

Pensions Committee

29 June 2022

Report title	Quarterly Investment Report to 31 March 2022	
Originating service	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 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 WMPF (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 Travel Limited (WMTL) and Preston Bus (PB).
- IV. The Strategic Investment Allocation Benchmark (SIAB) Policy targets 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 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 31 March 2022, the WMPF's market value was £20.2 billion (incl. WMTL and PB ABSF). Stock markets and fixed income generally fell over the quarter although performance varied by region and sector.
- 3.2 The Main Fund decreased by 1.9% over the quarter, underperforming its benchmark by 0.5%. The Fund has produced strong absolute and relative returns over the 1 year outperforming the benchmark by 0.7%. Performance has trailed the benchmark over longer time periods.

3.3 The ABSF underperformed against their benchmarks over the quarter. WMTL has also underperformed over longer time periods whereas PB has outperformed over 1, 3 and 5 years. Negative relative performance was driven by the allocations to Diversified Growth Funds and Multi-Asset Credit which lagged their 'base rate plus' target performance as equity and credit markets fell over the period.

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 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:

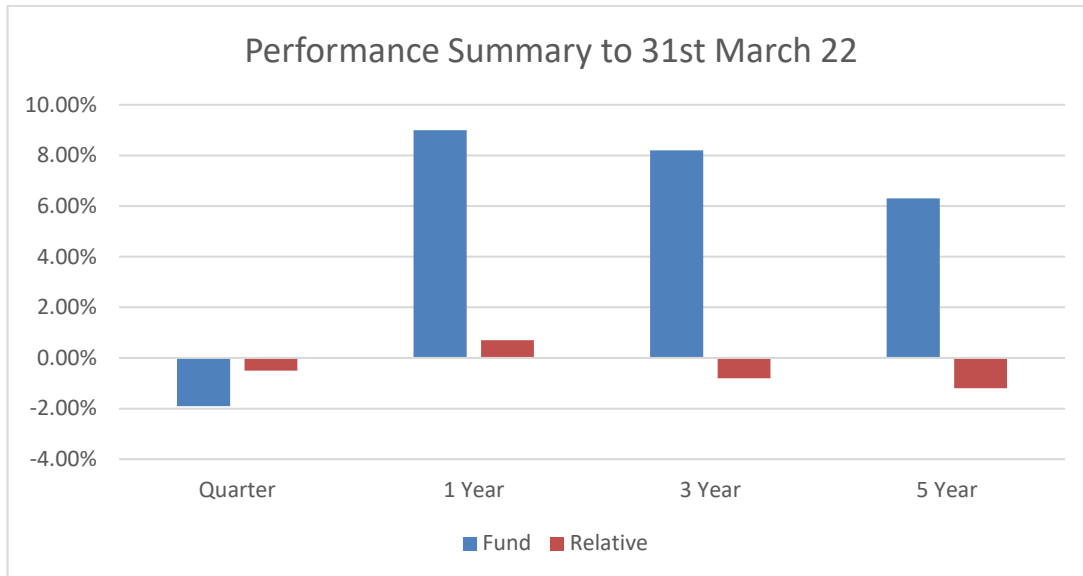
Total Return (£)	<u>Quarter</u>	<u>12 months</u>
US Equity (S&P 500)	-1.9%	21.2%
Emerging Markets (MSCI Emerging Markets)	-4.4%	-7.1%
UK Equity (FTSE All Share)	0.5%	13.0%
Gilts (GBI UK All Mats)	-7.4%	-5.3%
Corporate Bonds (BofA ML Non-Gilts)	-6.2%	-5.1%
High Yield (BofA ML Global High Yield)	-3.3%	-0.1%

4.3 Equities generally fell in the quarter, although there was slightly positive performance from UK equities. There was negative performance across bond markets, with corporate bonds outperforming government bonds.

5.0 West Midlands Pension Fund

Main Fund Performance Summary

- 5.1 The Main Fund delivered a return of -1.9% over the quarter, underperforming the benchmark return by 0.5%. 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 of March. 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.
- 5.3 Infrastructure continues to be a negative contributor to relative performance over longer time periods.
- 5.4 Over 3 years the main detractors remain infrastructure, the combined global equity portfolio and a drag from holding excess cash in rising markets.
- 5.5 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. 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 over the longer time period.

	Weight @ 31/03/22	Final ISS target	Interim Benchmark
Total Equity	54%	42%	48%
Private Equity	8%	6%	6%
Opportunistic	2%	2%	2%
TOTAL GROWTH	63%	50%	56%
Corporate Bonds	5%	4%	4%
Multi-Asset Credit/Specialist	3%	6%	6%
Emerging Market Debt	4%	5%	5%
Private Debt	1%	6%	1%
Infrastructure	4%	9%	7%
Property	8%	9%	9%
TOTAL INCOME	25%	38%	31%
Gilts	2%	2%	2%
ILG	7%	3%	5%
Low risk strategy (orphan liabilities)	1%	5%	4%
Cash	3%	2%	2%
TOTAL STABILISING (incl. low risk)	12%	12%	13%
TOTAL	100.0%	100.0%	100.0%

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, emerging market debt and private debt in particular, with equity holdings expected to be trimmed over the coming 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 negative returns during the quarter but has produced strong absolute returns over the 1 year and longer time periods to 31 March.

6.2 The Main Fund's passive equity assets are now almost exclusively managed by the investment pool company, Local Government Pension Scheme 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:

	Quarter	12 months
LGPSC UK (FTSE All Share)	0.4%	12.6%
LGPSC Global ex UK	-3.1%	8.8%
LGPSC Dividend Growth (Blended)	-2.1%	11.7%
LGPSC Climate Multi-Factor	-3.9%	14.9%

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 The LGPSC Global Active Equity Fund has outperformed the benchmark over the quarter and longer time periods. The LGPSC Global Active Equity Fund is a blended multi-manager portfolio consisting of 3 underlying portfolios.

6.5 Emerging markets performed negatively over the quarter with the Fund's Emerging Market Equity portfolio underperforming its benchmark. The portfolio has lagged its benchmark over longer time periods.

6.6 The private equity portfolio outperformed during the quarter and significantly outperformed over 1 year. The benchmark used for this asset class comprises listed equities plus an outperformance target (with a 3 month lag). Over longer time periods the portfolio has met expectations.

	Quarter	1 Year	3 year
Private Equity Portfolio	9.3%	36.5%	23.0%
FTSE All World +1% (3m lagged)	6.4%	21.0%	19.4%

Income Assets

- 6.7 The Fund's income segment trailed its respective benchmark over the quarter and over 12 months. The aggregate property portfolio outperformed the benchmark over the quarter with strong relative performance from the indirect portfolio. The property portfolio has delivered strong absolute returns over the 1 year and longer time periods.
- 6.8 The infrastructure portfolio has delivered a positive return over the course of the quarter and year but, as previously reported, the portfolio has significantly underperformed its target return (CPI +4%) over most time periods.

	Quarter		1 Year		3 Year	
	Return	Relative	Return	Relative	Return	Relative
Infrastructure Portfolio	3.3%	0.8%	7.7%	-2.8%	1.7%	-5.1%
Property Portfolio	5.6%	1.1%	18.4%	-1.1%	7.9%	-0.1%

- 6.9 The Fund's fixed interest holdings produced negative performance as a result of the increasing interest rate environment. Within the Fund's fixed interest holdings, corporate bonds have outperformed the benchmark over the quarter and longer time periods. The emerging market debt holdings underperformed their benchmark over the quarter, which has impacted longer term performance. Whilst the Fund's multi asset credit holdings managed to provide some protection from broader credit markets, they have underperformed over the quarter and longer time periods.

	Quarter		1 Year		3 Year	
	Return	Relative	Return	Relative	Return	Relative
Corporate Bonds	-5.0%	1.2%	-3.6%	1.6%	2.9%	1.9%
Multi Asset Credit	-3.0%	-1.0%	-0.3%	-0.5%	1.8%	-1.2%
Emerging Market Debt	-7.5%	-1.8%	-4.4%	-0.8%	0.6%	1.5%

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 negative returns for the quarter as yields on sovereign debt rose (meaning prices fell).
- 6.11 Over the quarter, 1 and 3 year timeframes the stabilising portfolio has outperformed its benchmark.

Currency

6.12 The Fund currently only hedges a small proportion of its foreign currency exposure (25% for EUR equities). The hedge has had a small negative impact on performance over the quarter but has had a positive impact over the 1 and 3 year period. 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):

Asset Class	Value @31/03/22	Target %	Current %
Total Equities	£ 93,613,009		32%
UK Equities	£ 6,786,960		2%
North America Equity Index	£ 37,349,295		13%
Europe (ex UK) Equity Index	£ 22,112,210		8%
Japan Equity Index	£ 7,521,575		3%
Asia Pac exJap Dev Equ Ind	£ 8,114,696		3%
World Emerging Markets Equ Ind	£ 11,728,274		4%
Newton Real Return	£ 35,910,260		12%
Baillie Gifford DGF	£ 37,815,066		13%
Total Equities & DGF	£ 167,338,336	16%	58%
Corporate Bonds	£ 9,719,006		3%
Multi Asset Credit	£ 52,261,146		18%
Private Debt	£ 1,451,627		1%
LDI	£ 56,085,945		19%
Total Credit & LDI	£ 119,517,724	84%	41%
Cash	£ 2,146,775	0%	1%
Total	£ 289,002,834.71		100%

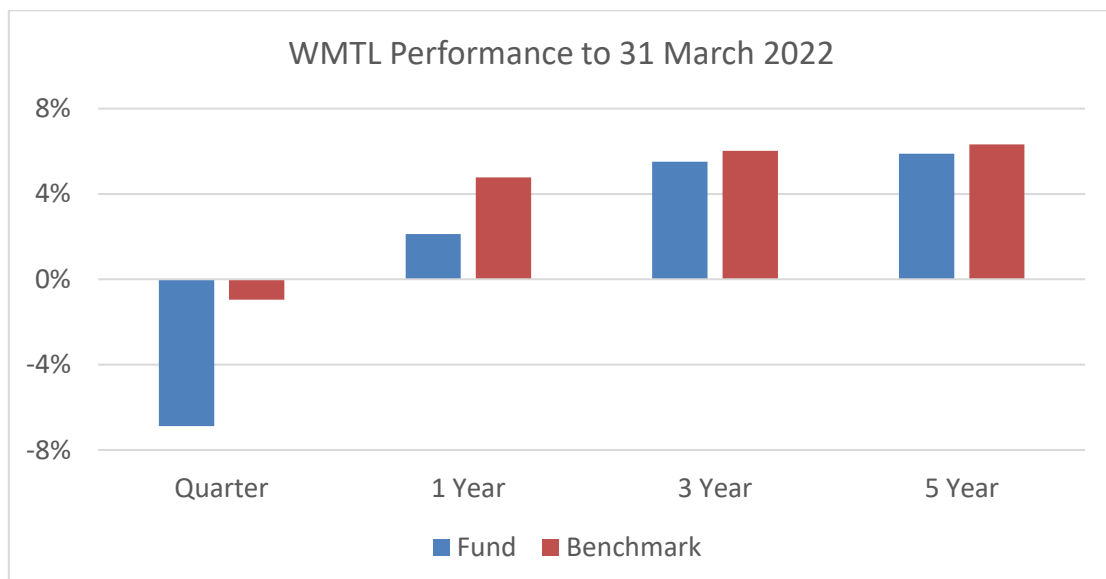
The allocation to private debt is expected to increase over time. Commitments have been made in this area, however, given the private nature of these assets these commitments will draw down over a period of time, moving the allocation towards the target.

PB asset allocation:

Asset Class	Value @31/03/22	Target %	Current %
Total Equities	£ 2,825,125	15%	14%
UK Equities	£ 237,118		1%
North America Equity Index	£ 1,223,551		6%
Europe (ex UK) Equity Index	£ 390,268		2%
Japan Equity Index	£ 314,489		2%
Asia Pac exJap Dev Equ Ind	£ 228,810		1%
World Emerging Markets Equ Ind	£ 430,889		2%
Total Fixed Interest, LDI & cash	£ 16,500,042	85%	84%
Corporate Bonds	£ 5,004,094		26%
Multi Asset Credit	£ 5,720,162		29%
LDI	£ 5,775,785		29%
Cash	£ 291,512		1%
Total	£ 19,616,679.34	100%	100%

WMTL Performance

7.2 The Fund significantly underperformed over the quarter and 1 year. Performance is more in line with the benchmark over the 3 and 5 year periods. Relative performance is driven by the multi-asset credit and diversified growth fund holdings which underperformed their 'base rate plus' target performance as equity and credit markets fell over the period.



Fixed Income

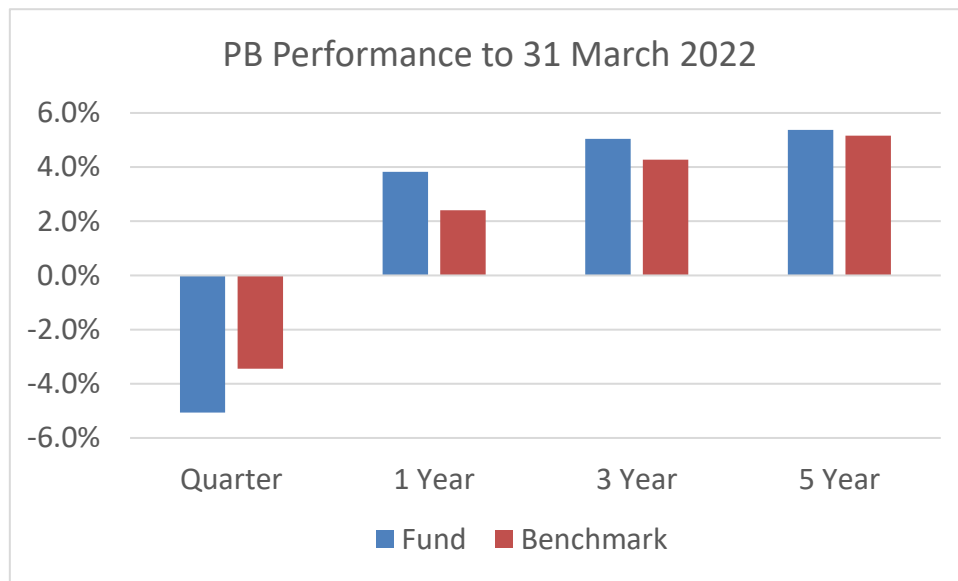
- 7.3 Alongside the multi-asset credit holding in the bond portfolio, there are passive index linked gilts and actively managed corporate bonds. The corporate bond mandate has outperformed its benchmark over the quarter and 1 year whilst the multi-asset credit has underperformed over the same time periods.

Diversified Growth Funds

- 7.4 Both Diversified Growth Fund holdings delivered negative absolute and relative performance over the quarter. Over the 1 year the total Diversified Growth portfolio underperformed the benchmark.

PB Performance Summary

- 7.5 PB performance is summarised below. The Fund underperformed over the quarter but has outperformed over the 1, 3 and 5 year periods. Underperformance over the quarter was driven by the Multi-Asset Credit allocation.



- 7.6 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 LGPSC Ltd 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.

9.0 Investment Strategy Statement (Annual Review)

- 9.1 In defining the implementation of the Fund's Investment Strategy the ISS sets out the SIAB including the permitted ranges for each asset type.
- 9.2 A full in-depth review of the Fund's ISS is completed every 3 years in conjunction with the triennial funding and valuation process. In addition, interim annual reviews are also completed to complement this cycle.
- 9.3 The Fund completed a full review of its Investment Strategy over 2019/20 resulting in significant changes to the Funds SIAB being approved in March 2020. Implementation of these strategy changes is underway as communicated separately to this Committee. As the Fund is significantly increasing its allocation to private markets it will take time until the Funds positioning closely matches the policy targets stated in the ISS.
- 9.4 The interim review referenced last quarter confirms these strategy changes remain appropriate for the Fund to meet its longer-term objectives. The Fund's Investment Consultant, Redington, who advised the Fund during the 2019/20 review has provided Fund Officers with a confirmation statement confirming their ongoing support for the strategy changes being implemented.
- 9.5 Whilst the longer-term strategy remains the focus and is unchanged, Fund Officers are alive to the significant changes to the investment and economic landscape that have occurred since 2020. Given this backdrop and the Fund's overarching goals, including with regards to sustainability objectives, it was agreed by the Pensions Committee last quarter that the increase in allocation to emerging markets equities, which was agreed within the Liquid Growth portion of the SIAB, is put on hold for the time being pending a full review of the Fund's existing and potential holdings in this area. This area of the portfolio is to be reviewed in more detail in line with the broader strategy review as part of the triennial valuation.

10.0 Financial Implications

- 10.1 The financial implications are set out throughout the report.

11.0 Legal Implications

- 11.1 This report contains no direct legal implications.

12.0 Equalities Implications

- 12.1 This report contains no direct equal opportunities implications.

13.0 Other Implications

13.1 There are no other implications.

14.0 Schedule of Background Papers

14.1 There are no background papers.

15.0 Schedule of Appendices

15.1 Appendix A – Redington Economic and Market Update