London Borough of Merton Pension Fund

Q4 2022 Investment Monitoring Report

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Executive Summary

The Fund's assets returned 3.5% during the final quarter of 2022. To provide context, we have assessed total returns against a composite benchmark - a weighted average of the underlying manager benchmarks. Against this comparator, the Fund was behind the benchmark by -1.1% (top left chart). We have also shown performance against the Fund's actuarial target (top right chart), on the 3-year measure the Fund is behind with relative returns of -1.5% p.a.

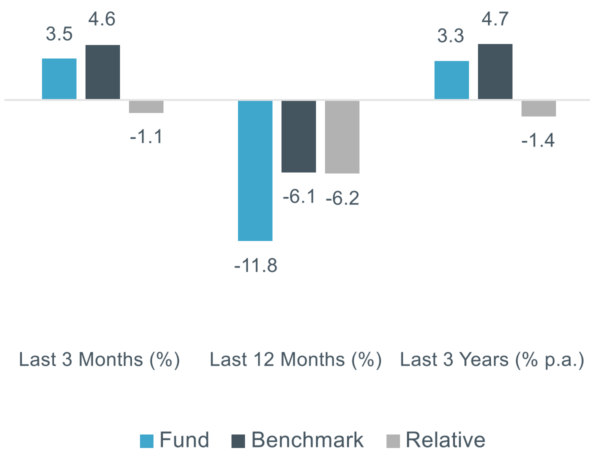
Overall, the Fund's assets decreased by £1.2m from £851.1m to £849.9m.

The fourth quarter brought resilient data on economic activity, a peak in headline inflation, reduced risk of European energy rationing and China's economic re-opening. This eased concerns about the downside risks to global growth this year. Global equities rallied strongly from their October low, credit spreads tightened significantly, and the dollar fell sharply from its peak early in the fourth quarter.

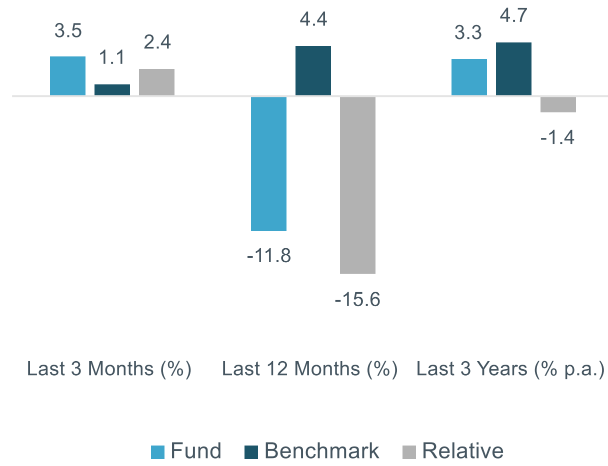
From an asset class perspective:

- The majority of equity mandate also contributed positively to returns.
- The diversified growth funds also contributed positive returns
- The UK property funds detracted
- The Risk Management Framework contributed positively as gilt yields fell and dollar weakened.

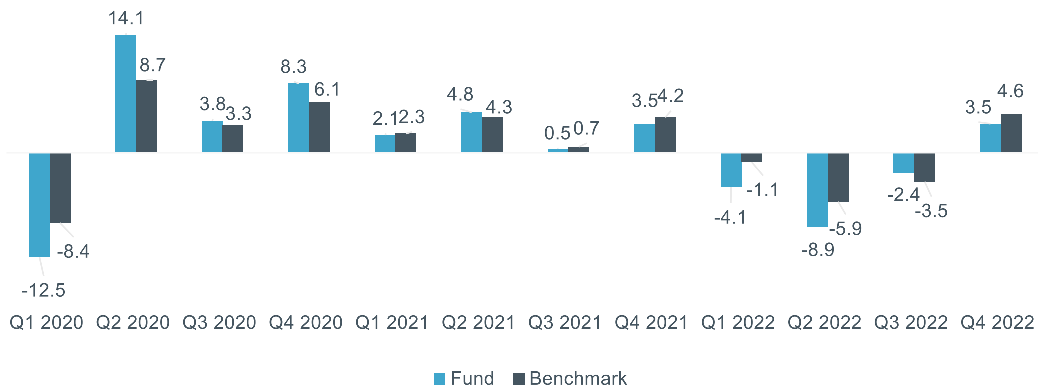
Fund performance vs benchmark/target



Fund performance vs actuarial target



Relative quarterly performance vs benchmark/target



Following the 2019 strategy review the agreed long-term target allocation for the Fund is as follows:

Global equities: 30.0%
Emerging market equities: 10.0%
Diversified growth fund: 8.0%
Property: 5.0%
Private credit: 6.5%
Infrastructure: 11.5%
Social Impact: 5.0%
Multi-asset credit: 9.0%
Risk management framework: 15.0%

In time the Fund will transition towards this target allocation. As it does, the benchmark (as agreed with Officers) shown in the table and used in the benchmark performance calculation on the next will be gradually updated to reflect progress to date.

We are currently in the process of reviewing the investment strategy following completion of the triennial valuation.

Commitments to social impact infrastructure and private credit investments continued to be drawn down over time.

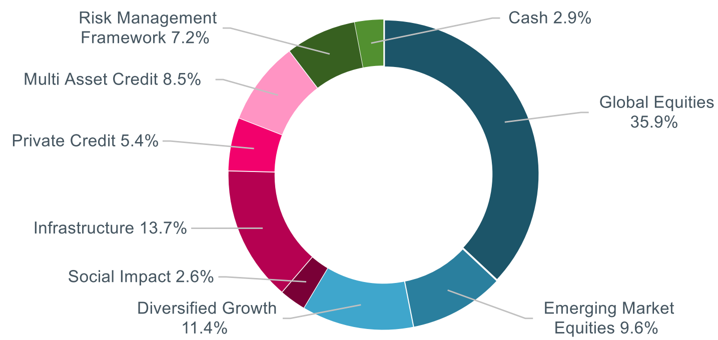
The Fund disinvested £14,900,000 from LCIV Baillie Gifford Diversified Growth Fund during this quarter. Proceeds were used to help fund commitments with Permira and Henley.

Asset Allocation

Mandate	Valuation (£m) Q3 22	Valuation (£m) Q4 22	Actual Proportion	Benchmark	Relative
UBS Alternative Beta	45.1	47.6	5.6%	5.0%	0.6%
LCIV RBC Sustainable Equity Fund	84.5	84.1	9.9%	10.0%	-0.1%
LCIV Baillie Gifford Global Alpha Growth Paris Aligned Fund	70.4	71.5	8.4%	10.0%	-1.6%
BlackRock World Low Carbon Equity Tracker	101.1	101.6	12.0%	10.0%	2.0%
Global Equities	**301.1**	**304.7**	**35.9%**	**35.0%**	**0.9%**
UBS GEM HALO	47.5	47.6	5.6%	5.0%	0.6%
LCIV JP Morgan Emerging Market Equity Fund	33.3	34.1	4.0%	5.0%	-1.0%
Emerging Market Equities	**80.8**	**81.6**	**9.6%**	**10.0%**	**-0.4%**
LCIV Ruffer Absolute Return Fund	59.4	62.3	7.3%	5.0%	2.3%
LCIV Baillie Gifford Diversified Growth Fund	48.5	34.0	4.0%	5.0%	-1.0%
Diversified Growth	**107.9**	**96.4**	**11.4%**	**10.0%**	**1.4%**
UBS Triton Property Fund	19.8	16.8	2.0%	2.5%	-0.5%
BlackRock UK Property Fund	8.7	7.4	0.9%	2.5%	-1.6%
Property	**28.5**	**24.2**	**2.9%**	**5.0%**	**-2.1%**
Henley Secure Income Property Fund II	13.3	22.4	2.6%	1.0%	1.6%
Social Impact	**13.3**	**22.4**	**2.6%**	**1.0%**	**1.6%**
MIRA Infrastructure Global Solutions II L.P Fund	18.9	20.4	2.4%	2.0%	0.4%
Quinbrook Low Carbon Power LP Fund	16.1	16.5	1.9%	1.5%	0.4%
Quinbrook Net Zero Power Fund	33.1	14.3	1.7%	3.0%	-1.3%
JP Morgan Infrastructure Fund	64.9	64.9	7.6%	5.0%	2.6%
Infrastructure	**133.0**	**116.2**	**13.7%**	**11.5%**	**2.2%**
Permira Credit Solutions IV Fund	23.5	23.7	2.8%	4.5%	-1.7%
Churchill Middle Market Senior Loan II Fund	20.0	21.8	2.6%	3.0%	-0.4%
Private Credit	**43.5**	**45.5**	**5.4%**	**7.5%**	**-2.1%**
Allspring RMF Fund	49.9	60.7	7.2%	10.0%	-2.8%
Risk Management Framework	**49.9**	**60.7**	**7.2%**	**10.0%**	**-2.8%**
LCIV CQS / PIMCO MAC Fund	68.9	71.8	8.5%	10.0%	-1.5%
Multi Asset Credit	**68.9**	**71.8**	**8.5%**	**10.0%**	**-1.5%**
Cash	24.1	24.7	2.9%	0.0%	2.9%
Total Fund	**851.1**	**848.2**	**100.0%**	**100.0%**	

At the time of writing, latest quarterly information in respect of mandates held with MIRA, Quinbrook, Permira and Churchill are unavailable. We have lagged reporting by 3 months, therefore the valuations shown are as at Q3 2022 respectively. The FX rate used is lagged and at each of these dates also.

Asset class exposures



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Source: Investment Managers

During the last quarter of 2022, the Fund delivered an absolute return of 3.5%, underperforming the composite benchmark with relative returns of -1.1%.

Over the longer time periods shown, the Fund has recorded positive absolute returns for the last 3 years and since inception, however relative return are more varied at -1.4% p.a. and 0.8% p.a. respectively.

All equities with the exception off LCIV RBC Sustainable Equity fund contributed positively to the overall absolute performance.

Of the two diversified growth funds, the LCIV Ruffer fund was the stand out contributor during the quarter.

The performances within real assets were more varied. Henley, Quinbrook LCP and JP Morgan Infrastructure brought positive returns to the portfolio, while UBS Triton, BlackRock UK Property, and MIRA detracted from overall returns.

The Risk Management Framework was the biggest contributor to performance. Rising yields coupled with a strengthening pound-sterling relative to dollar contributed positively.

At time of writing, MIRA, Quinbrook LCP & NZPF, Permira and Churchill reporting information was unavailable. For performance reporting purposes we have lagged performance and valuations shown within our report by 3 months. We expect, given the illiquid nature of these mandates, this will be a regular occurrence.

Manager performance

Mandate	Last 3 Months (%)			Last 12 Months (%)			Last 3 Years (% p.a.)			Since Inception (% p.a.)		
	Fund	B'mark	Relative	Fund	B'mark	Relative	Fund	B'mark	Relative	Fund	B'mark	Relative
UBS Alternative Beta	5.5	5.4	**0.0**	-0.4	-0.4	**0.0**	6.4	6.4	**0.0**	1.3	1.3	**0.0**
LCIV RBC Sustainable Equity Fund	-0.5	2.4	**-2.8**	-15.6	-6.0	**-10.3**	7.9	9.3	**-1.3**	8.6	7.7	**0.8**
LCIV Baillie Gifford Global Alpha Growth Paris Aligned Fund	1.2	1.6	**-0.4**	-	-	**-**	-	-	**-**	-7.6	-4.1	**-3.6**
BlackRock World Low Carbon Equity Tracker	0.5	0.4	**0.1**	-9.4	-9.9	**0.5**	8.2	8.0	**0.2**	11.5	11.2	**0.2**
Global Equities												
UBS GEM HALO	0.2	1.8	**-1.6**	-15.3	-10.0	**-5.9**	-2.4	0.4	**-2.8**	2.9	3.4	**-0.5**
LCIV JP Morgan Emerging Market Equity Fund	2.3	2.4	**-0.2**	-9.5	-7.8	**-1.9**	3.0	1.5	**1.4**	2.9	1.5	**1.4**
Emerging Market Equities												
LCIV Ruffer Absolute Return Fund	4.9	1.4	**3.4**	6.9	4.4	**2.4**	-	-	**-**	7.4	3.8	**3.5**
LCIV Baillie Gifford Diversified Growth Fund	1.5	1.6	**-0.0**	-15.8	5.1	**-20.0**	-2.1	4.2	**-6.0**	0.2	3.8	**-3.5**
Diversified Growth												
UBS Triton Property Fund	-15.2	-14.1	**-1.3**	-9.0	-9.5	**0.6**	2.4	2.2	**0.2**	0.8	0.7	**0.1**
BlackRock UK Property Fund	-14.2	-14.1	**-0.1**	-10.0	-9.5	**-0.6**	1.2	2.2	**-0.9**	1.1	1.4	**-0.3**
Property												
Henley Secure Income Property Fund II	3.9	1.5	**2.4**	-	-	**-**	-	-	**-**	1.6	3.0	**-1.4**
Social Impact												
MIRA Infrastructure Global Solutions II L.P Fund	-2.3	1.8	**-4.0**	4.3	7.4	**-2.9**	8.1	7.4	**0.6**	4.4	5.7	**-1.2**
Quinbrook Low Carbon Power LP Fund	1.5	1.8	**-0.3**	16.8	7.4	**8.7**	5.8	7.4	**-1.5**	6.7	6.6	**0.0**
Quinbrook Net Zero Power Fund	-	-	**-**	-	-	**-**	-	-	**-**	-3.0	6.0	**-8.4**
JP Morgan Infrastructure Fund	8.0	2.5	**5.4**	14.6	10.4	**3.8**	8.2	10.4	**-2.0**	7.6	9.6	**-1.8**
Infrastructure												
Permira Credit Solutions IV Fund	0.7	1.7	**-1.0**	2.3	7.0	**-4.4**	-	-	**-**	4.0	5.3	**-1.3**
Churchill Middle Market Senior Loan II Fund	1.3	1.7	**-0.4**	4.1	7.0	**-2.7**	5.6	6.7	**-1.1**	3.7	6.0	**-2.2**
Private Credit												
Allspring RMF Fund	36.6	36.6	**0.0**	-42.8	-42.8	**0.0**	-	-	**-**	-9.0	-9.0	**0.0**
Risk Management Framework												
LCIV CQS / PIMCO MAC Fund	4.1	1.8	**2.3**	-8.0	5.9	**-13.1**	-0.1	5.0	**-4.8**	1.2	4.6	**-3.2**
Multi Asset Credit												
Cash	-	-	**-**	-	-	**-**	-	-	**-**	-	-	**-**
Total Fund	3.5	4.6	**-1.1**	-11.8	-6.1	**-6.2**	3.3	4.7	**-1.4**	5.7	4.8	**0.8**

Note: Q4 2022 performance figures for MIRA, Quinbrook LCP & NZPF, Permira and Churchill are lagged by 3-months due to lack of manager information at the time of writing (see comment on left). As such, the performance shown is reflective of Q3 2022.

Source: Fund performance provided by Investment Managers and is net of fees.
Benchmark performance provided by Investment Managers and DataStream

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Q4 growth outturns surprised to the upside as US labour and consumer demand remains resilient while the economic impact of potential European gas shortages abated more recently. Despite more recent upwards revisions for some economies, global growth forecasts for 2023 fell over the quarter, as high inflation and tighter monetary policy weigh on the outlook.

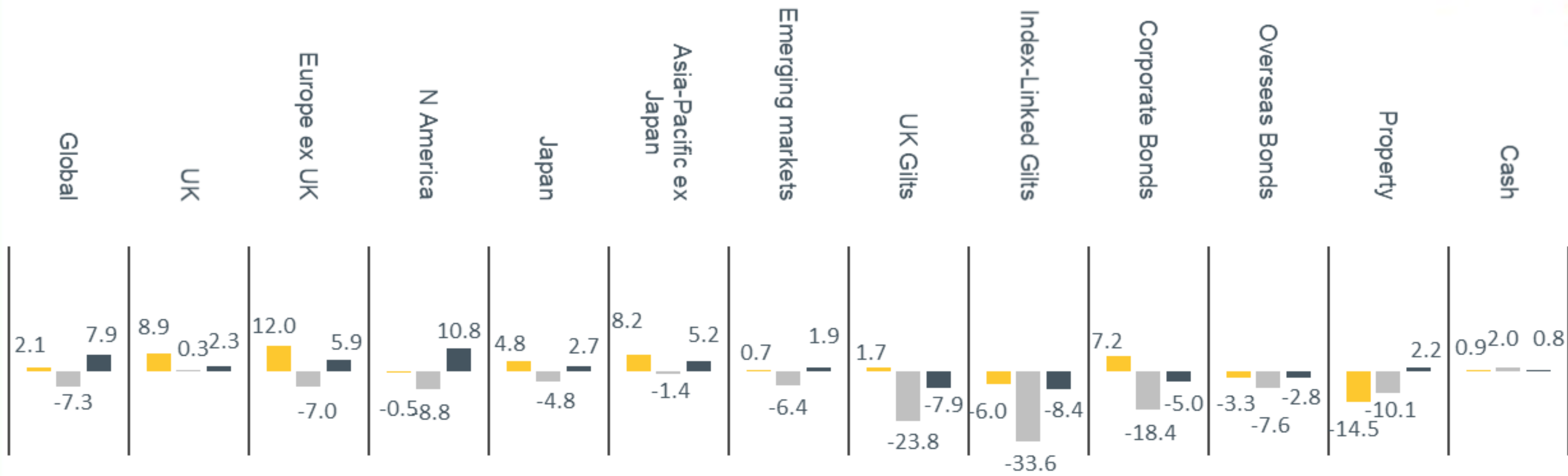
Downside CPI surprises, support the idea that inflation peaked in Europe and the US. Year-on-year headline CPI inflation fell to 7.1%, 10.7%, and 10.1% in the US, UK, and Eurozone, respectively, in November.

After a round of 0.75% p.a. interest rate rises, major central banks shifted down to smaller 0.5% p.a. increases in December. The 1.25% p.a. of rate rises delivered by each of the major central banks in Q4 takes policy rates in the US, UK, and Eurozone to 4.5% p.a., 3.5% p.a., and 2.0% p.a., respectively.

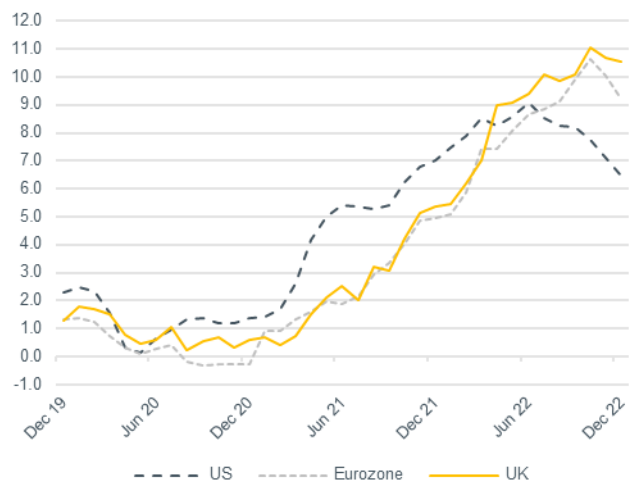
UK 10-year yields ended the period at 3.7% p.a., 0.5% p.a. below end-September levels. Equivalent US yields rose 0.1% p.a., to 3.9% p.a., and German yields rose 0.5% p.a., to 2.6% p.a., respectively. Japanese yields rose 0.2% p.a., to 0.4% p.a., as the Bank of Japan loosened the target range for 10-year yields under its yield curve control policy.

UK 10-year implied inflation, as measured by the difference between conventional and inflation-linked bonds of the same maturity, fell 0.6% p.a. to 3.4% p.a. Equivalent US implied inflation rose 0.1% p.a., to 2.3% p.a.

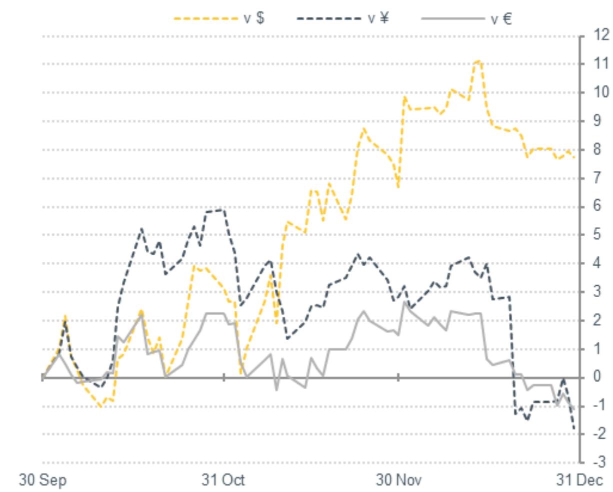
Historic returns for world markets [1]



Annual CPI Inflation (% p.a.)



Sterling trend chart (% change)



Source: DataStream. [1] Returns shown in Sterling terms. Indices shown (from left to right) are: FTSE All World, FTSE All Share, FTSE AW Developed Europe ex-UK, FTSE North America, FTSE Japan, FTSE AW Developed Asia Pacific ex-Japan, FTSE Emerging, FTSE Fixed Gilts All Stocks, FTSE Index-Linked Gilts All Maturities, iBoxx Corporates All Investment Grade All Maturities, ICE BofA Global Government Index, MSCI UK Monthly Property; UK Interbank 7 Day

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Market Background

Global investment grade credit spreads fell 0.3% p.a., to 1.5% p.a., while speculative-grade spreads fell 1.0% p.a., to 5.1% p.a. Speculative-grade default rates have risen a little since the start of 2022 but remain below long-term average levels.

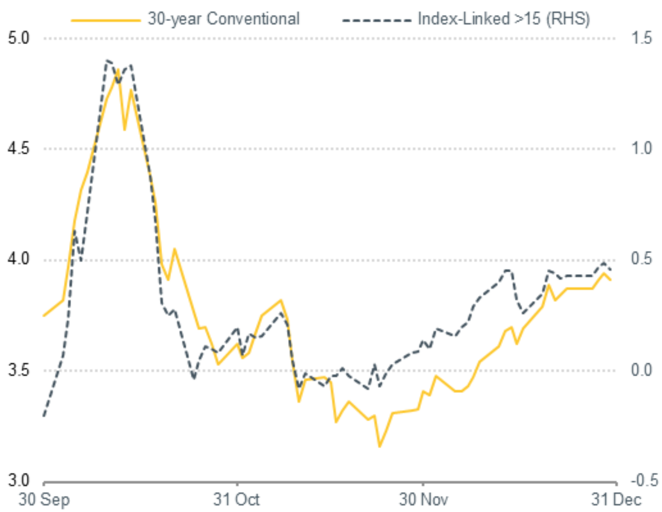
The FTSE All World Total Return Index rose 7.6% (local currency) .The energy sector outperformed amid record earnings reports, as did Industrials and basic materials. Consumer discretionary and technology stocks underperformed as the cost-of-living squeeze intensified. Europe ex-UK outperformed the most while Japan notably underperformed on the back of yen strength and doubts over ongoing monetary support from the Bank of Japan.

Page 70

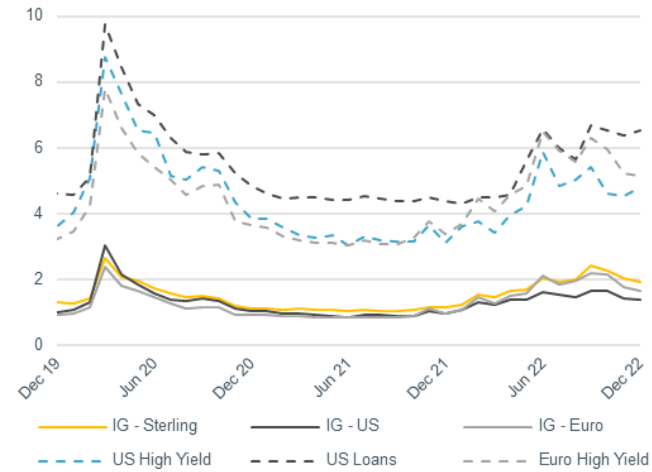
Easing inflation in the US saw the US dollar fall 4.8% in trade-weighted terms, reducing its year-to-date gains to 6.3%. Equivalent sterling, euro, and yen measures rose 1.9%, 4.4%, and 5.2%, respectively.

MSCI UK Monthly Property Index declines slowed from falling 0.5% in November to falling 0.03% in December. The extent of recent declines in capital values, which are now 20% below their June peak, has been the primary driver. Capital values have fallen across the 3 main commercial sectors but have been most notable in the industrial sector, where they have fallen 27% since the end of June.

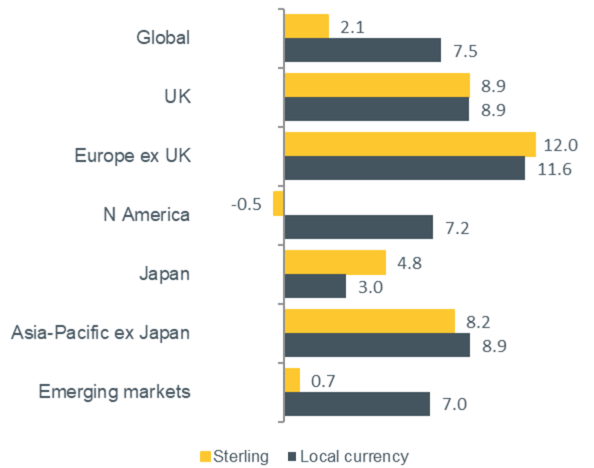
Gilt yields chart (% p.a.)



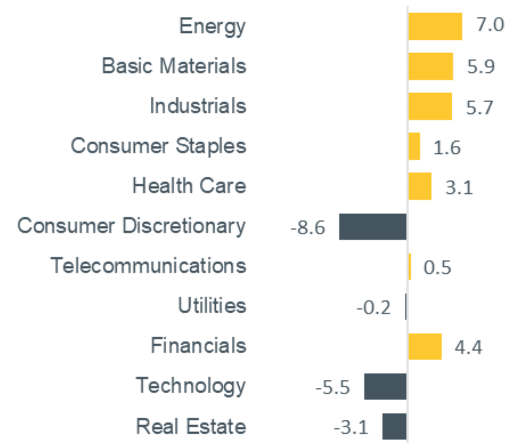
Investment and speculative grade credit spreads (% p.a.)



Regional equity returns [1]



Global equity sector returns (%) [2]



Source: DataStream, Barings, ICE [1] FTSE All World Indices. Commentary compares regional equity returns in local currency. [2] Returns shown in Sterling terms and relative to FTSE All World.

Risk Warning

Please note the value of investments, and income from them, may fall as well as rise. This includes equities, government or corporate bonds, and property, whether held directly or in a pooled or collective investment vehicle. Further, investment in developing or emerging markets may be more volatile and less marketable than in mature markets. Exchange rates may also affect the value of an investment. As a result, an investor may not get back the amount originally invested. Past performance is not necessarily a guide to future performance.

In some cases, we have commercial business arrangements/agreements with clients within the financial sector where we provide services. These services are entirely separate from any advice that we may provide in recommending products to our advisory clients. Our recommendations are provided as a result of clients' needs and based upon our independent research. Where there is a perceived or potential conflict, alternative recommendations can be made available.

Geometric v Arithmetic Performance

Hymans Robertson are among the investment professionals who calculate relative performance geometrically as follows:

$$\frac{(1 + Fund\ Performance)}{(1 + Benchmark\ Performance)} - 1$$

Some industry practitioners use the simpler arithmetic method as follows:

$$Fund\ Performance\ - Benchmark\ Performance$$

The geometric return is a better measure of investment performance when compared to the arithmetic return, to account for potential volatility of returns.

The difference between the arithmetic mean return and the geometric mean return increases as the volatility increases.

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