

CITY OF WOLVERHAMPTON COUNCIL	Pensions Committee 23 June 2021
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Report title	Quarterly Investment Report to 31 March 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 (appendix A).
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 previous ISS and SIAB policy targets. These were refreshed as part of the 2020 ISS review and later re-confirmed in the interim 2021 review, approved by the Pensions Committee in March 2021. Implementation of the 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.

3.0 Executive Summary

- 3.1 As at 31 March 2021, the West Midlands Pension Fund's market value was £18.7 billion (incl. WMTL and PB ABSF). Investment markets generally rose in the quarter continuing the strong recovery from lows seen in March 2020.
- 3.2 The Main Fund increased by 1.7% 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 March 2021. Income and stabilising assets performed less well. 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 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 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 31 March 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:

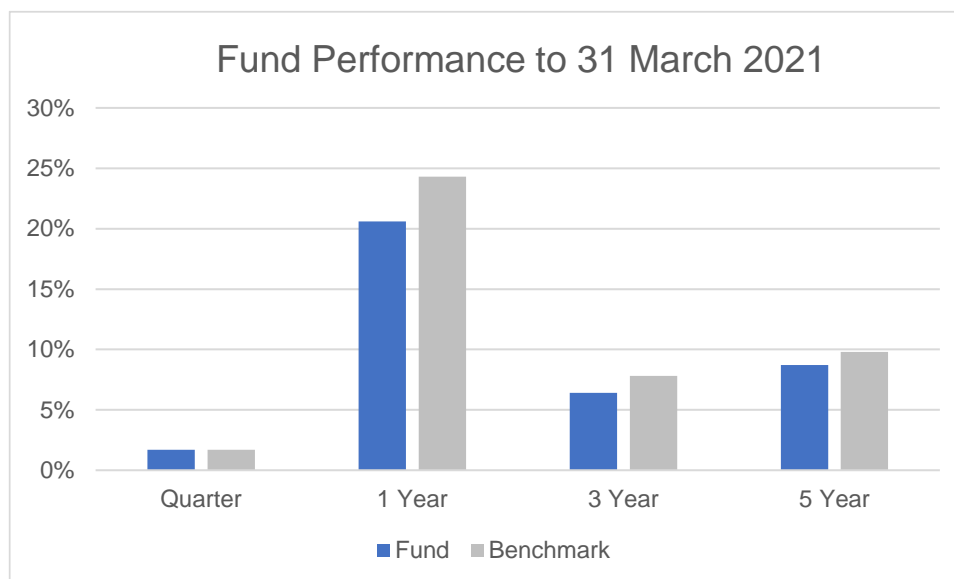
Asset Class Returns (£)	3 months (%)	12 months (%)
US Equity (S&P 500)	5.2%	40.5%
UK Equity (FTSE All Share)	5.2%	26.7%
Emerging Market Equity	1.3%	42.3%
UK Gilts (All Maturities)	-7.4%	-5.6%
Corporate Bonds	-4.1%	7.0%
Global High Yield Bonds	-1.0%	12.9%

- 4.3 Equities advanced further in Q1 2021 capping a very strong rebound for the 12-month period. Cyclical and lowly-valued parts of the market fared well. Emerging Markets lagged developed markets. Government bond yields rose and Corporate Bonds 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 Including the currency hedge the Main Fund delivered a return of 1.7% over the quarter matching the benchmark return. The Fund's relative return remains negative over 1, 3 and 5 years.



- 5.2 The Fund trailed its benchmark significantly over the 12 months to 31/03/2021. Private Equity, Infrastructure and holding excess cash were the main causes. Relative returns are also negative over 3 and 5 years. Strong performance from Active Equity and Direct Property portfolio are the main positives. The currency hedge added to absolute returns (as Sterling strengthened) but Fund relative return worsens vs benchmark when the hedge is considered (the Fund was underhedged vs the ratio assumed benchmark).
- 5.3 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 revised 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 allocations to sovereign debt. This position is being deliberately maintained whilst the Fund holds excess Growth assets versus new targets being adopted.

	Value (£m)	Allocation (%)	Current Benchmark (%)	New Target (%)
Quoted equities	9,900,382,079.06	53.9%	48%	42.0%
Private Equity	1,375,520,896.38	7.5%	10%	6.0%
Opportunistic	304,745,372.48	1.7%	5%	2.0%
Total growth	11,580,648,347.92	63.1%	63%	50.0%
UK Gilts	429,611,851.78	2.3%	2%	2.0%
Index Linked bonds	1,247,946,545.81	6.8%	5%	4.0%
Cash	524,890,713.98	2.9%	2%	2.0%
Corporate bonds	1,163,994,590.65	6.3%	5%	6.0%
Total Stabilising	3,366,443,702.22	18.3%	14%	14.0%
Multi-Asset Credit	392,204,225.30	2.1%	4%	6.5%
Private Debt	65,837,774.15	0.4%	0%	7.0%
Emerging Market Debt	750,128,613.62	4.1%	4%	4.5%
Property	1,377,101,350.92	7.5%	10%	9.0%
Infrastructure	819,688,000.51	4.5%	6%	9.0%
Total Income	3,404,959,964.50	18.6%	23%	36.0%
TOTAL	18,352,052,014.64	100%		

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 (private debt) in particular, with cash holdings expected to be deployed over the coming quarters.

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 31 March 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.

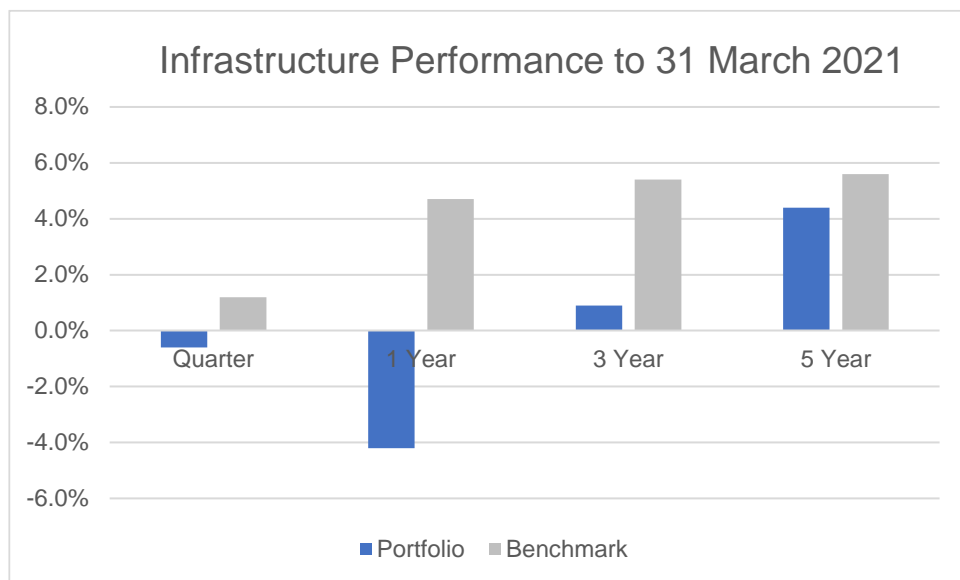
	Q1 2021	Full Year 2020
LGPSC UK (FTSE All Share)	5.0%	26.4%
LGPSC Global ex UK	3.0%	38.0%
LGPSC Dividend Growth (Blended)	4.2%	28.4%
LGPSC Climate Multi-Factor	3.1%	34.7%

- 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 5.8% outperforming by the benchmark and target return by 1.4%. 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 3 underlying 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 and 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 outperformed during the quarter but significantly underperformed over 1 year. The benchmark used for this asset class comprises listed equities plus an outperformance target. Most Private Equity assets experience at least a 3 month 'lag' in being valued. As such, during volatile periods (such as last year) the relative performance (against benchmark) should be interpreted with caution. Over longer time periods the portfolio has met expectations and achieved benchmark level returns. Underperformance from the Private equity portfolio was a significant driver for underperformance for the entire Fund. For illustration purposes, the portfolio is shown below against the assigned benchmark (global equities +1% outperformance target) and the same index with a lag (i.e. to December 2020).

	Quarter	1 Year	3 year	5 Year
Private Equity Portfolio	14.0%	20.2%	12.8%	12.6%
FTSE All World +1%	4.1%	40.6%	14.2%	16.1%
FTSE All World (to Dec'20)	8.5%	13.0%	10.1%	14.5%

Income Assets

- 6.7 The Income pool underperformed its respective benchmark over the quarter. The aggregate property portfolio had a very mixed 12 months 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, supermarkets 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. 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 performed well over the year. Both Emerging Market Debt holdings are ahead of benchmark (the LGPS Central fund making a strong start since launch). 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 negative 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	-3.7%	0.4%	8.9%	1.9%	5.8%	4.0%	6.2%	4.5%
Multi Asset Credit	2.1%	0.1%	25.0%	2.2%				
Emerging Market Debt	-6.3%	0.2%	6.1%	3.2%	3.4%	1.2%		

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 negative returns for the quarter as yields on sovereign debt rose (meaning prices fell). This performance should be expected when risky assets such as equities deliver such strong 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 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):

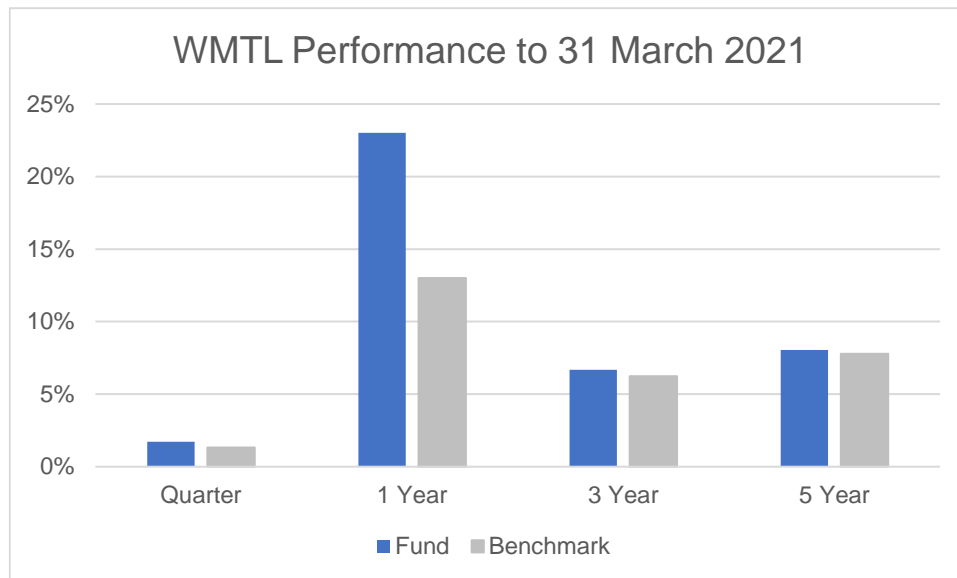
	Value (£m)	Allocation (%)
Equities	85,828	30%
Diversified Growth Funds	107,146	38%
Total Growth	192,974	68%
Corporate Bonds	10,135	4%
Multi Asset Credit	51,038	18%
LDI/Index Linked Bonds	27,015	10%
Cash	2,352	1%
Total Defensive	90,540	32%
TOTAL	283,574	100%

WMPB asset allocation:

	Value (£m)	Allocation (%)
Equities	3,429	18%
Total Growth	3,429	18%
Corporate Bonds	5,454	28%
Multi Asset Credit	5,586	29%
LDI/Index Linked Bonds	5,054	26%
Cash	<1	0%
Total Defensive	16,094	82%
TOTAL	19,534	100%

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

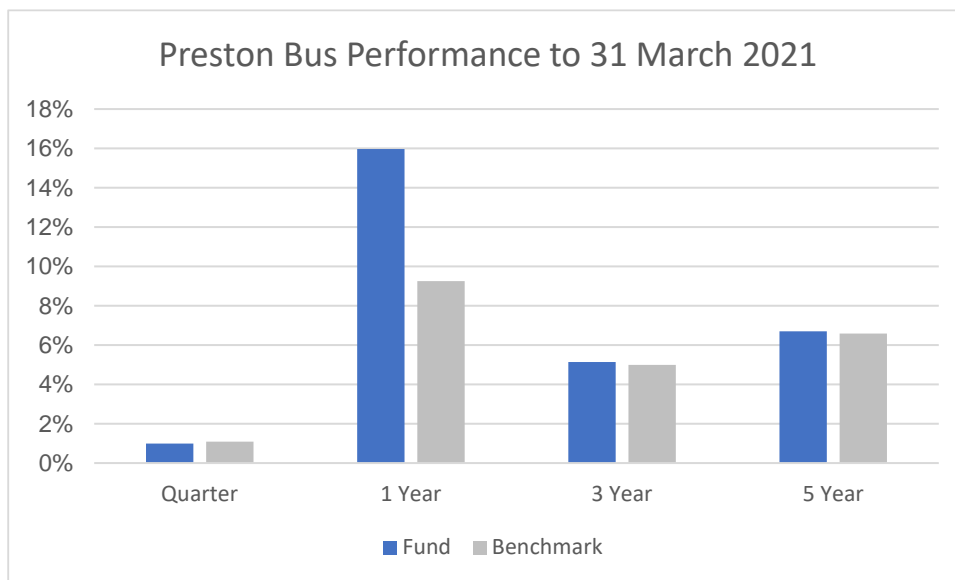
- 7.3 Alongside the Multi-Asset Credit holding in the bond portfolio, there are passive Index Linked Gilts and actively managed Corporate Bonds. The Corporate Bond mandate is performing well, ahead of benchmark over the 1-year period.
- 7.4 Multi-Asset Credit was introduced in Q3 2018. The fund continued its recovery in Q1 2021 and ended the year with a very strong return (but behind its benchmark).

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.

WM PB Performance Summary

- 7.6 WM 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.

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 All other implications

12.1 This report contains no other direct 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