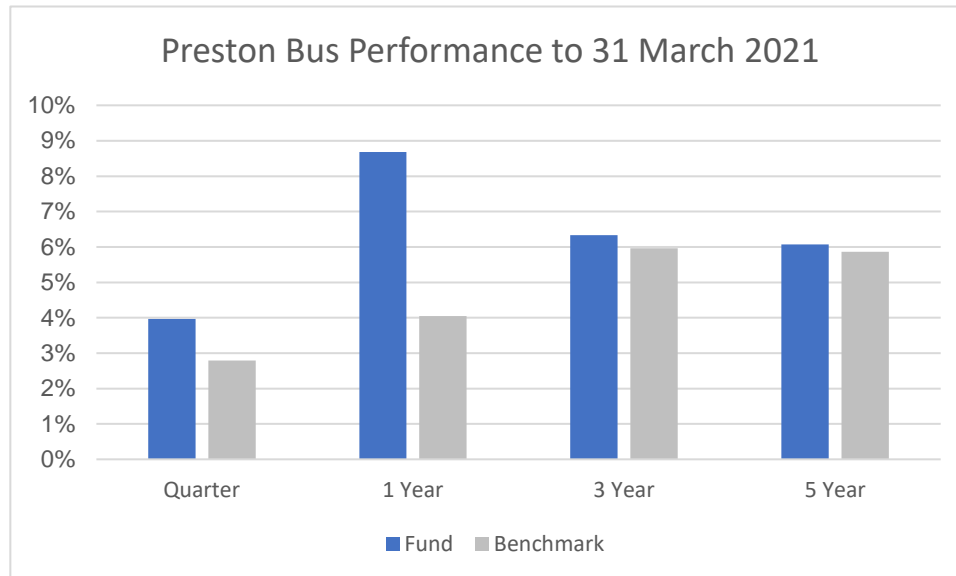
- 7.3 Alongside the Multi-Asset Credit holding in the bond portfolio, there are passive Index Linked Gilts and actively managed Corporate Bonds. The Corporate Bond mandate is performing well, ahead of benchmark over the 1-year period.
- 7.4 Multi-Asset Credit was introduced in Q3 2018. The fund continued its recovery in Q2 2021 and has performed strongly on a 12 month basis.

## Diversified Growth Funds

- 7.5 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.

## PB Performance Summary

7.6 PB performance is summarised below. The Fund very slightly underperformed for the latest quarter but significantly outperformed for 1 year. Relative performance for PB is almost entirely driven by the Multi-Asset Credit allocation, for the same reasons as those described above (for WMTL).



7.7 PB'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 launched in April 2021. In addition, the Fund has been working with a number of Partner Funds and LGPSC to develop a Private Debt offering with initial commitments made during the quarter to June 2021.

## 9.0 Financial implications

9.1 The financial implications are set out throughout the report.

## 10.0 Legal implications

10.1 This report contains no direct legal implications.

## **11.0 Equalities implications**

11.1 This report contains no direct equal opportunities implications.

## **12.0 Other implications**

12.1 There are no other implications.

## **13.0 Schedule of background papers**

13.1 Investment Strategy Statement -

<https://www.wmpfonline.com/CHttpHandler.ashx?id=16022&p=0>

13.2 Funding Strategy Statement -

<https://www.wmpfonline.com/CHttpHandler.ashx?id=12481&p=0>

## **14.0 Schedule of appendices**

14.1 Appendix A – Redington Economic and Market Update Q1 2021/22