London Borough of Havering Pension Fund

Q4 2020 Investment Monitoring Report

Simon Jones – Partner
Mark Tighe – Investment Analyst
Meera Devlia – Investment Analyst

HYMANS ROBERTSON

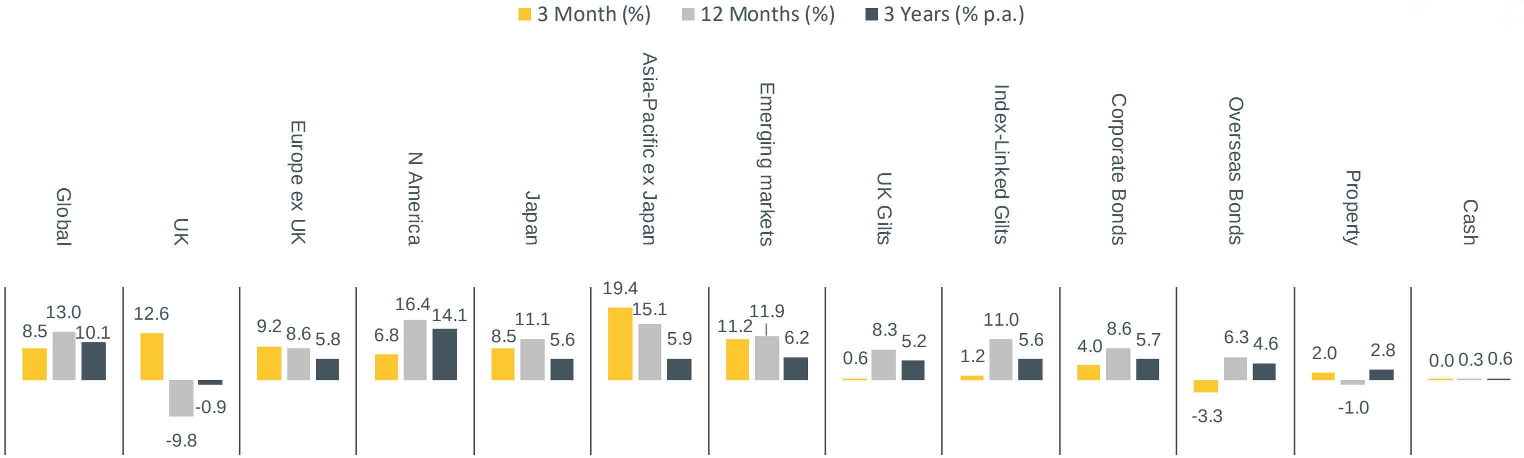
Q3 GDP releases show the initial rebound in activity was sharp as the major advanced economies emerged from lockdown but annualised falls in output have been significant. Composite Purchasing Manager Indices suggest the UK and Eurozone economies ended 2020 on a weak note but the global equivalent remains at a level signalling expansion, supported by solid readings in the US, China and elsewhere. Though COVID-19 cases continue to rise at a global level, many advanced economies could potentially vaccinate a large proportion of their most vulnerable citizens in the first half of 2021.

UK headline inflation slowed more than expected falling from 0.7% in October to 0.3% year-on-year in November as restrictions to curb the spread of coronavirus were re-imposed.

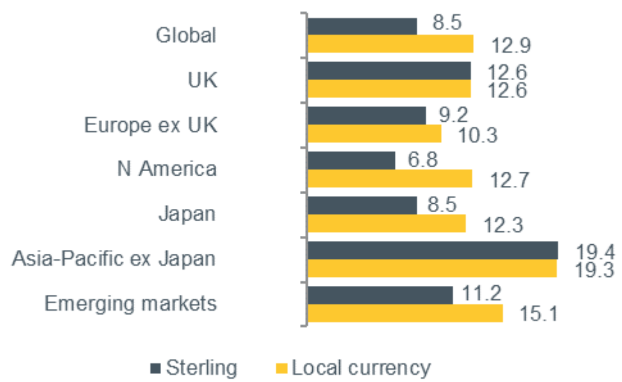
Despite hopes of economic recovery in 2021, government bond yields rose only modestly in the US and fell in the UK and Germany due to near-term economic weakness and central bank intervention. Implied inflation rose at longer terms despite the government's announcement that RPI will be aligned with CPIH from 2030. Global investment grade credit spreads fell from 1.4% p.a. to 1.0% p.a. and global speculative-grade spreads from 5.6% p.a. to 4.1% p.a., as lower rated credit outperformed higher quality.

Sterling was volatile as Brexit talks approached their conclusion, although it ended the period 1.9% higher in trade-weighted terms as the EU and UK reached a trade deal. In comparison, on a trade-weighted basis the US Dollar and Japanese Yen, both typically considered safe-haven currencies, fell 5.3% and 1.4% below end-September levels.

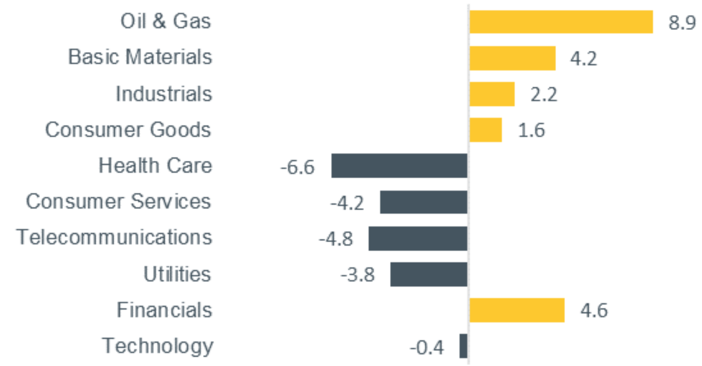
Historic returns for world markets [1]



Regional equity returns [2]



Global equity sector returns (%) [3]



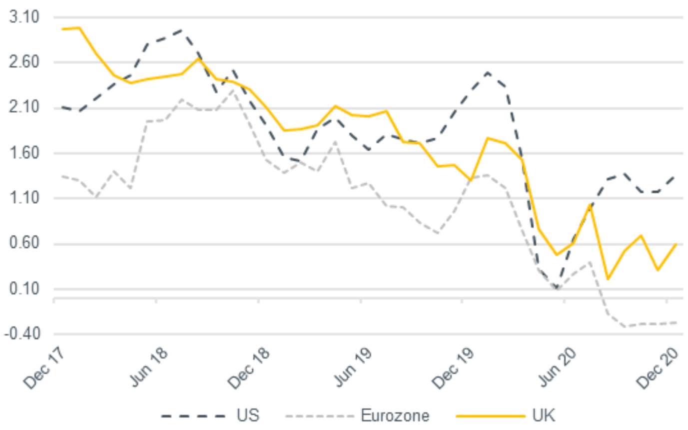
[1] All returns are in Sterling terms. Indices shown (from left to right) are as follows: FTSE All World, FTSE All Share, FTSE AW Developed Europe ex-UK, FTSE North America, FTSE Japan, FTSE AW Developed Asia Pacific ex-Japan, FTSE Emerging, FTSE Fixed Gilts All Stocks, FTSE Index-Linked Gilts All Maturities, iBoxx Corporates All Investment Grade All Maturities, JP Morgan GBI Overseas Bonds, MSCI UK Monthly Property Index; UK Interbank 7 Day. [2] FTSE All World Indices [3] Relative to FTSE All World Indices.

After falling in October amid renewed restrictions to curb rapidly rising COVID-19 cases, positive vaccine news propelled equity markets higher, with the FTSE All World returning 12.9% in Q4. This news also caused some moderate rotation within global equities as areas of the market most impacted negatively by the pandemic outperformed. This was evident in the outperformance of cyclical sectors such as oil & gas, financials and materials and interconnectedly, styles such as value and smaller capitalisation stocks. Defensive areas such Healthcare, Utilities and Telecoms all underperformed.

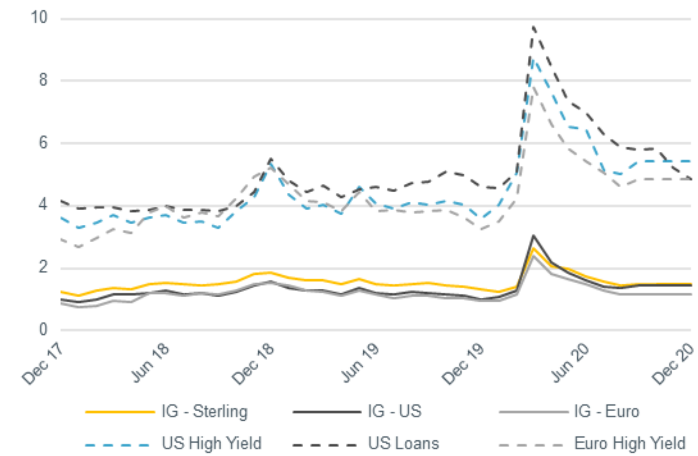
From a regional perspective, Emerging market and Asia ex-Japan equities outperformed, both benefiting from renewed hopes of a cyclical recovery, a falling dollar and increasing global trade activity.

The rolling 12-month total return on the MSCI UK Monthly Property index was -1.9% to the end of November, although monthly total returns have now been positive since July. Capital values, in aggregate, have fallen 7.1% in the year to November, predominantly due to a 17.9% fall in the retail sector, where capital values continue to decline sharply.

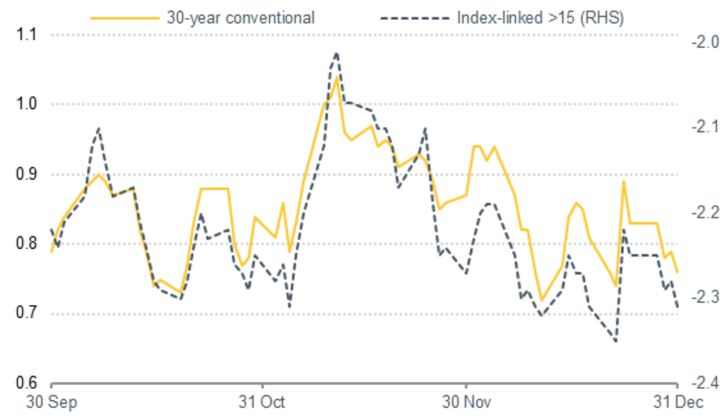
Annual CPI Inflation (% p.a.)



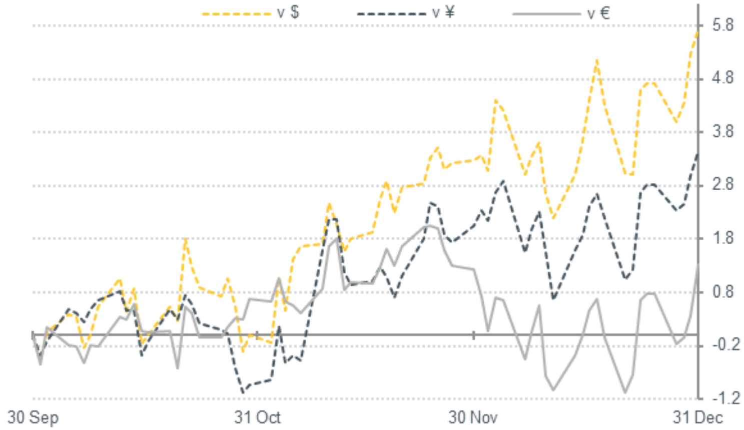
Investment and speculative grade credit spreads (% p.a.)



Gilt yields chart (% p.a.)



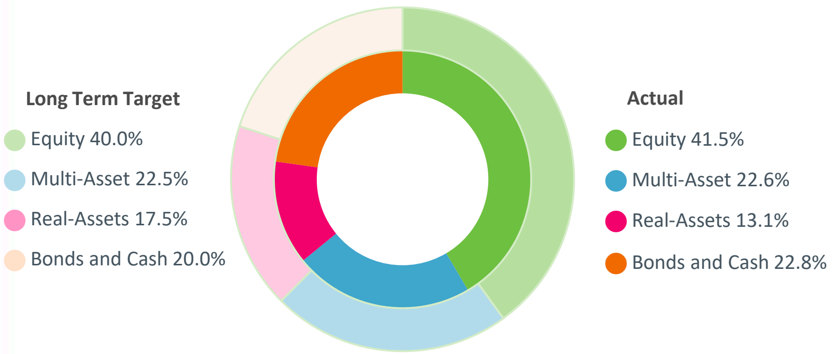
Sterling trend chart (% change)

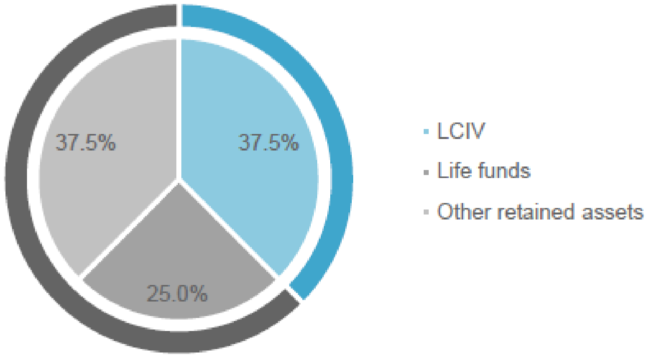


Source: Reuters

- The Fund's investment approach is implemented through the London Common Investment Vehicle ("LCIV"), and retained assets including life funds (with fee structures aligned with LCIV).
- The charts right summarise the approach agreed for the implementation of the Fund's longer-term strategy. We have indicated ongoing governance responsibilities in blue for LCIV and grey for the Committee.
- The drawdown in the Stafford and private debt mandates is expected to be completed in 2021.
- The target allocation to LCIV and life funds totals 75% of Fund assets. Other retained assets will be delivered through external managers, with the position reviewed periodically.
- A review of the Fund's investment strategy was carried out by the Committee in 2020. Agreed changes are currently being implemented.

Asset Allocation





Long Term Strategic Target

Asset class	Long term target	LCIV		Life funds		Other retained assets	
		Manager(s)	%	Manager(s)	%	Manager(s)	%
Equity	40	Baillie Gifford	15	LGIM	25		
Multi-Asset	22.5	Baillie Gifford, Ruffer	22.5				
Property	10					UBS, CBRE	10
Infrastructure	7.5					JP Morgan, Stafford	7.5
Private Debt	7.5					Permira, Churchill	7.5
Other bonds	12.5					RLAM	12.5
Total	**100**	**-**	**37.5**	**-**	**25**	**-**	**37.5**

Current Investment Implementation

- The total value of the Fund's assets rose by c. £54.3m over the quarter to c. £850.2m as at 31 December 2020 as equities rallied and credit spreads continued to narrow over the quarter.
- £21.5m was transferred from Baillie Gifford Global Alpha to RLAM MAC during the quarter in line with the Committee's decision to trim some of the Baillie Gifford profit and increase the allocation to MAC towards the target level. The Baillie Gifford mandate remains overweight and will be used to bring the Fund's other equity mandates in line with the relevant targets as part of the upcoming equity restructuring.

The Fund paid the following capital calls during the quarter:

- c.£1.7m to Churchill funded from existing cash.
- £1.7m to Permira funded using profits from the Russell currency hedging mandate.
- c.£2.4m to Stafford funded from the RLAM corporate mandate.

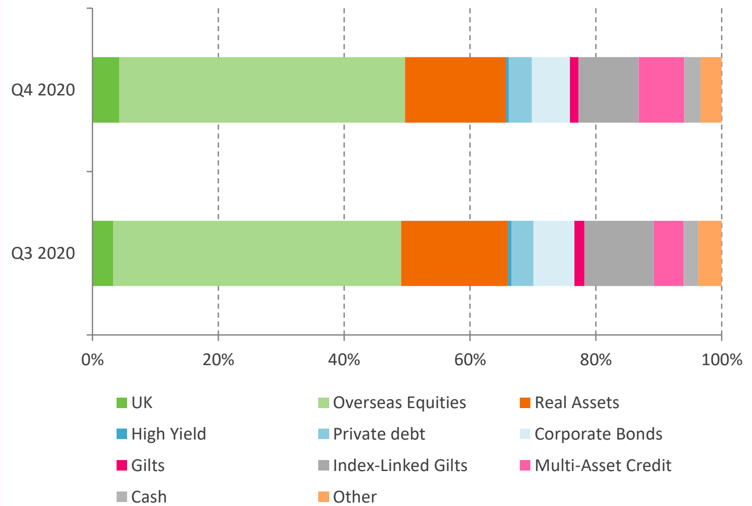
Asset Allocation

Manager		Valuation (£m) Q3 2020	Valuation (£m) Q4 2020	Actual Proportion	Benchmark	Relative
Equity		**337.2**	**352.9**	**41.5%**	**40.0%**	**1.5%**
LGIM Global Equity	LCIV aligned	63.5	68.9	8.1%	10.0%	-1.9%
LGIM Fundamental Equity	LCIV aligned	51.5	58.5	6.9%	10.0%	-3.1%
LGIM Emerging Markets	LCIV aligned	34.6	38.5	4.5%	5.0%	-0.5%
Baillie Gifford Global Equity (CIV)	LCIV	187.6	187.0	22.0%	15.0%	7.0%
Multi-Asset		**182.7**	**192.2**	**22.6%**	**22.5%**	**0.1%**
Ruffer Absolute Return (CIV)	LCIV	99.2	103.6	12.2%	12.5%	-0.3%
Baillie Gifford DGF (CIV)	LCIV	83.6	88.6	10.4%	10.0%	0.4%
Real-Assets		**111.8**	**111.4**	**13.1%**	**17.5%**	**-4.4%**
UBS Property	Retained	40.4	40.3	4.7%	6.0%	-1.3%
CBRE	Retained	27.5	26.7	3.1%	4.0%	-0.9%
JP Morgan	Retained	25.0	23.8	2.8%	4.0%	-1.2%
Stafford Capital Global Infrastructure	Retained	18.8	20.7	2.4%	3.5%	-1.1%
Bonds and Cash		**164.2**	**193.7**	**22.8%**	**20.0%**	**2.8%**
RLAM MAC	Retained	37.6	61.1	7.2%	7.5%	-0.3%
RLAM ILGs	Retained	41.0	41.7	4.9%	5.0%	-0.1%
RLAM Corporate Bonds	Retained	44.5	44.2	5.2%	0.0%	5.2%
Churchill	Retained	15.4	16.5	1.9%	4.5%	-2.6%
Permira	Retained	12.5	14.4	1.7%	3.0%	-1.3%
Cash at Bank	Retained	11.1	12.5	1.5%	0.0%	1.5%
Currency Hedging P/L	Retained	2.2	3.3	0.4%	0.0%	0.4%
Total Fund		**795.8**	**850.2**	**100.0%**	**100.0%**	

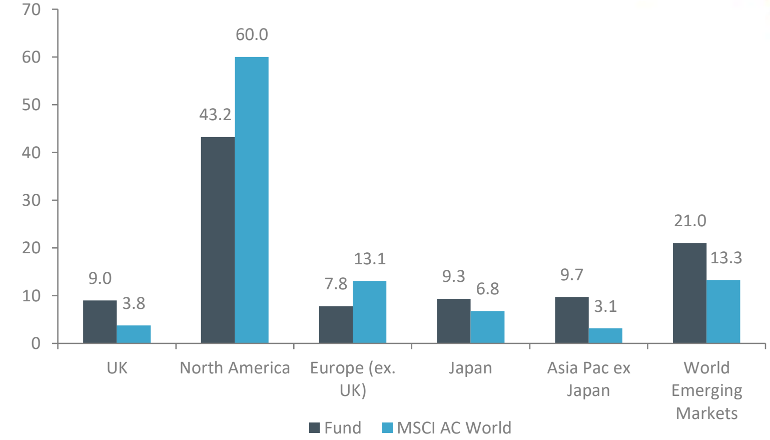
Source: Northern Trust, Investment Managers

- The chart right illustrates the underlying asset allocation of the Fund, i.e. taking account of the underlying holdings in the multi-asset funds on a 'look through' basis.
- The Fund's allocation to equities increased over the quarter to c.49.7% at 31 December 2020 (c.49.0% at 30 September 2020).
- The allocation to real assets decreased to c.16.% of Fund assets as at 31 December 2020 (c.17% as at 30 September 2020).
- These movements were in part driven by positive vaccine news, significantly propelling equity market gains.
- Strategic allocations to market-cap equity and factor-based equity were both increased from 7.5% to 10.0% following the Committee's review of investment strategy. A corresponding decrease to the multi-asset allocation took place.

Asset class exposures



Regional Equity Allocation



Source: Investment Managers, Datastream

- The table sets out the performance of each mandate against their respective benchmarks.
- The LGIM mandates tracked their respective benchmarks over the quarter, whilst the remaining of the Fund's mandates contributed both positive and negative relative returns.
- Please note that all asset performance is in GBP terms and does not make an allowance for currency fluctuations. The total Fund performance includes the impact of the Russell currency overlay mandate.
- Please note the separate slide for further detail on the Russell mandate, along with asset performance excluding the impact of currency fluctuations.

Manager performance

	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
Growth												
LGIM Global Equity	8.5	8.5	**0.0**	12.9	13.0	**-0.1**	10.1	10.0	**0.0**	12.5	12.6	**0.0**
LGIM Fundamental Equity	13.7	13.9	**-0.1**	1.2	1.1	**0.1**	3.9	3.9	**0.0**	10.1	10.2	**-0.1**
LGIM Emerging Markets	11.2	11.3	**-0.1**	11.5	11.9	**-0.4**	-	-	**-**	11.8	12.0	**-0.2**
Baillie Gifford Global Equity (CIV)	11.1	8.6	**2.4**	32.8	13.0	**17.5**	17.6	10.0	**6.9**	17.4	13.1	**3.8**
Ruffer Absolute Return (CIV)	4.5	1.0	**3.5**	9.9	4.5	**5.1**	4.0	4.8	**-0.8**	4.9	4.8	**0.1**
Baillie Gifford DGF (CIV)	6.0	0.9	**5.1**	2.2	3.8	**-1.6**	3.0	4.0	**-1.0**	4.4	4.0	**0.4**
Income												
UBS Property	1.4	2.1	**-0.7**	0.1	-1.0	**1.2**	3.5	2.4	**1.1**	5.7	6.6	**-0.9**
CBRE	-2.9	1.3	**-4.1**	2.4	5.7	**-3.1**	-	-	**-**	3.5	5.7	**-2.1**
JP Morgan	-1.8	1.3	**-3.0**	9.8	5.7	**4.0**	-	-	**-**	6.5	5.7	**0.8**
Stafford Capital Global Infrastructure	-2.3	1.3	**-3.6**	4.3	5.7	**-1.3**	-	-	**-**	6.3	6.1	**0.2**
Protection												
RLAM MAC and ILGs	3.3	2.9	**0.3**	10.7	10.8	**0.0**	7.1	6.9	**0.2**	8.7	8.1	**0.6**
RLAM Corporate Bonds	5.7	5.3	**0.4**	-	-	**-**	-	-	**-**	17.6	18.5	**-0.7**
Churchill	-1.6	1.0	**-2.6**	-0.5	4.6	**-4.9**	-	-	**-**	1.1	4.8	**-3.5**
Permira	-2.0	1.0	**-3.0**	-1.1	4.6	**-5.5**	-	-	**-**	0.0	4.7	**-4.4**
Total	6.7	4.5	**2.1**	11.9	7.3	**4.3**	7.1	6.2	**0.9**	8.2	-	**-**

Source: Northern Trust, investment managers. Please note that benchmark performance for Baillie Gifford DGF and Ruffer Absolute Return funds is inclusive of outperformance targets. In addition, longer term performance for Baillie Gifford Global Equity, Baillie Gifford DGF and Ruffer Absolute Return funds is inclusive of performance prior to their transfer in to the London CIV. LGIM Global and Fundamental Equity mandates were managed by SSGA prior to November 2017 and we have retained the performance history for these allocations. Performance figures for CBRE, Stafford ad JP Morgan has been taken from the managers rather than Northern Trust. The Fund performance figure includes the effect of the currency hedging mandate managed by Russell..

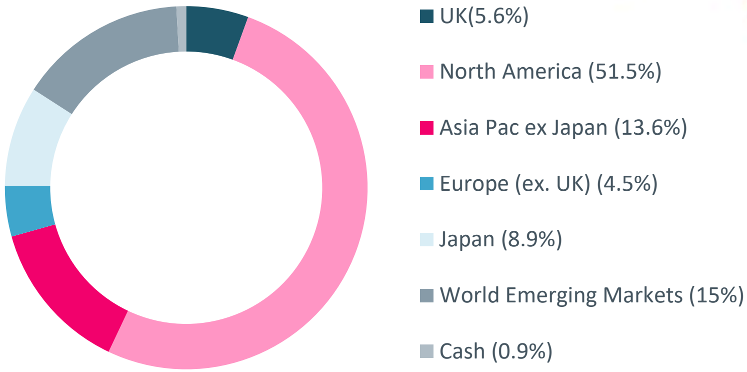
LCIV Funds

- The Fund accesses global equity and multi-asset sub-funds through LCIV.
- LCIV are responsible for the ongoing monitoring and governance of the underlying investment managers.
- The Global Alpha Growth sub-fund is managed by Baillie Gifford.
- The objective of the sub-fund is to exceed the rate of return of the MSCI All Country World Index by 2-3% per annum on a gross of fees basis over rolling five-year periods.
- Following exceptionally strong performance over 2020, the allocation to the Global Alpha Growth sub-fund is significantly over target weight. The Committee has agreed to trim this as part of the upcoming equity restructure.

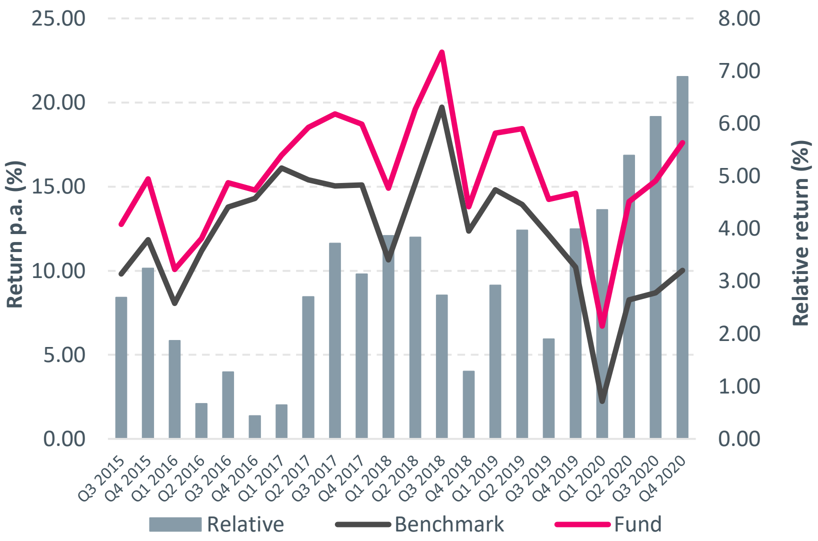
LCIV Global Alpha Growth

	Last 3 months (%)	Last 12 months (%)	Last 3 years (% p.a.)	Since Inception (% p.a.)
LCIV Global Alpha Growth	11.1	32.8	17.6	17.4
Benchmark	8.6	13.0	10.0	13.1
Relative	2.4	17.5	6.9	3.8

Regional Allocation



Rolling 3 year return



Source: Investment Manager, LCIV, Northern Trust
Date of inception 25 April 2012

LCIV Diversified Growth Fund

- The sub-fund is managed by Baillie Gifford through their Diversified Growth strategy.
- The sub-fund's objective is to achieve long term capital growth at lower risk than equity markets.
- Benchmark is UK base rate + 3.5% (net).

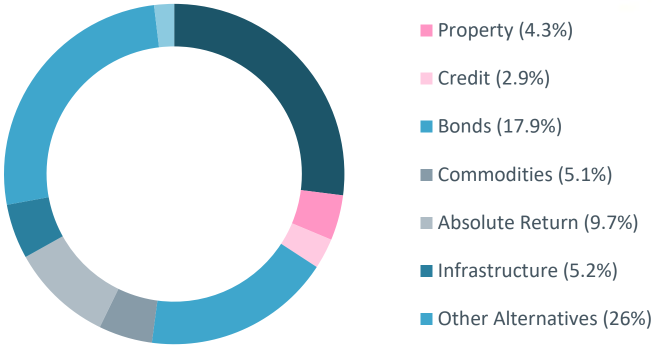
LCIV Absolute Return Fund

- The sub-fund is managed by Ruffer.
- The sub-fund's objective is to achieve low volatility and positive returns in all market conditions.
- Benchmark is 3 month LIBOR + 4% p.a.

LCIV Diversified Growth Fund

	Last 3 months (%)	Last 12 months (%)	Last 3 years (% p.a.)	Since Inception (% p.a.)
LCIV Diversified Growth	6.0	2.2	3.0	4.4
Benchmark	0.9	3.8	4.0	4.0
Relative	5.1	-1.6	-1.0	0.3

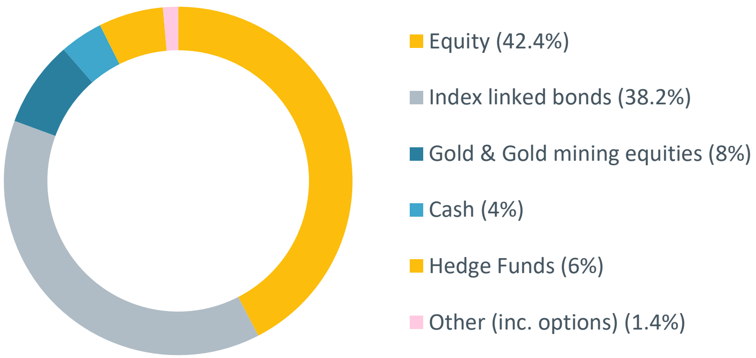
Asset Allocation



LCIV Absolute Return Fund

	Last 3 months (%)	Last 12 months (%)	Last 3 years (% p.a.)	Since Inception (% p.a.)
LCIV Absolute Return	4.5	9.9	4.0	4.9
Benchmark	1.0	4.5	4.8	4.8
Relative	3.5	5.1	-0.7	0.1

Asset Allocation



Source: Investment Managers, LCIV, Northern Trust
Diversified Growth Fund inception date: 26/11/2013
Absolute Return Fund inception date: 13/09/2010

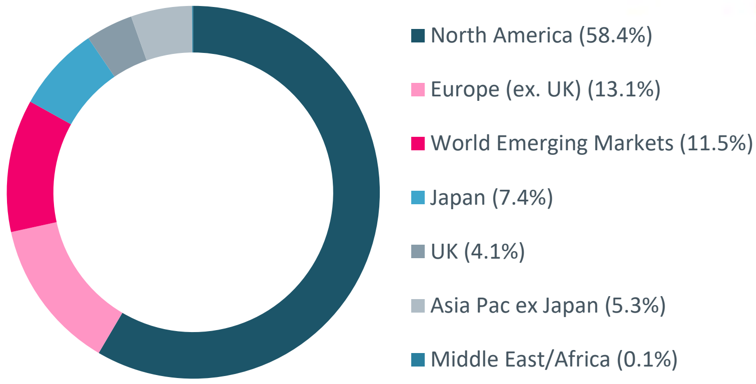
LGIM Equity Funds

- LGIM were appointed from November 2017 to manage the Fund's index tracking global equity portfolio, with the mandate being split equally between investment in a fund tracking a market cap weighted index and a fund tracking a fundamentally weighted index (RAFI).
- The objective of this mandate is to match the performance of the respective benchmark indices.
- Performance information reflects performance from LGIM from November 2017, and SSGA prior to this date.
- The RAFI fund has outperformed the global index by c.5% over the quarter. However, in the longer term continues to return poorly being c.12% behind the global index over 12 months to 31 December.
- The Committee are considering replacing the RAFI allocation (value tilted) with a multi-factor equity fund.

All World Equity Index

	Last 3 months (%)	Last 12 months (%)	Last 3 years (% p.a.)	Since Inception (% p.a.)
LGIM Global Equity	8.5	12.9	10.1	12.5
Benchmark	8.5	13.0	10.0	12.6
Relative	0.0	-0.1	0.0	0.0

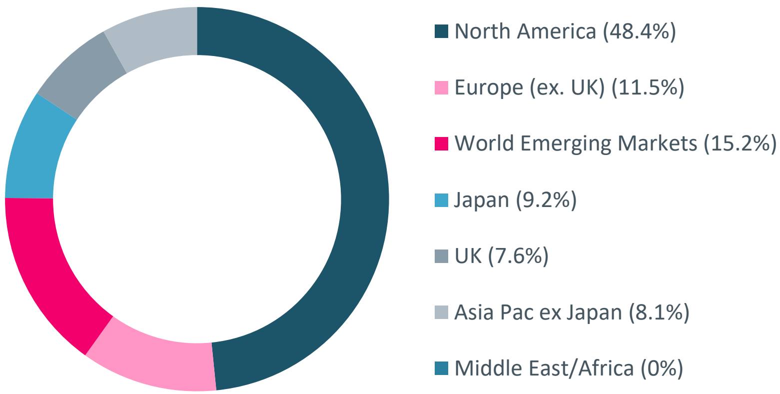
Regional Allocation



FTSE RAFI All World 3000 Equity Index

	Last 3 months (%)	Last 12 months (%)	Last 3 years (% p.a.)	Since Inception (% p.a.)
LGIM Fundamental Equity	13.7	1.2	3.9	10.1
Benchmark	13.9	1.1	3.9	10.2
Relative	-0.1	0.1	0.0	-0.1

Regional Allocation



Source: Northern Trust, LGIM
All World Equity Index inception date: 23/02/2011
FTSE RAFI All World 3000 inception date: 19/08/2015

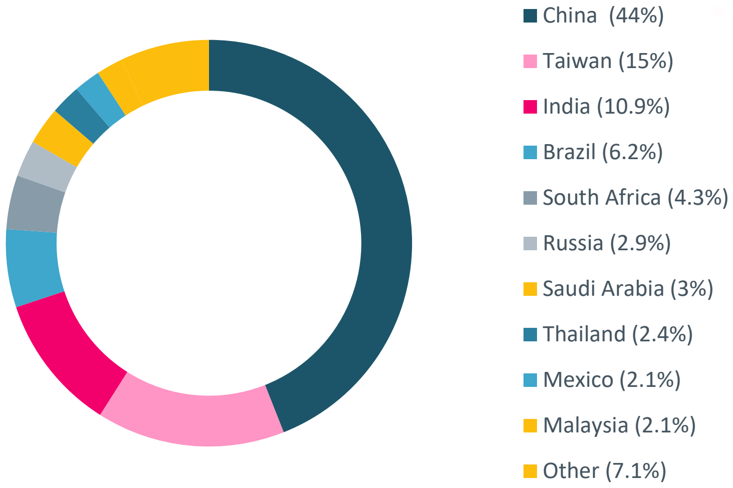
LGIM Emerging Markets

- The objective of this mandate is to match the performance of the FTSE Emerging indices.

World Emerging Markets Equity Index

	Last 3 months (%)	Last 12 months (%)	Since Inception (% p.a.)
LGIM Emerging Markets	11.2	11.5	11.8
Benchmark	11.3	11.9	12.0
Relative	-0.1	-0.4	-0.2

Regional Allocation



Source: Northern Trust, LGIM
Inception date: 01/01/2019

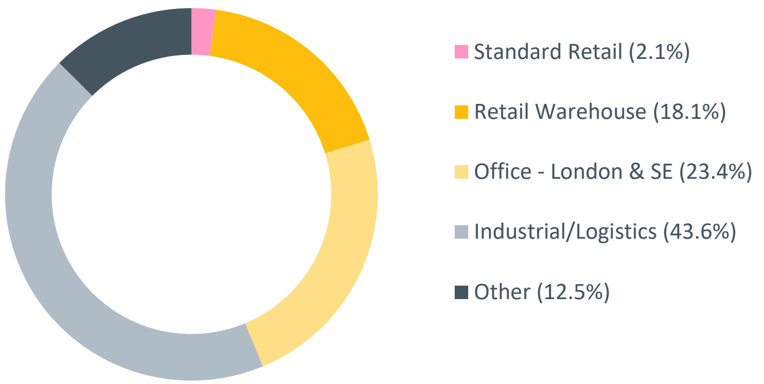
UBS Triton Property Fund

- The objective of the fund is to deliver returns broadly in line with a peer group of other UK property funds.
- The fund invests directly in UK properties with returns generated through the collection of rental income and growth in both rental levels and capital values.
- The Triton fund continued to increase the level of rent collection over the quarter and this is moving towards more normal levels after a dip during the start of the pandemic. Rent collection over Q4 was 91% (79% over Q3). The improvement in rent collection is due to the fund being underweight in the retail sector. However, the relative underperformance of the fund to the benchmark this quarter is also due to being underweight to the retail sector, as this contributed strong returns over the quarter in a reversal of recent trends.

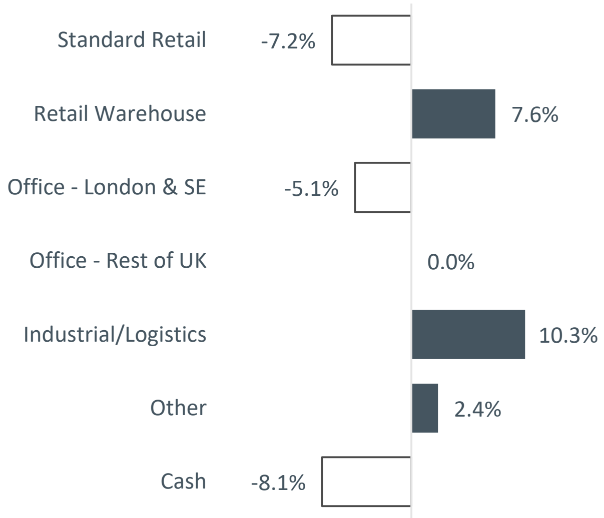
UBS Fund Performance

	Last 3 months (%)	Last 12 months (%)	Last 3 years (% p.a.)	Since Inception (% p.a.)
UBS Property	1.4	0.1	3.5	5.7
Benchmark	2.1	-1.0	2.4	6.6
Relative	-0.7	1.2	1.1	-0.9

Sector Allocation



Sector Allocation Relative to Benchmark



Source: Northern Trust, UBS
Inception date: 28/02/2005

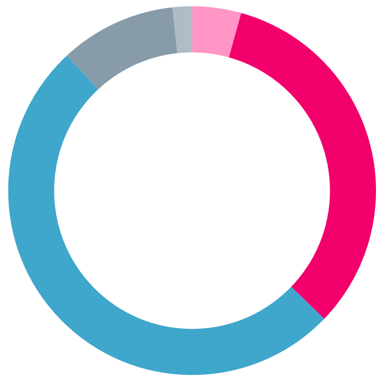
RLAM – Bond mandates

- Royal London Asset Management (RLAM) was appointed in February 2005 to manage the Fund's bond mandate.
- RLAM now manage two separate portfolios: the existing portfolio consisting of index linked gilts and with the addition of MAC; and a separate corporate bond portfolio which is being sold down to fund the strategic changes.
- The chart below right compares the credit rating breakdown of the multi-asset credit and corporate bond portfolios at the end of the quarter.
- The strategic allocation to corporate bonds is now 0%, with allocations to index linked gilts and multi-asset credit 5% and 7.5% respectively.
- Credit spreads continued to narrow over the quarter which benefitted the corporate bond and MAC portfolios. However, low real yields over the period dampened returns from the joint MAC and ILGs portfolio.

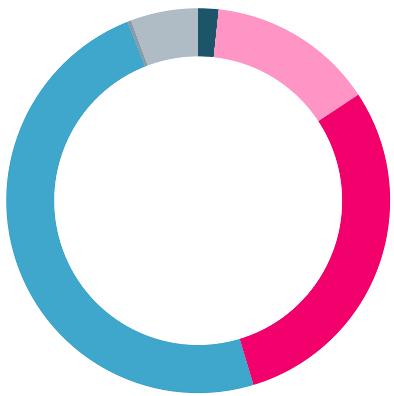
RLAM Fund Performance

	Last 3 months (%)	Last 12 months (%)	Last 3 years (% p.a.)	Since Inception (% p.a.)
RLAM MAC and ILGs	3.3	10.7	7.1	8.7
Benchmark	2.9	10.8	6.9	8.1
Relative	0.3	0.0	0.2	0.6
RLAM Corporate Bonds	5.7	n/a	n/a	17.6
Benchmark	5.3	n/a	n/a	18.5
Relative	0.4	n/a	n/a	-0.7

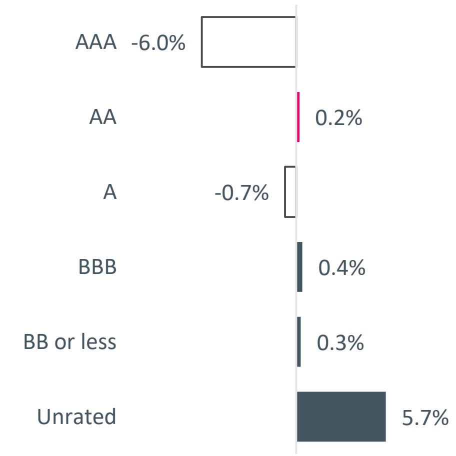
Credit Allocation (MAC)



Credit allocation (Corporate Bonds)



Credit Allocation relative to benchmark (Corporate Bonds)



MAC and ILGs Benchmark: FTSE Index Linked over 5 Year 50%, ICE BAML BB-BBB Index 25%, Credit Suisse US Leveraged Loan GBP Hedged 25%.
Corporate Bonds Benchmark: iBoxx Sterling Non-Gilt Over 10 year Index.

Source: Northern Trust, RLAM

Russell Currency Hedging

- Russell Investments have been appointed to manage the Fund's currency overlay mandate.
- The current policy is to hedge non-sterling exposures in the Fund's private markets mandates. Currency exposure in equity mandates is retained.
- At present, 100% of the exposure to USD, EUR and AUD from the private market investments is hedged within any residual currency exposure retained on a de-minimis basis.
- The charts illustrate the breakdown of hedged currency exposures in each mandate (ignoring unhedged exposures).
- Since implementation, the mandate has a realised loss of c.£0.6m. This is due to underperformance of sterling against the Euro and Australian Dollar. A corresponding gain has been seen in the value of the assets exposed to these currencies.

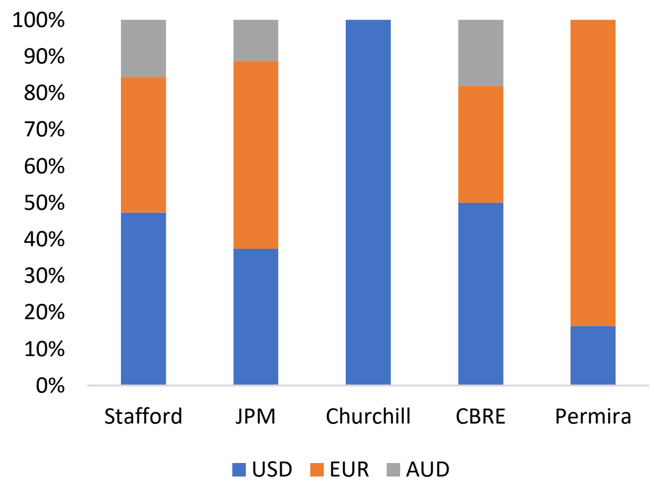
Q4 performance

	Asset return (inc. FX impact)	Currency return (via Russell mandate)	Asset return (ex. FX impact)	BM return	Relative return (ex. FX impact)
Stafford	-2.3	1.8	-0.6	1.3	-1.9
JPM	-1.8	1.8	0.0	1.3	-1.3
Churchill	-1.6	3.0	1.4	1.0	0.4
CBRE	-2.9	1.6	-1.2	1.3	-2.5
Permira	-2.0	1.0	-1.0	1.0	-1.9

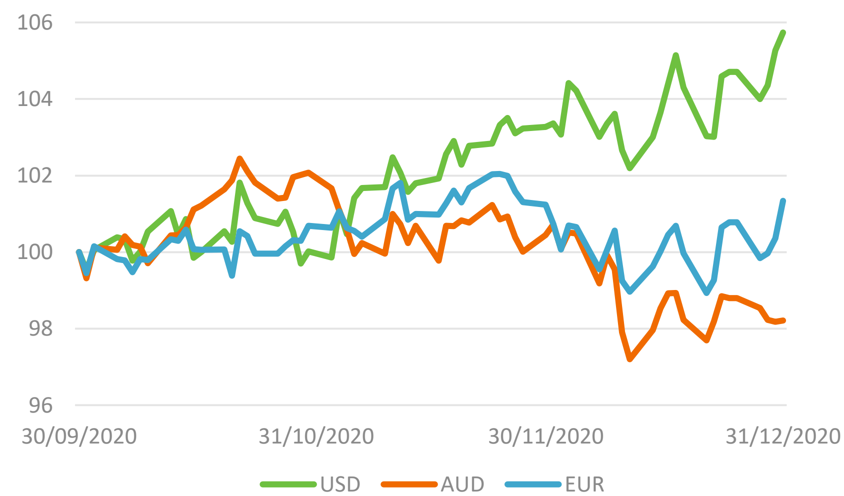
Performance since mandate inception*

	Asset return (inc. FX impact)	Currency return (via Russell mandate)	Asset return (ex. FX impact)	BM return	Relative return (ex. FX impact)
Stafford	4.3	-1.9	2.4	5.7	-3.1
JPM	9.8	-3.1	6.7	5.7	1.0
Churchill	-0.5	-0.2	-0.7	4.6	-5.1
CBRE	2.4	-2.1	0.2	5.7	-5.1
Permira	-1.1	-1.3	-2.4	4.6	-6.7

Hedged currency exposure as at quarter end



Sterling performance vs foreign currencies (rebased to 100 at 30 September 2020)



Source: *Northern Trust, Investment managers*

**Performance shown since 31 December 2019 which was the first month end after inception*

- Since March 2018, the Fund has made commitments to five private markets funds as outlined below. The table provides a summary of the commitments and drawdowns to 31 December 2020.
- The allocations to JP Morgan and CBRE are fully drawn.
- There are outstanding commitments of approximately £35m to the remaining funds which will be primarily funded from the RLAM mandate.

Mandate	Infrastructure			Global Property	Private Debt	
Vehicle	**Stafford Infrastructure Secondaries Fund II**	**Stafford Infrastructure Secondaries Fund IV**	**JP Morgan Infrastructure Investments Fund**	**CBRE Global Investment Partners Global Alpha Fund**	**Churchill Middle Market Senior Loan Fund II**	**Permira Credit Solutions IV Senior Fund**
Commitment Date	25 April 2018	18 December 2020	31 July 2018	30 September 2018	December 2018	December 2018
Fund currency	EUR	EUR	USD	USD	USD	EUR
Gross commitment	c. £26m (EUR 28.5m)	c.£18m (EUR 20m)	c. £26.1m (USD 34m)	c. £26.1m (USD 34m)	c. £23.8 m (USD 31m)	c. £36 m
Net capital called during quarter (Payments less returned capital)	c. £2.4m (EUR c.2.7m)	-	-	-	c. £1.7m (USD 2.3m)	c.£1.7m
Net capital drawn to date	EUR 20.5m (c. £18.4m)	-	c. £26.1m (USD 34m)	c. £26.1m (USD 34m)	c. £14.3.m (USD 19.4m)	c. £11.0m (EUR 12.6m)
Distributions/returned capital to date (includes income and other gains)	EUR 5.5m (c. £4.8m)	-	c. £4.1.m (USD 5.5m)	-	c. £0.2.m (USD 0.3m)	£0.7m
NAV at quarter end	EUR 23.1m (c. £20.7m)	-	USD 32.5m (c. £23.8m)	USD 36.5m (c. £26.7m)	USD 22.5m (c. £16.5m)	£14.4m
Net IRR since inception (in fund currency)	5.3% p.a. *(vs. 8-9% target)**	-	6.9%*	9.6%*	9.0%**	15.4%
Net cash yield since inception (in fund currency)	5.0% p.a. *(vs. 5% target)**	-	11.4%*	4.8%*	5.5%*	4.8%*
Number of holdings	20 funds, 306 underlying assets*	-	19 companies, 560 assets	50 investments, 2,644 properties*	76 investments	22 investments

**as at 30/09/2020 (latest available) **refers to the IRR of realised investments in the portfolio*

Source: Investment Managers

Asset Class	Market Summary
Equities	• Further rises in global equities leaves valuation measures increasingly stretched versus history. • There remains significant disparity in valuations by region and overall valuations do not look as expensive in the context of very low real yields. • Q3 earnings have continued to outperform expectations and estimates for Q4 have risen. • The bounce in earnings expected in 2021 would leave full-year earnings in 2021 above end-2019 levels. • Given high valuations and near-term economic uncertainty, we retain a degree of caution, despite the fundamental improvement expected in 2021.
Investment Grade Credit	• Despite a continued rise in leverage and fall in interest coverage, investment-grade spreads are now well below long-term median levels. • Low central bank policy rates and government bond yields will likely provide ongoing technical support and fundamentals should improve as earnings recover in 2021, but very low spreads and yields may pose a headwind to returns going forward. • Sterling investment grade spreads, on a ratings-consistent basis, have fallen well below long-term median levels and the premium relative to equivalent global credit is low relative to history. • Given less recent central bank support, equivalently rated European ABS spreads have lagged the recovery in corporate credit spreads since the peak of market disruption at the end of Q1 and spreads relative to similarly rated corporate credit are attractive versus history.
Liquid Sub-Investment Grade Debt	• Central bank intervention has enabled companies to raise huge amounts of debt to see them through near-term disruption. • This increase in leverage, coupled with falling profits, has resulted in lower interest coverage, despite a significant decline in yields. • Although default rates have risen – to 8.4% in the last 12 months to November in the US high yield market – accommodative funding conditions have helped keep them well below the peaks of previous crises. • It is likely defaults could remain elevated as companies lose government support. • Global high yield credit spreads have retraced significantly since Q1 and are now well below longer-term medians. • US leveraged loan spreads have also fallen but offer a premium relative to US high yield.
Private Lending	• Transaction levels have returned to pre-COVID levels and, while pricing has also returned to pre-COVID levels, loans are typically being written with better lender protections meaning a better risk-adjusted return overall. • The illiquidity premium to the loan market remains slightly compressed. • More affected outstanding debt in public and private markets may create opportunities for new stressed/distressed and special situations financing strategies.
Core UK Property	• While transaction activity picked up following the easing of the initial lockdown, the market is continuing to face significant uncertainty as restrictions return. • Fundamentals in the UK commercial property market remain weak to reflect to continued downside risk faced as the pandemic rages on while valuation and technical data remains underwhelming.
Long Lease Property	• On an absolute basis, valuations remain less attractive than the wider property market, but they are supported by stronger fundamental and technical drivers.
Conventional Gilts	• Gilt yields remain well below our assessment of longer-term fair value - 3.0-3.5% p.a. for nominal yields. • Economic recovery may drive today's very low yields higher but, while GDP remains below trend and unemployment elevated, 10-year nominal yields may be expected to rise no higher than 1.0-1.5% p.a.
Index-Linked Gilts	• Despite the government's announcement that RPI will be aligned with CPIH (c.1% p.a. lower), with no compensation for index-linked gilt holders, implied inflation actually rose at longer terms as gilt yields rose more than index-linked gilt yields. • Implied inflation looks expensive at terms up to around 25 years.

The table summarises our broad views on the outlook for markets. The ratings used are Positive, Attractive, Neutral, Cautious and Negative. The ratings are intended to give a guide to our views on the prospects for markets over a period of around three years; although they are updated quarterly, they are not intended as tactical calls. The ratings reflect our expectations of absolute returns and assume no constraints on investment discretion. In practice, they need to be interpreted in the context of the strategic framework within which individual schemes are managed.

Source: Hymans Robertson

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.