Minutes of IMWP Meeting held on 5th June 2024

Attendees

Name	Initials	Organisation
Councillor Stephen Bennett (Chair)	SB	WBC
Councillor Helen Cameron	HC	WBC
Councillor Ann Ainsworth	AA	WBC
Councillor Brenda Hall	BH	WBC
Councillor George Davies	GD	WBC
Councillor Brian Kenny	BK	WBC
Councillor Pat Cleary	PC	WBC
Jill Davys	JD	Redington
Charlie Sheridan	CS	Redington
Paul Watson	PWa	Independent Advisor
Rohan Worrall	RW	Independent Advisor
Peter Wallach	PW	MPF
Owen Thorne	OT	MPF
Alex Abela-Stevenson	AAS	MPF
Emma Littler	EL	MPF
Daniel Proudfoot	DP	MPF
Adil Manzoor	AM	MPF
Neil Gill	NG	MPF
Roksana Klapkowska	RK	MPF
Allister Goulding	AG	MPF
Dragos Serbanica	DS	MPF

1. **Apologies**

Roger Bannister
Councillor Martin Bond

2. **Introductory Comments**

Peter Wallach introduced the new Chair – Stephen Bennet.

PW proposed to defer the June performance update to September as MPF is in a transitional phase but highlighted that the Fund value increased over 12 months from GBP 10.4 billion in March 2023 to GBP 10.8 billion in March 2024.

3. Market Commentary – Rohan Worrall (RW)

In Q1 2024, the Bond market continues to disappoint, reflecting the disappointment concerning the likelihood of interest rate cuts.

Core inflation excludes more volatile components, such as energy, and remains relatively high. It’s a measure of domestic inflation rather than global, so it's of special interest to central banks. The inflation is coming down but slower than expected.

Economies are growing and likely to keep growing, recession is rather unlikely at the moment. China is growing slower than historically; therefore global growth is also slower.

Equities had a good quarter and year so far with growth stocks doing better than value.

Bond yields have risen, so the bond prices have fallen. Corporate spreads are not particularly attractive, premium over government bonds is steadily declining, making corporate bonds look relatively expensive.

Sterling has done relatively well over 3 months and last year against the USD. GBP also appreciated much against the yen, but that’s rather caused by the yen's weakness.

Commodities are doing very well, gold and silver are up, as are oil and copper, indicating an increase in economic activity.

Manufacturing activity is picking up, however, inflation remains sticky, especially domestic inflation, and central banks are still trying to get it down. The outlook is that inflation will be higher over the next 10 years than it was in the past 10 years and this should be considered in the portfolio management.

US and UK elections are upcoming, and conflicts in Ukraine and Gaza persist. However, generally, the outlook is stable for the time being, with the interest rates expected to gradually fall.

Q&A

In response to a question as to why the PMI for the Euro is so weak, RW replied that PMI has been weak in Germany in particular, and this downtrend over several years in German manufacturing is suggesting that Europe is not as competitive as it used to be. Services are strong but manufacturing is not as strong as it was 5-10 years ago.

Regarding yen weakness, RW explained that since the financial crisis, Japan has been issuing debt, and was very reluctant to raise interest rates as the debt would be more expensive to service. This negatively affects the yen.

It was noted that 5-year gilts are not included in the report and asked whether they are not material in this context. RW replied that long-term gilts are a better proxy for long-term liabilities than short-term gilts, so there is more focus on 10 – 15-year gilts.

With regard to how uncertainty around the US election affects the market, RW highlighted that there is no precise answer until the result, but in terms of the impact on the market, there shouldn't be a huge difference as both candidates are fiscally loose.

4. MPF Monitoring Report – Peter Wallach (PW)

PW noted that the monitoring report reveals a number of mandates flagged as red, so, as discussed last time, additional narrative is provided to support the RAG report. The fund is looking to terminate and retender mandates of concern over the next 6-12 months in accordance with Redington's presentation and discussions about the future shape of the portfolio.

Q&A

An update on the internal UK equity portfolio was requested as beneficial for the new members of Committee.

Allister Goulding (AG) summarised that since the end of March, a number of portfolio constituents have outperformed, especially silver. Strong demand for silver is expected in the long term as it's essential for the energy transition, especially photovoltaics and electric vehicles. Precious metals equities are also well-positioned. Historically precious metals equities have been significantly undervalued and have not fully participated in the recovery. There is some exposure to technology as well. There have been companies that previously underperformed but have improved now, and their ratings have improved as well. Companies can be subject to fashion and can be undervalued because of that.

Attention was drawn to a mistake in fixed income on page 11. RW agreed there was a typo.

It was questioned why the fund is not shifting away from the mandates that have been underperforming for 3 years.

PW explained that some actions had been held in abeyance pending the imminent finalisation of the interim asset allocation and outlined the internal team's intended actions once this had been concluded. Positive market sentiment towards equities also was another consideration as, despite some mandates underperforming, equities overall are doing considerably better than fixed income which is where much of the capital will be reallocated. PW also explained that if a mandate underperforms over the preceding 12 months, it affects the 3- year number as well so underperformance may not be as protracted as the numbers suggest. 3 – 5 years is a reasonable period of time to assess a mandate's performance.

AG was asked why he prefers to take a position in a particular company rather than in an ETF for a particular sector. AG explained the fund has significant holdings in physical silver and gold, providing a different volatility and risk exposure compared to equity. He expressed a preference for picking the best assets available, rather than investing in generic ETFs.

It was asked whether the Fund is asking questions about active performance doing worse than the tracker. PW confirmed it is a part of the monitoring process and explained that managers have different tilts, with performance depending on the market conditions.

5. Strategy Update and Investment Workplan– Charlie Sheridan (CS)

CS presented what has been covered in the previous meetings and previously set long-term targets. The Fund's SAA has been approved and is moving into the implementation phase. The fixed income change programme is due to come to the IMWP in September.

The fund increased its funding level over the 6-month period to the end of March 2024 up 5.7% (to 107%). The drivers of that were the performance of the overall market and discounting liabilities using a higher rate. The expected return is 5.5% above inflation.

The liquidity stress test indicates a positive change over the quarter. A metric used for the risk was VAR – essentially the minimum amount the fund is expected to lose that Redington supplements with some scenario analysis. There was a small increase there, but Redington is comfortable that it stems from the market performance.

There were no changes to PRMF objectives from the previous quarter.

CS mentioned there were minor changes to SAA: risk reduction from improved diversification, reduction in equities, focus on increased cash flow generation, and looking to lower exposure to climate risk.

CS outlined the 2024/25 workplan on page 34 and the fixed income change programme, explaining the characteristics of fixed income investments and common terms related to them.

CS moved on to presenting the survey responses. There is a strong support for an increase in yielding investments and to achieve portfolio emission reduction through fixed income, looking at global fixed income and diversified exposure across the credit spectrum.

Q&A

Paul Watson (PWa) highlighted that equity is the key risk driver.

Clarification was sought on the metrics omitted from the PRMF. JD replied that the Net Zero target setting is going to the July Committee meeting and will be updated thereafter.

A question was raised as to whether the Fund will set a target proportion of investments in the Merseyside region. PW replied it is ultimately up to the Members to decide but advised against it as it may encourage sub-optimal decision-making. MPF is actively seeking opportunities in the region and proceeds with those offering a commercial return. Regarding levelling up, there would be a requirement for pension funds to have an objective of 5%, but MPF already exceeds it as of now. Currently, the Fund has around £100 million invested in Merseyside. Setting a target could lead to an increase in counterparty and concentration risk in the case of an economic downturn in the region.

PWa: asked whether the funded position changes the mentality to protect surplus rather than driving for growth. PW expressed a preference to move the MPF to a more defensive position but it needs to be balanced with sufficient growth opportunities in order to preserve affordability for the employers. SAA is key to the fund in terms of that.

Redington was asked to clarify the difference between the IMWP and the new RIWP in the interests of the new members. JD explained that an increasing amount of the IMWP‘s time was spent on ESG issues rather than the key investment issues. Therefore, a dedicated working party has been established for Responsible Investment, especially since the time spent on ESG is not going to decrease in the near term due to the Stewardship Code and discussions around defence companies. PW clarified there are three working parties: IMWP – scrutinising investment matters in more detail, Governance and Risk Working Party focused on the administration side, and RIWP dealing with Responsible Investment issues.

6. Public Equities Change Programme – Jill Davys (JD)

JD introduced the programme and explained that Redington takes a pragmatic approach, recognising the current position of MPF and the time required to implement the changes. The main outcome is to reduce the overall exposure to equities, reducing the risk within the Fund while maintaining the level of returns. The goal is to improve the cash flow position thanks to income and inflation linkage.

Currently, the allocations are very regional, and Redington is recommending a shift to a global focus so that the managers can determine the best markets at the current times with less reliance on the home market.

Analysing views of the stakeholders there is a focus on ESG, Net Zero, and incorporating active management. Redington is also considering where to reduce the governance burden and cost so looking to reduce the number of mandates and manage internally where possible.

JD moved on to the portfolio-construction approach and gave a brief overview of the key building blocks. Redington propose a range of styles to complement each other, without concentration in any particular style. Making sure there is an appropriate exposure to EM with stronger economic growth, avoiding home bias, and where possible, recognising where adding value through active management is possible and where passive management would be more suitable.

The model portfolio looks at a more style-balanced and more global approach as there is currently heavy exposure to the UK.

The key changes in the medium term are moving from an almost fully active approach to 50% passive, shifting from a value bias to a more balanced approach, improving the ESG and sustainability of the portfolios, and more global exposure.

Looking at the transitional portfolio in more detail it reflects the initial moves to get closer to the ultimate SAA. Key changes here are reducing the UK exposure and some of the European exposure to increase global mandates exposures. Looking to increase exposure to higher growth Asian markets.

Medium-term Target Portfolio increases focus on global and style blended, lowering home bias but maintaining it. Specific allocation to China is considered but doesn't have to be pursued further, especially in terms of the ESG criteria.

Q&A

A question was asked about how many mandates are too many? JD clarified there is no specific number but commented that having a number of small mandates is inefficient as monitoring them is resource intensive.

It was noted that in previous meetings it had been mentioned that China is not performing as well as in the past and whether moving to Chinese equities is still valid in such a case. JD explained that over the long term, China is still expected to outperform Developed Markets. PW added that, strategically, MPF had the objective of investing in China but, considering the tactical aspect, now may not be a suitable time due to the slowdown in economic growth, ESG considerations, and geopolitical perspective.

An explanation of the basis of the sliders on page 71 was sought. JD explained it was a blended approach, considering where the Fund is today in terms of growth assets and value assets, as well as a passive and active approach.

7. **Responsible Investment Update – Owen Thorne (OT)**

RIWP minutes noted.

We work with PIRC and Northern Pool specifically on executing our voting policy and stewardship engagement. LAPFF is our collective partnership with other

LGPS funds across the UK that work together to carry out collaborative engagement.

8. PIRC/LAPFF Report – Owen Thorne (OT)

OT explained what different reports refer to and that each of them highlights some areas of engagement.

OT elaborated that through engagement, shareholders can act on gaps in company statements and ensure that resolutions at AGMs progress in the right direction. Especially in the case of Starbucks.

OT commented on climate. Particularly, the LAPFF report has taken up engagement policies, highlighting carbon-intensive projects and activities. HSBC and Barclays are scrutinised for their financing of emissions as shareholders are becoming aware of the risks around potentially stranded assets.

OT gave an update on engagement around human rights risks, highlighting that the progress is slow but we're starting to see increased responsiveness.

Q&A

It was pointed out there is not a lot in the report and there was a request to see the responses that LAPFF received that would be relevant for the Pensions Committee. OT clarified that LAPFF is helping to find a larger network of investors focusing on the issue of human rights in conflict areas, increasing pressure for responsiveness.

It was asked what happens to companies that are responding but not providing the desired response and how to ensure that responsiveness is not discouraged. OT explained that engagement is about creating the space for discussion, and quasi-responses affect shareholders' view of effective management.

https://lapfforum.org/engagements/q1-2024-quarterly-engagement-report/
https://northernlgps.org/assets/pdf/stewardq1_2024.pdf

9. Minutes of IMWP 12th March 2024

Noted, no amendments.