REDINGTON

West Midlands Pension Fund

YOUR MARKET AND INVESTMENT UPDATE

Q2 2023

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WHAT HAPPENED DURING THE QUARTER

Pete Drewienkiewicz (Chief Investment Officer)

Market Summary

Q2 saw markets shrug off the banking sector turmoil seen in Q1, with risk assets performing strongly as inflation moderated meaningfully in the US and Europe. Technology stocks also saw a resurgence, led by a wave of Artificial Intelligence enthusiasm. The ECB, Fed and Bank of England continued to hike interest rates in response to inflation prints above their respective targets. The BoE hiked rates by 75bps over the quarter relative to 25bps and 50bps moves in the US and Europe, a likely response to the slower fall in UK inflation. This put pressure on UK markets which performed poorly relative to other developed market counterparts over the quarter.

Key Points for You

- Expected returns increased slightly over the quarter from Gilts + 3.6% at 31 March 2023 to Gilts + 3.8% at 30 June 2023. This was largely driven by higher expected return assumptions for Equities and Property.
- Asset-side risk, as measured by VaR 95%, increased from 16.2% at 31 March 2023 to 16.5% at 30 June 2023.

Market Data

Equity Index	Level	Change since 31-Mar-23	Change since 30-Jun-22
FTSE 100 (Total Return)	7905	-0.3%	9.1%
S&P 500 (Total Return)	9560	8.7%	19.6%
EuroStoxx 50 (Total Return)	2031	4.2%	31.6%
Nikkei 225 (Total Return)	57670	18.5%	28.6%
MSCI World (Total Return)	7180	7.1%	18.2%
MSCI Emerging Markets (Total Return)	662	1.7%	3.3%
FX			
USD vs GBP	1.27	3.0%	4.3%
EUR vs GBP	1.16	2.3%	0.3%
Credit Spreads			
Sterling Non-Gilt Index	122	-14 bps	-5 bps
Sterling Non-Gilt 15Y+ Index	164	-17 bps	-31 bps
Global Investment Grade	132	-13 bps	-23 bps
US Investment Grade	150	-16 bps	-21 bps
Global High Yield	393	-49 bps	-135 bps
European High Yield	339	-25 bps	-136 bps

Market Data

UK Gilts	Level	Change since 31-Mar-23	Change since 30-Jun-22
10Y	4.43	87 bps	212 bps
30Y	4.38	50 bps	182 bps
UK Nominal Swaps			
10Y	4.54	86 bps	194 bps
30Y	3.92	52 bps	151 bps
Gilt Breakeven Inflation			
10Y	3.79	0 bps	11 bps
30Y	3.39	-8 bps	17 bps
UK RPI Swap			
10Y	3.97	3 bps	-8 bps
30Y	3.40	-2 bps	5 bps
UK Gilt Real Rates			
10Y	0.65	87 bps	201 bps
30Y	0.99	58 bps	165 bps
US TIPS			
20Y	1.82	16 bps	46 bps
30Y	1.51	15 bps	61 bps

VIEWS FROM THE ASSET CLASS SPECIALISTS

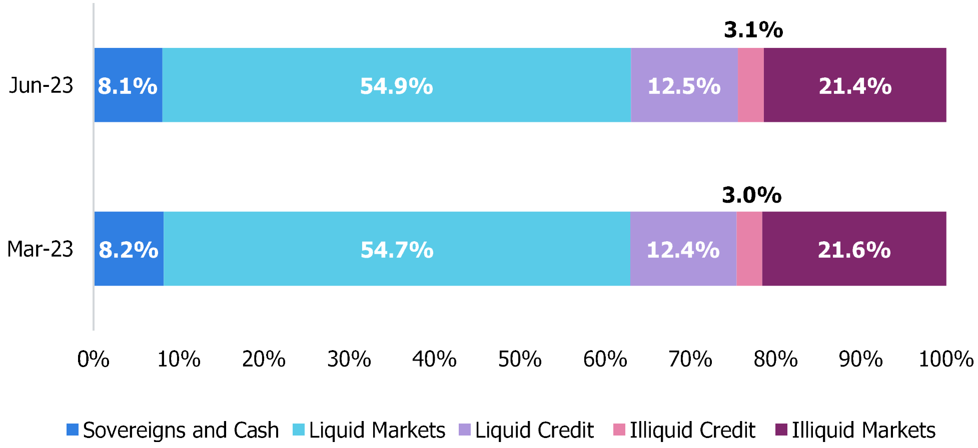
 **Kate Mijakowska** **Government Bonds**	The second quarter of 2023 saw a significant increase in yields, particularly in May, as the UK labour market proved surprisingly resilient to the central bank rate hikes, but inflation prints remained elevated. Over the quarter, UK 30-year nominal gilt yields rose 50bps, while 20-year index-linked gilt yields increased 63bps. Bank of England hiked the base rate by 25bps in May, and another 50bps in June. UK CPI May year-on-year figure printed at 8.7%, above expectations and more than double the US CPI of 4.0% for that month. That said, in June, UK CPI fell to 7.9% which was below market expectations. In April, TPR published a guidance around resilience of LDI portfolios. This was in line with the recommendations published in March by the Bank of England Financial Policy Committee. We saw a few LDI managers re-adjust their collateral buffer frameworks, including levels at which notifications are sent to clients.
 **Oliver Wayne** **Liquid Markets (Equities)**	Developed markets (“DM”) delivered positive returns over Q2, largely attributed to the strong performance of mega-cap tech names that were boosted by enthusiasm over Artificial Intelligence (“AI”). This created an exceptionally narrow market leadership, with the vast majority of DM market returns generated by a small number of companies. Emerging markets (“EM”) generated moderately negative returns, primarily driven by China which was the worst-performing market. Despite the removal of pandemic-related restrictions, the economic rebound has disappointed investors. On a style factor basis, there has been contrasting performance across DM and EM. Growth and Quality factors performed strongly in DM but poorly within EM. Value and Momentum underperformed within DM and outperformed within EM. From a size perspective, larger cap names outperformed within DM but underperformed with EM. Overall, this backdrop was more supportive for active EM managers whereas active DM managers faced headwinds.
 **Alexander Robinson** **Liquid Markets (Multi-Asset)**	It was a mixed second quarter for multi-asset performance. Global equities rose, led by the US, global investment grade corporates were broadly flat whilst high yield gained. Interest rates rose over the quarter causing pain for those long government bonds. Broad commodities had a volatile quarter and also ended in negative territory. This combination has led to varying results for long only multi-asset strategies as they try to navigate this macro-driven environment, with fairly mixed results across the board both positively and negatively depending on risk allocation. Diversified Risk Premia (“DRP”) strategies had a positive quarter, helped by strong performance from trend following after what was a historically challenging Q1 as a result of the banking turmoil in March. Most style factors also performed well, benefitting style premia strategies.

VIEWS FROM THE ASSET CLASS SPECIALISTS

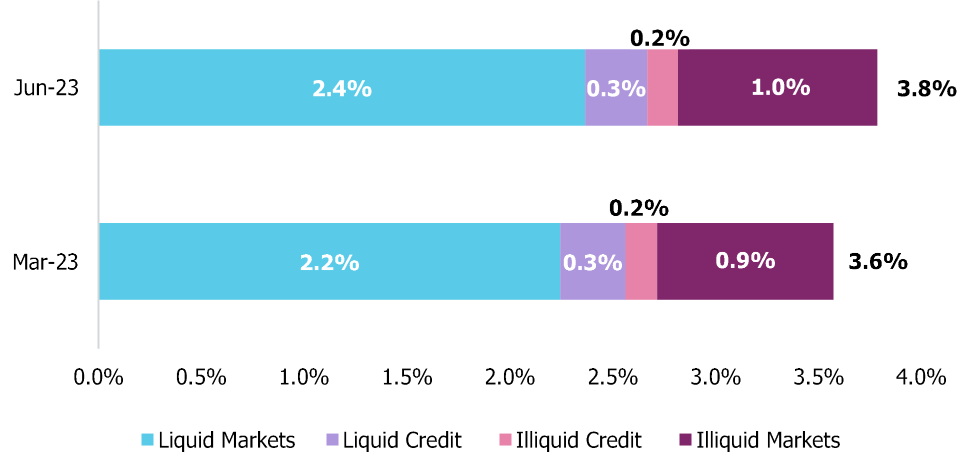
 **Chris Bikos** **Liquid & Semi-Liquid Credit**	From a credit perspective, the second quarter proved resilient as corporate balance sheets remained relatively strong, despite some uptick in default rates. Consequently, credit spreads tightened across the board. However, the volatility in interest rates remained elevated with all the major developed market central banks raising interest rates. More specifically, the Federal Reserve (Fed) raised interest rates by 25 basis points (bps) in May, European Central Bank (ECB) hiked twice in the quarter, as did the Bank of England (BoE). With that in mind, corporate credit outperformed government bonds with high yield outperforming its investment grade counterparts. Long-duration assets, such as long-dated corporate bonds, suffered the most. On the other hand, floating-rate assets such as structured credit and leveraged loans benefited from the high income on offer due to the high level of rates. Dispersion within emerging market debt picked up, with South Africa being among the worst performers as the country's power situation continued to deteriorate.
 **Tricia Ward** **Illiquid Markets**	Infrastructure had a relatively resilient Q2, with the Infra300 index returning 0.89% driven primarily by renewables. Infrastructure equity valuations remained stable over the quarter despite major central bank rate rises. Despite positive returns, infrastructure fundraising continued to suffer, with Preqin reporting only c.$7bn raised over the quarter, a c.88% decrease against Q2 last year. A surprise rise in UK core inflation caught the Real Estate market off-guard leading to further falls, albeit marginal ones, in commercial property values in May and June, with the MSCI UK Quarterly Property Index showing capital returns of -0.03% and -0.48%. This was offset by steady income returns, with only June showing a negative total return (-0.03%). The decline in capital values continued to be led by offices, with yields on prime city offices expanding 0.25% over the quarter, and market sentiment around offices more broadly remaining negative due to ongoing concerns around working from home and asset stranding resulting from minimum energy efficiency standards.
 **Sarah Miller** **Illiquid Credit**	Private credit issuance in Q2 continued to outpace broadly syndicated loan financing - taking 85%, by count, of LBO deals (LCD, Pitchbook). Default rates declined marginally in Q2, per Proskauer, to 1.64%, suggesting stability. However, interest and fixed charge coverage ratios declined to ~1.1x as interest expenses have almost doubled, reflecting the potential stress for existing loans. Concurrently, continued higher rates constrain the amount of debt lenders will offer and companies can support for new loans, typically resulting in larger equity cushions and a stronger relative positioning for lenders. Current credit market activity is driven by refinancings and loan extensions (Pitchbook, KKR), addressing near-term maturities. Larger private credit facilities would historically have been replaced by cheaper public credit at maturity, but private lenders now provide the refinancing, owing to their certainty of capital. As pressure on bank lending continues, opportunity is created for corporate direct lending and for asset-based lending – either as replacement capital to banks or for private lenders to finance collateralised loans sitting on bank balance sheets.

YOUR ASSET ALLOCATION AND EXPOSURE

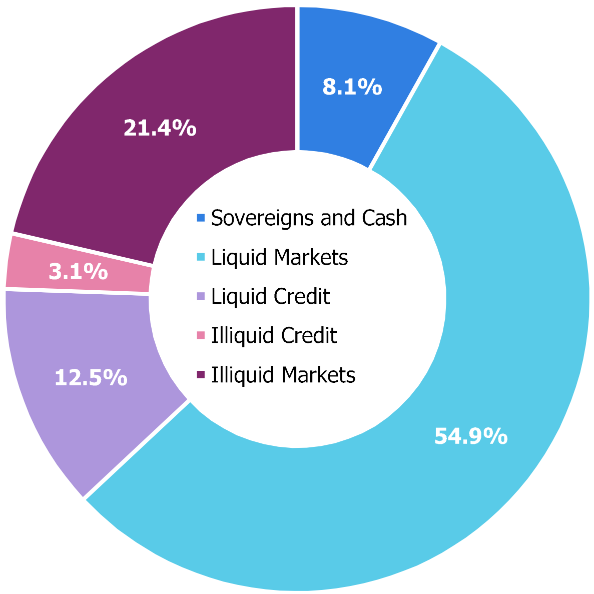
Asset Allocation Change



Expected Return Contribution Change (over gilts)



Note, asset class expected returns are in the appendix.

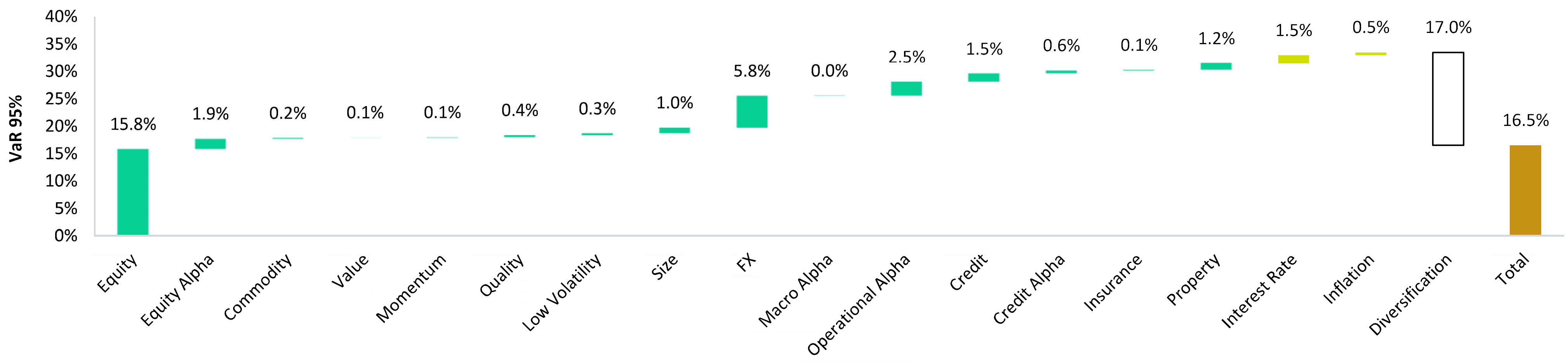


Detailed Asset Allocation

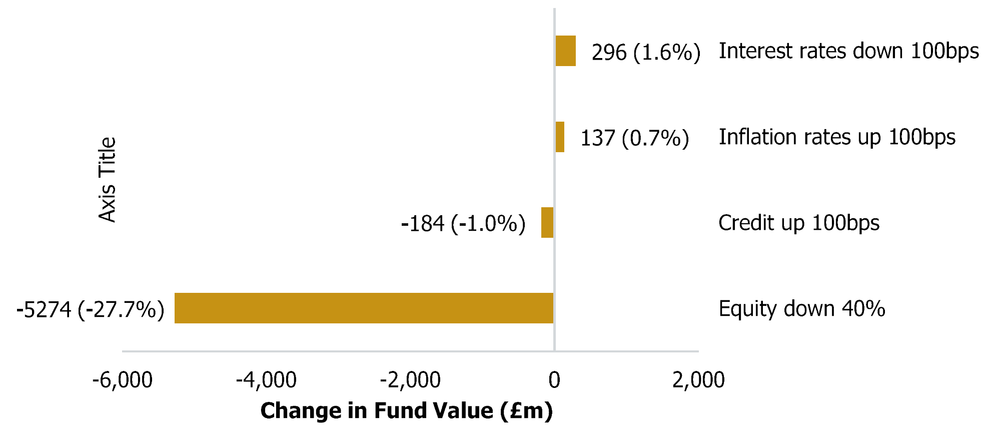
Cash	3.3%	Sustainable Equities - RBC	2.2%
LGIM Overseas Bonds	0.5%	Sustainable Equities - WHEB	0.6%
Index-Linked Gilts	3.6%	Emerging Markets Equities	6.6%
Nominal Gilts	0.7%	Aegon Short Dated Investment Grade Bond Fund	1.5%
ACS LGPS UK Equity Passive Fund	6.5%	UK Corporate Bonds	2.7%
ACS LGPS Global Ex UK Passive Equity	15.0%	LGPS Central Global Active IG Corporate Bond Fund	0.9%
ACS LGPS Global Equity Dividend Growth Factor	2.5%	Multi-Class Credit	3.5%
ACS LGPS All World Equity Climate Multi Factor	11.5%	Emerging Market Debt Funds	3.8%
LGPS Central Global Equity Multi Manager Fund	6.6%	Diversified Private Credit	3.1%
LGIM UK All Share	0.3%	Infrastructure	5.5%
Equities held with Merrill Lynch	0.4%	Property	7.2%
Smaller Equity Positions	0.1%	Opportunistic Funds	1.2%
Sustainable Equities - Impax	2.7%	Private Equity	7.6%

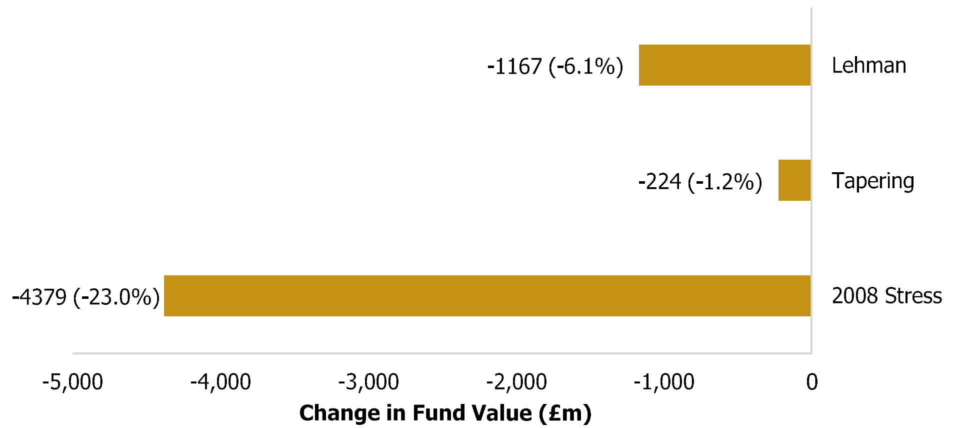
HELPING YOU UNDERSTAND YOUR RISK

Current Value-at-Risk 95% (Asset Only)



Scenario Analysis





APPENDICES

REDINGTON'S EXPECTED RETURNS – JUNE 2023

Asset Class	Expected Return (Gilts +)	Volatility	Expected Fees (p.a.)
Equity			
Developed Market Equities	4.1% ↑	17.0% ↑	0.0%-0.1%
Sustainable Equities	4.2% ↑	16.0% ↑	0.2%-0.4%
Emerging Markets Equities	4.7% ↑	20.2% ↑	0.1%-0.2%
Liquid Credit			
Corporate Debt GBP – Passive	1.3% ↓	5.7% ↓	0.1%-0.2%
Corporate Debt GBP – Active	1.6% ↓	5.8% ↓	0.2%-0.3%
Emerging Market Debt – Corporates	2.2% ↓	6.8% ↓	0.4%-0.6%
Emerging Market Debt – Local Currency Sovereign	3.1% ↓	13.4% ↓	0.5%-0.8%
Emerging Market Debt – Hard Currency Sovereign	2.1% ↓	8.2% ↓	0.5%-0.8%
Multi-Class Credit Global	4.0% ↓	7.3% ↓	0.4%-0.7%
Illiquid Credit			
Diversified Matching Illiquids	2.8% ↑	7.5% ↑	0.3%-0.5%
Opportunistic Illiquid Credit	4.9% ↓	11.0% ↓	1.0%-1.5% (+ performance fee)
Securitised Opportunities	3.7% ↓	5.6% ↓	0.5%-0.7%
Special Situations	6.6% ↓	13.8% ↓	1.0%-1.5% (+ performance fee)
Illiquid Markets			
Private Equity	5.7% ↑	31.0% ↑	1.0%-1.5% (+ performance fee)
Commercial Property	3.5% ↑	11.8% ↓	0.4%-0.6%
Renewable Infrastructure (Whole Projects)	3.5% ↓	14.8% ↑	0.5%-0.7% (+ performance fee)

Fee data is estimated based on fees of preferred managers in each strategy. In practice, each fee would be negotiated for West Midlands and may be considerably lower.

GLOSSARY

Term	Description
Annual Management Charge (AMC)	The fee charged by the asset manager for managing the fund, typically expressed as an annual percentage on the invested assets. This excludes additional expenses, e.g. administrative costs, which when combined with the AMC make up a fund’s total expense ratio (TER).
Credit Risk	The risk of financial loss as a result of the inability or unwillingness of an entity to make payments as they become due. Many types of relationships involve credit risk, such as those in which a company owes money to its suppliers (trade debt) or where a counterparty is required to make payments under a derivative contract (counterparty credit risk).
Credit Spread	The difference in the yield between two different bonds, due to different credit quality. The credit spread reflects the additional yield an investor can earn from taking incremental credit risk. Is it often quoted in relation to the yield on government bonds.
Inflation	The average rate at which prices (of products and services) increase over time. It gradually reduces the value of money over time – the higher the rate of inflation, the greater the erosion of value.
Risk Attribution	The process of attributing certain components of total risk to various sources such as inflation risk, credit risk, equity risk, etc.
Stress Testing	A tool used to assess a portfolio’s exposure to large – but plausible – shocks. In the broadest sense, stress testing is a ‘what if’ exercise and can be modelled across various scenarios. For example, a stress test can be used to simulate the performance of a portfolio during 9/11, Black Monday and the Global Financial Crisis of 2007-08.
Value-at-Risk (VaR)	The minimum value that the Fund would expect to lose (at risk) for a given confidence level, over a given time horizon. We have used a 1-in-20 (i.e. 95%) confidence level. For example, if a portfolio’s 95% 1-year VaR is £200 million, it would have a 5% chance (1-in-20) of suffering a loss over the year of £200 million or more.
Volatility	A measure of variability that is used as a common metric for risk. It represents the value of one standard deviation change in the value of an assets’ return. Under certain assumptions, we are able to use this measure to calculate the probability of a given change in the value of the asset or portfolio.
Yield	The income return on an investment. It is based on the received cash flows of a security and is usually expressed as an annual percentage.
Yield Curve	A graphical representation showing the yields of a set of financial instruments by maturity. For example, the par interest rate swap curve or the UK Gilt curve.

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