REDINGTON

West Midlands Pension Fund

YOUR MARKET AND INVESTMENT UPDATE

Q1 2022

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WHAT HAPPENED DURING THE QUARTER

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Market Summary

Markets have moved from an environment where growth is the main driver of price movements to one where inflation is the main price driver. Historical asset class relationships may not be maintained in this new environment, from both a return and a correlation perspective. This has been manifested this quarter by equities and bonds selling off in tandem while commodities have risen – a reversal of the behaviour seen over the last 20 years.

In order to dampen inflation, central banks are tightening monetary policy; however, it remains to be seen whether this will be sufficient to pull inflation back in line with central bank targets without sending economies into recession. While higher interest rates can reduce demand, they may not offer additional supply and this supply/demand interplay will be crucial in determining whether inflation will persist.

Key Points for You

- Expected Returns remained broadly unchanged over the quarter at Gilts + 3.4%. A decreased allocation to equities was largely offset by an increased expected return for credit assets (see appendix) and a higher allocation to illiquid markets.
- Asset-side risk, as measured by VaR 95%, increased slightly from 15.8% at 31 December 2021 to 16.2% at 31 March 2022.
- The Pension Risk Management Framework ("PRMF") in this report contains asset-only monitoring metrics. Our proposed PRMF, which includes liability-based metrics, has been included in the appendices.

Market Data

Equity Index	Level	Change since 31-Dec-21	Change since 31-Mar-21
FTSE 100 (Total Return)	7524	2.9%	16.1%
S&P 500 (Total Return)	9527	-4.6%	15.6%
EuroStoxx 50 (Total Return)	1704	-8.9%	2.1%
Nikkei 225 (Total Return)	47174	-2.5%	-2.8%
MSCI World (Total Return)	7089	-4.6%	11.6%
MSCI Emerging Markets (Total Return)	698	-6.1%	-9.9%
FX			
USD vs GBP	1.31	-2.9%	-4.7%
EUR vs GBP	1.19	-0.3%	1.0%
JPY vs GBP	159.9	2.7%	4.8%
Credit Spreads			
Sterling Non-Gilt Index	105	36 bps	15 bps
Sterling Non-Gilt 15Y+ Index	175	38 bps	31 bps
Global Investment Grade	124	37 bps	32 bps
US Investment Grade	146	46 bps	44 bps
Global High Yield	367	33 bps	15 bps
European High Yield	318	28 bps	28 bps

Market Data

UK Gilts	Level	Change since 31-Dec-21	Change since 31-Mar-21
10Y	1.64	66 bps	70 bps
30Y	1.75	64 bps	34 bps
UK Nominal Swaps			
10Y	1.93	49 bps	86 bps
30Y	1.69	48 bps	44 bps
Gilt Breakeven Inflation			
10Y	4.36	44 bps	75 bps
30Y	3.67	28 bps	29 bps
UK RPI Swap			
10Y	9.29	295 bps	600 bps
30Y	5.72	103 bps	222 bps
UK Gilt Real Rates			
10Y	-2.72	22 bps	-5 bps
30Y	-1.92	36 bps	5 bps
US TIPS			
20Y	0.12	46 bps	52 bps
30Y	-0.03	14 bps	24 bps

VIEWS FROM THE ASSET CLASS SPECIALISTS

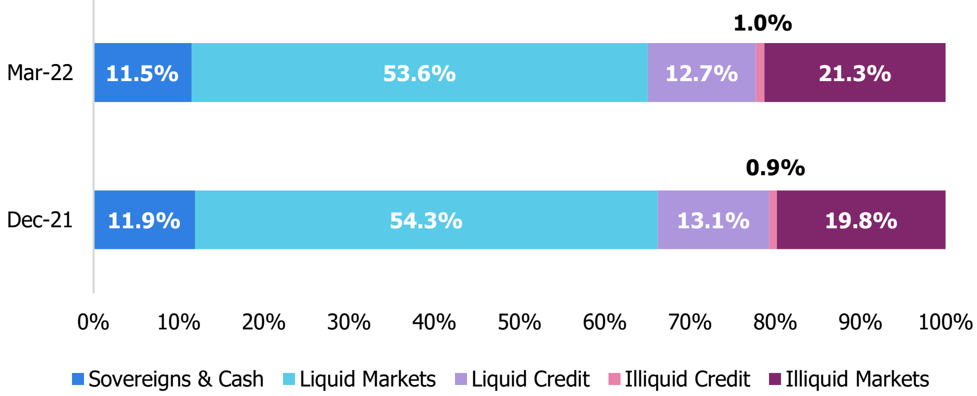
		**Kate Mijakowska** **Government Bonds**	Q1 2022 saw a considerable move up in gilt yields. The 20-year nominal yield increased by 64bps (intra-quarter, it was up as much as 76bps at one point). As inflation expectations also rose meaningfully, real yields at the 20-year point only increased by 33bps. Inflation expectations at the front end of the curve saw some extreme movements, with a 5-year UK RPI swap up 71bps on the quarter. During the quarter, the Bank of England delivered two 25bps hikes and announced that it would start to cease reinvesting the proceeds of maturing bonds from the Quantitative Easing Programme. In March, the government also issued the Spring Statement, which suggested the government plans to issue £125bn of gilts in the 2022/23 financial year, c. £25bn below market expectations.
		**Oliver Wayne** **Liquid Markets (Equities)**	Global developed markets (DM) delivered negative absolute returns in Q1. The best-performing market was the UK, which benefited from its exposure to the energy and materials sectors, which performed well over the quarter. Emerging market (EM) equities delivered negative absolute returns, driven primarily by the weak performance of China as lockdowns were imposed in several cities due to rising Covid-19 cases. The Central Bank of Russia closed local markets to all foreign investors, leaving managers with exposure to Russian companies that could not be unwound. Russian securities held in portfolios are now being written down as part of a fair value assessment in the absence of true market values. Our rated managers' exposure to Russia was generally low and any remaining exposure has been written down to zero. From a factor perspective, value and low volatility delivered excess returns in both DM and EM. Larger companies continued to outperform smaller companies in DM and smaller companies continued to outperform larger companies in EM.
		**Tom Wake-Walker** **Liquid Markets (Multi-Asset)**	We witnessed increased dispersion in the performance of both underlying assets and multi-asset/liquid alternative strategies in Q1, as the impact of the Russian/Ukrainian war and rising inflation expectations rippled through markets. Equity markets sold off as risk aversion took hold – negatively affecting some Diversified Growth Fund managers who maintained higher allocations. We also saw a sell-off in government bonds, driven by fears of high and rising inflation. Largely speaking, Redington-rated managers held reduced or short bond exposure, so either benefited or were relatively unaffected by this move. Trend-following strategies proved particularly profitable due to their positioning here. The other large move over the quarter was in commodities where the Russian/Ukrainian war magnified pressures on supply constraints, particularly in energies and agriculturals. Our rated managers predominantly held long exposure – through risk parity, trend-following and discretionary strategy allocations – taking advantage of these moves. Equity style premia strategies were positive, with value continuing to perform strongly.

VIEWS FROM THE ASSET CLASS SPECIALISTS

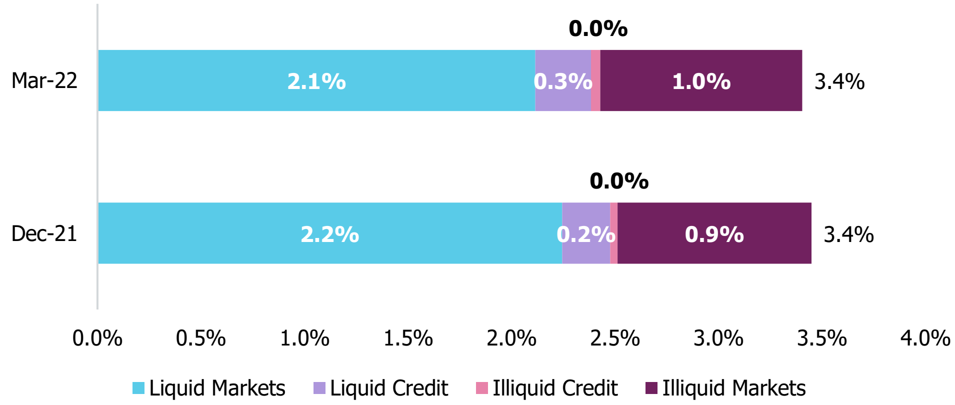
		**Chris Bikos** **Liquid & Semi-Liquid Credit**	Risk sentiment in the first quarter of 2022 was dominated by the conflict in Ukraine and central banks' hawkish stances. Credit spreads widened across the board; with rates moving higher, government securities outperformed their corporate counterparts of similar duration. Both the Federal Reserve (Fed) and the Bank of England (BoE) raised rates by 0.25% and 0.50% respectively. Yield moves differed across markets, with the US Treasury market exhibiting one of its worst sell-offs on record, but moves were less pronounced in core Europe and the UK. High yield spreads widened more than investment grade, but the higher income offered by the asset class provided a cushion. Overall, on the corporate side, credit metrics remain strong, although the flattening of the yield curve has elevated concerns about future economic growth or even a recession. Towards the end of the quarter, EM currencies and EM spreads stabilised. The differentiation in EM regions became more pronounced, with commodity exporters and Latin American countries proving the most resilient. At the asset class level, local-currency bonds were slightly more resilient than hard-currency bonds. Finally, structured credit and leveraged loans were the top-performing asset classes, benefiting from their floating-rate nature.
		**Tricia Ward** **Illiquid Credit**	Private credit markets were relatively insulated from the public market volatility of Q1 amid geopolitical uncertainty and expectations of more aggressive monetary policy. Underlying borrower fundamentals remain strong, with a renewed lender focus on borrower pricing power and shorter-duration loans. Whilst global M&A activity declined 20% vs Q1 2021, private equity buyouts rose by 18%, reinforcing demand for direct lending (source: Refinitiv). As the market matures, private loans compete directly with broadly syndicated loans in the upper-mid markets. 'Mega loans' of >$1bn are commonplace and direct lenders now represent c.5% of the large corporate debt market. Borrowers appreciate the speed, flexibility and certainty of direct loans compared with the defined ratings process in public markets. There is only a small pool of lenders of sufficient size to cater to this segment of the market, but they typically benefit from the increase in borrower quality that comes with scale. However, deals are usually covenant lite (i.e. they provide more flexibility to borrowers). We require managers to retain strong deal terms in our middle-market focus areas and evaluate opportunities arising from the changing dynamics.
		**Jaspal Phull** **Illiquid Markets**	The UK property market remains buoyant, with All-property up 3.9% throughout Q1 according to the CBRE Monthly Index. The industrial sector continues to lead the way, reporting capital growth of 3.0% in March alone, shortly followed by the retail sector reporting capital growth of 2.9%. UK property investment soared throughout Q1, in particular in the build-to-rent sector where investment grew 50% in Q1 2022, representing £1.7bn in transactions. Throughout the UK, house price growth hit its highest level in 18 years at 14.3% year on year in March. Wholesale gas prices hit a new peak over the quarter, up 26% on the previous Q4 peak, driven by the conflict in Ukraine. The European Commission proposed a new strategy, REPowerEU, to boost Europe's energy independence, phasing out the reliance on Russian gas, oil and coal imports. The plan is based on 2 pillars: diversifying gas supplies, and accelerating renewables and energy efficiency with the hope of lowering gas consumption by 30% by 2030.

YOUR ASSET ALLOCATION AND EXPOSURE

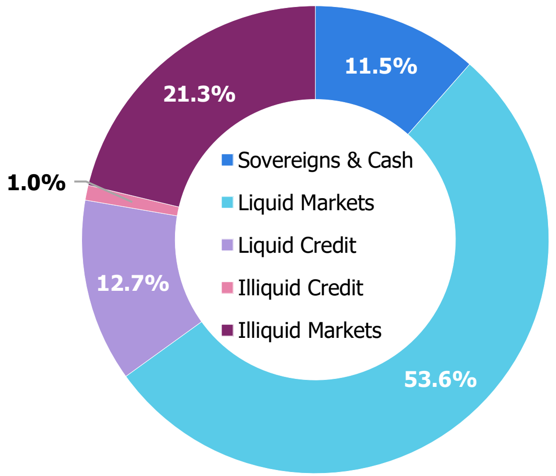
Asset Allocation Change



Expected Return Contribution Change (over gilts)



Note, asset class expected returns are in the appendix.

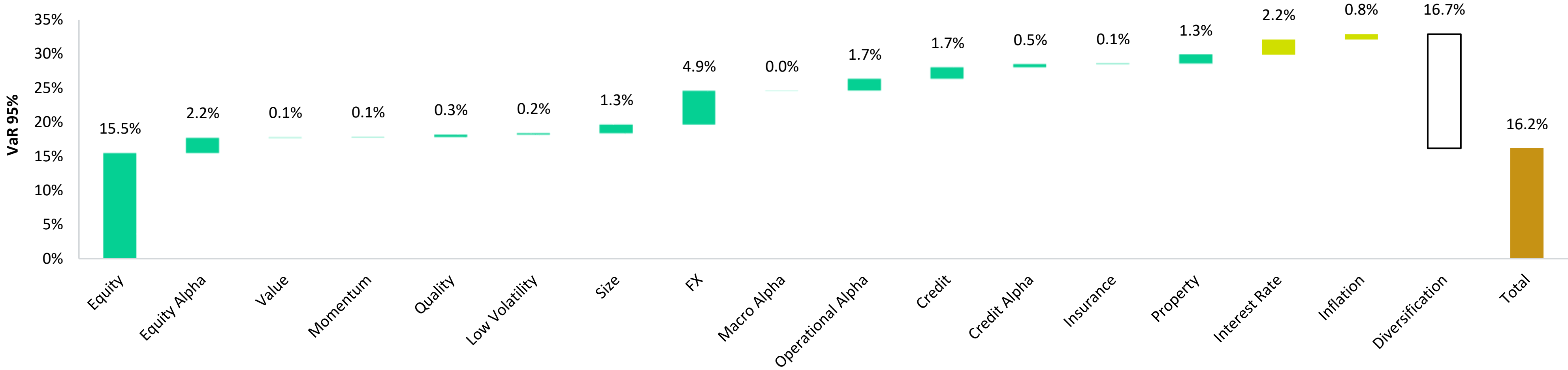


Detailed Asset Allocation

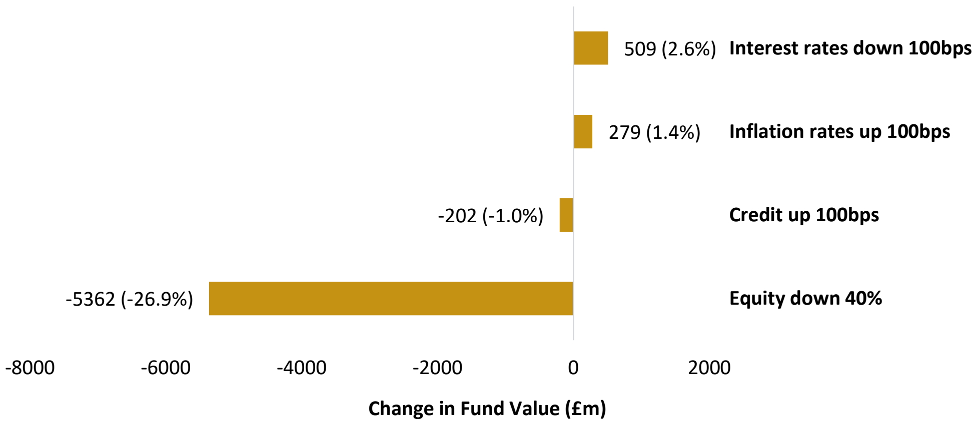
2.7% Cash
5.1% Index-Linked Gilts
1.6% Nominal Gilts
0.5% LGIM Overseas Bond Fund
1.6% US TIPS
6.1% ACS LGPS UK Equity Passive Fund
13.8% ACS LGPS Global Ex UK Passive Equity Fund
3.1% ACS LGPS Global Equity Dividend Growth Factor Fund
10.7% ACS LGPS All World Equity Climate Multi Factor Fund
6.0% LGPS Central Global Equity Multi Manager Fund
0.3% LGIM UK All Share
1.0% Global Active Futures
0.5% Equities held with Merrill Lynch
0.1% Smaller Equity Positions
2.4% Sustainable Equities - Impax
2.2% Sustainable Equities - RBC
0.6% Sustainable Equities - WHEB
2.4% Emerging Markets Equities - AGF
2.6% Emerging Markets Equities - BMO
1.7% Emerging Markets Equities - Mondrian
1.5% Aegon Short Dated Investment Grade Bond Fund
3.1% UK Corporate Bonds
1.0% LGPS Central Global Active IG Corporate Bond Fund
3.5% Multi-Class Credit
3.6% Emerging Market Debt Funds
1.0% Schroders FOCUS II / LGPS Credit Fund II
4.2% Infrastructure
7.6% Property
1.7% Opportunistic Funds
7.7% Private Equity

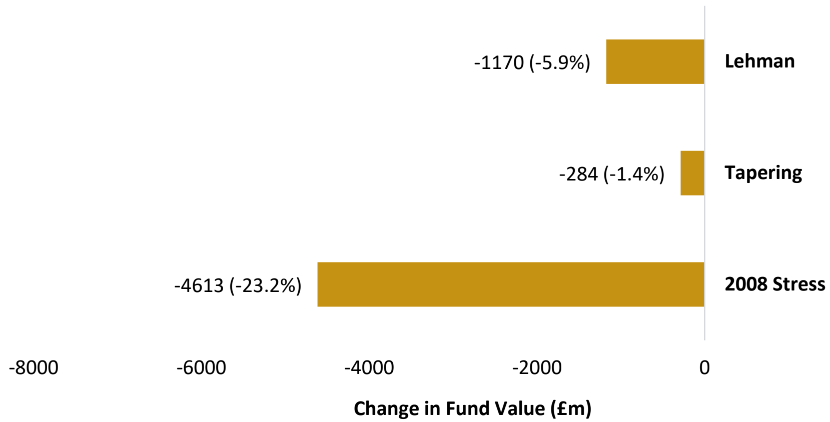
HELPING YOU UNDERSTAND YOUR RISK

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



Scenario Analysis





APPENDICES

REDINGTON’S EXPECTED RETURNS – MARCH 2022

Asset Class	Expected Return (Gilts +)	Volatility	Expected Fees (p.a.)
Equity			
Developed Market Equities	3.8% ↓	17.0% ↑	0.0%-0.1%
Sustainable Equities	4.0% ↓	15.8% ↑	0.2%-0.4%
Emerging Markets Equities	4.3% ↓	20.3% ↑	0.1%-0.2%
China A Share Equities	5.6% ↓	30.6% ↓	0.3%-0.8%
Liquid Credit			
Corporate Debt GBP – Passive	1.1% ↑	6.2% ↓	0.1%-0.2%
Corporate Debt GBP – Active	1.4% ↑	6.3% ↓	0.2%-0.3%
Emerging Market Debt – Corporates	2.4% ↑	7.9% –	0.4%-0.6%
Emerging Market Debt – Local Currency Sovereign	3.4% ↑	14.6% ↓	0.5%-0.8%
Emerging Market Debt – Hard Currency Sovereign	2.4% ↑	9.3% ↓	0.5%-0.8%
Multi-Class Credit Global	2.9% ↑	7.9% ↑	0.4%-0.7%
Illiquid Credit			
Diversified Matching Illiquids (Uninvested)	2.7% ↑	7.1% –	0.3%-0.5%
Opportunistic Illiquid Credit	4.3% ↑	12.1% ↑	1.0%-1.5% (+ performance fee)
Securitised Opportunities	3.3% ↑	6.1% ↑	0.5%-0.7%
Special Situations	5.2% ↑	17.2% ↑	1.0%-1.5% (+ performance fee)
Illiquid Markets			
Private Equity	5.4% ↓	30.2% ↓	1.0%-1.5% (+ performance fee)
Insurance-Linked Securities	4.8% –	8.4% –	1.0%-1.5%
Renewable Infrastructure (Whole Projects)	3.6% ↓	13.9% ↑	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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