

<b>CITY OF WOLVERHAMPTON COUNCIL</b>	<b>Pensions Committee</b> 22 March 2023
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<b>Report title</b>	Quarterly Investment Report to 31 December 2022	
<b>Originating service</b>	Pension Services	
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**Recommendations for action:**

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 Main Fund and Admitted Body Separate 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 Separate 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. The Fund'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.
  - III. This report provides separate commentary on the Main Fund and Admitted Body Separate Funds (ABSF), established for former employers of the West Midlands Integrated Transport Authority Pension Fund, West Midlands Travel Limited (WMTL) and Preston Bus (PB).
  - IV. The Fund has undertaken a fundamental review of the Investment Strategy Statement (ISS) and Funding Strategy Statement (FSS) in conjunction with the triennial actuarial valuation. The updated ISS is presented for Committee approval in a separate report. The SIAB policy targets incorporated will be reflected in future quarterly reports, in line with the 2023 ISS.

## **3.0 Executive Summary**

- 3.1 As at 31 December 2022, the West Midlands Pension Fund's market value was £19.1 billion (incl. WMTL and PB ABSF). Stock markets rebounded over the quarter in what has been a challenging 12 month period for markets in general (in local currency terms), although performance varied by region and sector.
- 3.2 The Main Fund returned 1.8% over the quarter outperforming its benchmark by 0.9%. Over the 1 year the Fund returned -5.9% outperforming the benchmark by 1.2%. Performance relative to the benchmark was 0.2% p.a. and -0.6% p.a. over the 3 and 5 year period respectively.
- 3.3 The ABSFs experienced negative performance over the quarter, one year and three years to 31 December 2022. Negative performance was predominantly driven by the Liability Driven Investment (LDI) and corporate bond allocations. The LDI portfolios are

designed to move in a similar fashion to the expected change in the value of the ABSFs' liabilities in response to changes in interest rates and inflation expectations.

#### 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 2022, 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:

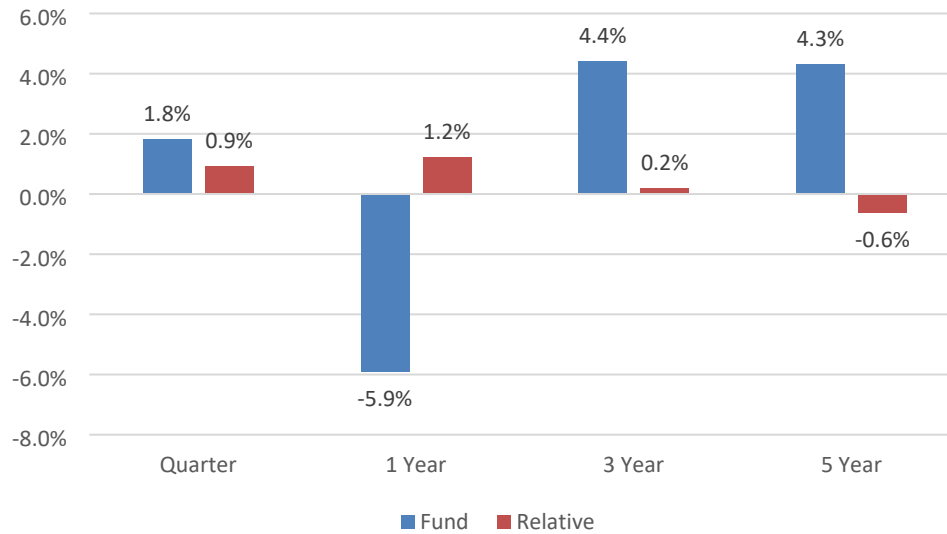
<b>Total Return (£)</b>	<b><u>Quarter</u></b>	<b><u>12 months</u></b>
Global Equity (MSCI World)	1.9%	-7.8%
US Equity (S&P 500)	-0.2%	-7.8%
Emerging Markets (MSCI Emerging Markets)	1.8%	-10.0%
UK Equity (FTSE All Share)	8.9%	0.3%
Gilts (GBI UK All Mats)	1.7%	-24.6%
Corporate Bonds (BofA ML Non-Gilts)	6.2%	-17.8%
High Yield (BofA ML Global High Yield)	-0.7%	-2.3%

#### 5.0 West Midlands Pension Fund

##### ***Main Fund Performance Summary***

5.1 The Main Fund delivered a return of 1.8% over the quarter outperforming the benchmark return by 0.9%. The Fund's relative returns versus its benchmark over various time periods are shown on the following page.

### Performance Summary to 31/12/2022



- 5.2 The Fund outperformed its benchmark over the 12 months to the end of December. Private equity was a large contributor to positive relative performance as continued strong performance from the portfolio outperformed the listed equity index to which it is compared. The Private Equity allocation has also been a significant contributor to positive relative performance over the longer-term.
- 5.3 The Fund's developed listed equity portfolio contributed positively to relative performance over the quarter and 1 year, however, this allocation has detracted from performance over the longer-term.
- 5.4 The asset allocation of the Main Fund as at the quarter end is set out overleaf. Interim benchmark weights have been introduced to reflect partial transition to the strategic targets outlined in the Fund's ISS in force over the quarter. Following the triennial review revised strategic targets are proposed for approval as part of the 2023 ISS. Changes to targets will be reflected in future reporting.
- 5.5 The Fund remained overweight in growth assets versus policy targets, as a result of existing equity positions and the strong absolute performance from these asset types over longer time periods.

	Weight @ 31/12/2022	Existing ISS target	Interim Benchmark
<b>Total Equity</b>	<b>54%</b>	<b>42%</b>	<b>48%</b>
Private Equity	8%	6%	6%
Opportunistic	2%	2%	2%
<b>TOTAL GROWTH</b>	<b>64%</b>	<b>50%</b>	<b>56%</b>
Corporate Bonds	4%	4%	4%
Multi-Asset Credit/Specialist	3%	6%	5%
Emerging Market Debt	4%	5%	5%
Private Debt	3%	6%	1%
Infrastructure	5%	9%	7%
Property	7%	9%	9%
<b>TOTAL INCOME</b>	<b>27%</b>	<b>38%</b>	<b>31%</b>
Gilts	1%	2%	2%
ILG	3%	3%	5%
Low risk strategy (orphan liabilities)	1%	5%	4%
Cash	3%	2%	2%
<b>TOTAL STABILISING (incl. low risk)</b>	<b>9%</b>	<b>12%</b>	<b>13%</b>
<b>TOTAL</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>

Note: Totals may not sum due to rounding.

5.6 The Fund continues to see a good level of capital calls in relation to commitments made to Infrastructure and Private Debt Funds. Higher levels of cash are currently being held pending completion of the triennial investment strategy review and update of SIAB.

## 6.0 West Midlands Pension Fund

### *Detailed Performance Commentary*

#### **Growth Assets**

6.1 The total combined equity fund delivered positive returns during the quarter, outperforming its benchmark. Whilst performance was negative over the 1 year, the equity portfolio did outperform its benchmark over this period. However, there has been underperformance over the three and five year periods to 31 December 2022.

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, however, there was divergence between region and strategy as shown below.

	<b>Quarter</b>	<b>12 months</b>
LGPSC UK (FTSE All Share)	9.0%	0.2%
LGPSC Global ex UK	5.9%	-6.1%
LGPSC Dividend Growth (Blended)	5.9%	-3.0%
LGPSC Climate Multi-Factor	3.7%	-5.9%

- 6.3 The Fund's actively managed global developed market equities comprised the LGPSC Active Equity fund and an allocation to sustainable equity managers.
- 6.4 The LGPSC Global Active Equity Fund outperformed the benchmark over the quarter, one year and three year period. The LGPSC Global Active Equity Fund is a blended multi-manager portfolio consisting of three underlying portfolios.
- 6.5 Emerging markets performed positively over the quarter with the Fund's Emerging Market Equity portfolio outperforming its benchmark. The portfolio has lagged its benchmark over longer time periods.
- 6.6 The private equity portfolio underperformed during the quarter, however, has significantly outperformed over the one year and longer time periods. The benchmark used for this asset class comprises listed equities plus an outperformance target (with a three month lag). Over longer time periods the portfolio has met expectations.

	<b>Quarter</b>	<b>1 Year</b>	<b>3 year</b>
Private Equity Portfolio	-0.4%	12.7%	21.8%
FTSE All World +1% (3m lagged)	1.7%	-2.6%	8.7%

### ***Income Assets***

- 6.7 The Fund's income segment has underperformed its respective benchmark over the quarter and longer time periods. The aggregate property portfolio provided negative returns over the quarter and one year but has delivered positive absolute returns over longer time periods.
- 6.8 The infrastructure portfolio was negative over the quarter, however, has produced strong returns over the one year, outperforming its return objective (CPI +4%), however, the portfolio has underperformed against its return objective over longer time periods.

	<b>Quarter</b>		<b>1 Year</b>		<b>3 Year</b>	
	<b>Return</b>	<b>Relative</b>	<b>Return</b>	<b>Relative</b>	<b>Return</b>	<b>Relative</b>
Infrastructure Portfolio	-0.4%	-3.8%	17.8%	4.5%	5.8%	-3.1%
Property Portfolio	-11.1%	-1.7%	-7.0%	-3.2%	3.2%	-1.0%

6.9 The Fund's fixed interest holdings produced positive performance over the quarter. Within the Fund's fixed interest holdings, corporate bonds have underperformed the benchmark over the quarter but have outperformed over longer time periods. The multi asset credit portfolio has underperformed its benchmark over the quarter, one year and three year time periods.

	Quarter		1 Year		3 Year	
	Return	Relative	Return	Relative	Return	Relative
Corporate Bonds	4.4%	-1.4%	-14.4%	3.3%	-2.6%	2.3%
Multi Asset Credit	3.1%	-0.4%	-9.7%	-7.3%	-1.0%	-2.9%
Emerging Market Debt	4.8%	1.7%	-8.2%	-6.6%	-1.8%	0.0%

### **Stabilising Assets**

6.10 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 negative returns for the quarter as yields on sovereign debt rose (meaning prices fell).

6.11 Over the quarter, one and three year timeframes the stabilising portfolio has outperformed its benchmark.

### **7.0 Admitted Body Separate Funds (ABSFs)**

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

#### WMTL asset allocation (excluding buy-in policy):

Asset Class	Value @31/12/2022	Target %	Current %
<b>Total Equities</b>	£ 53,996,046		24%
UK Equities	£ 4,039,181		2%
North America Equity Index	£ 20,903,306		9%
Europe (ex UK) Equity Index	£ 13,226,253		6%
Japan Equity Index	£ 4,505,094		2%
Asia Pac exJap Dev Equ Ind	£ 4,595,487		2%
World Emerging Markets Equ Ind	£ 6,726,725		3%
DGF	£ 22,017,725		10%
<b>Total Equity and DGF</b>	£ 76,013,771	16%	34%
Corporate Bonds	£ 8,536,608		4%
Multi Asset Credit	£ 48,531,544		22%
Private Debt	£ 20,011,976		9%
LDI	£ 54,561,245		25%
<b>Total Credit &amp; LDI</b>	£ 131,641,373	84%	60%
<b>Cash</b>	£ 13,260,925	0%	6%
<b>Total</b>	£ 220,916,069	100%	100%

The allocation to private debt is expected to increase over time. Commitments have been made in this area, however, given the private nature of these assets, these commitments will draw down from the growth portfolio over a period of time, moving the allocation towards the target.

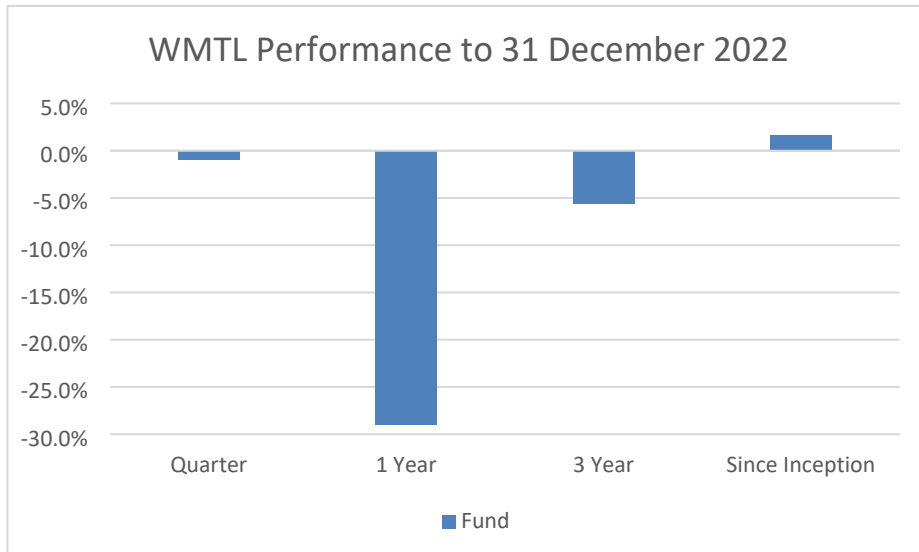
PB asset allocation:

Asset Class	Value @31/12/2022	Target %	Current %
<b>Total Equities</b>	<b>£ 1,685,134</b>	<b>15%</b>	<b>13%</b>
UK Equities	£ 147,567		1%
North America Equity Index	£ 722,769		5%
Europe (ex UK) Equity Index	£ 244,188		2%
Japan Equity Index	£ 189,098		1%
Asia Pac exJap Dev Equ Ind	£ 133,519		1%
World Emerging Markets Equ Ind	£ 247,992		2%
Multi Asset Credit	£ 3,932,280		30%
Corporate Bonds	£ 2,513,241		19%
LDI	£ 3,544,943		27%
Cash	£ 1,580,273		12%
<b>Total Fixed Interest, LDI &amp; Cash</b>	<b>£ 11,570,737</b>	<b>85%</b>	<b>87%</b>
<b>Total</b>	<b>£ 13,255,871</b>	<b>100%</b>	<b>100%</b>

**WMTL Performance**

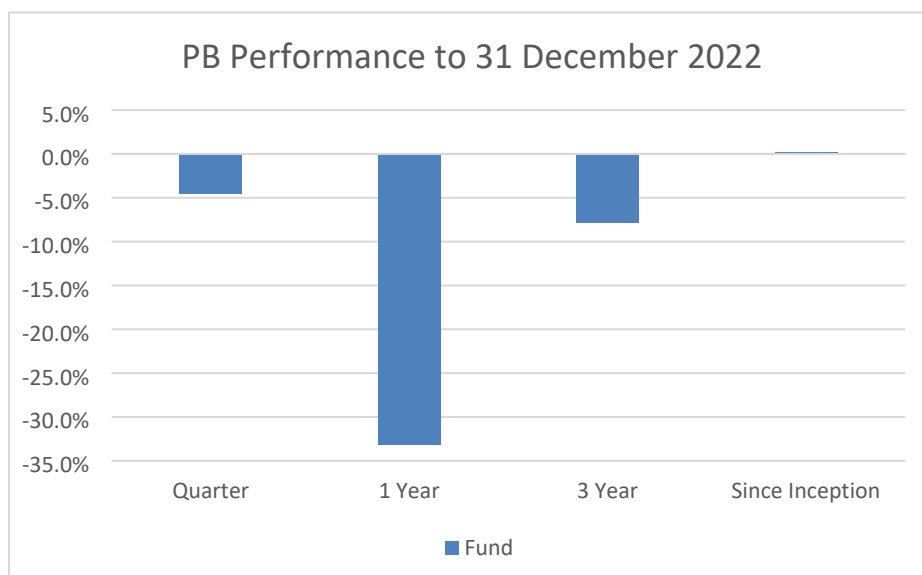
- 7.2 The Fund has produced negative returns over the quarter, one year and three years to 31 December 2022. All assets have contributed to negative performance over the 1 year period, however, the Fund's fixed interest holdings have been the most impacted due to the increasing interest rate environment.
- 7.3 Large falls in the value of the Liability Driven Investment (LDI) portfolio were experienced over the one year period due to sharp increases in UK gilt yields. Whilst this resulted in negative asset returns for the LDI portfolio, the Fund's liabilities are expected to have decreased by a greater extent than the fall in the LDI portfolio.
- 7.4 The diversified growth funds and the multi-asset credit allocation continued to underperform their 'base rate plus' target performance. The corporate bond mandate has outperformed its benchmark over the quarter and one year period.
- 7.5 A review of the Fund's benchmark is currently being undertaken and therefore only absolute Fund returns have been shown below.





### PB Performance Summary

- 7.6 PB performance is summarised below. Similar to WMTL, the Fund produced negative returns over the quarter, one year and three years to 31 December 2022 with recent performance impacting longer-term numbers.
- 7.7 The majority of negative performance was driven by the fixed interest holdings, in particular the LDI portfolio given the sharp increase in UK gilt yields experienced over the one year period. The LDI mandate is designed to move in a similar manner to the Fund's liabilities in response to changes in interest rates and inflation expectations.
- 7.8 A review of the Fund's benchmark is currently being undertaken and therefore only absolute Fund returns have been shown below.



## **8.0 Investment Pooling**

8.1 The Fund continues to work closely with its investment pool company LGPS Central Ltd (LGPSC) to review the ongoing suitability of investment products and look for opportunities to transition assets to the pool where relevant.

## **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 None.

## **14.0 Schedule of Appendices**

14.1 Appendix A – Redington Economic and Market Update