

Asset class insight: Equity

An in-depth review of the Equity investments held in PruFund. These reviews are updated every six months with the latest details available at the time of publishing.

Introduction

This update from the M&G Treasury and Investment Office (T&IO) provides an insight into the characteristics of the equity portfolios within the PruFund range of funds.

This update covers the standard rather than Planet versions of PruFund. We hope to highlight the key differentiators and strengths including;

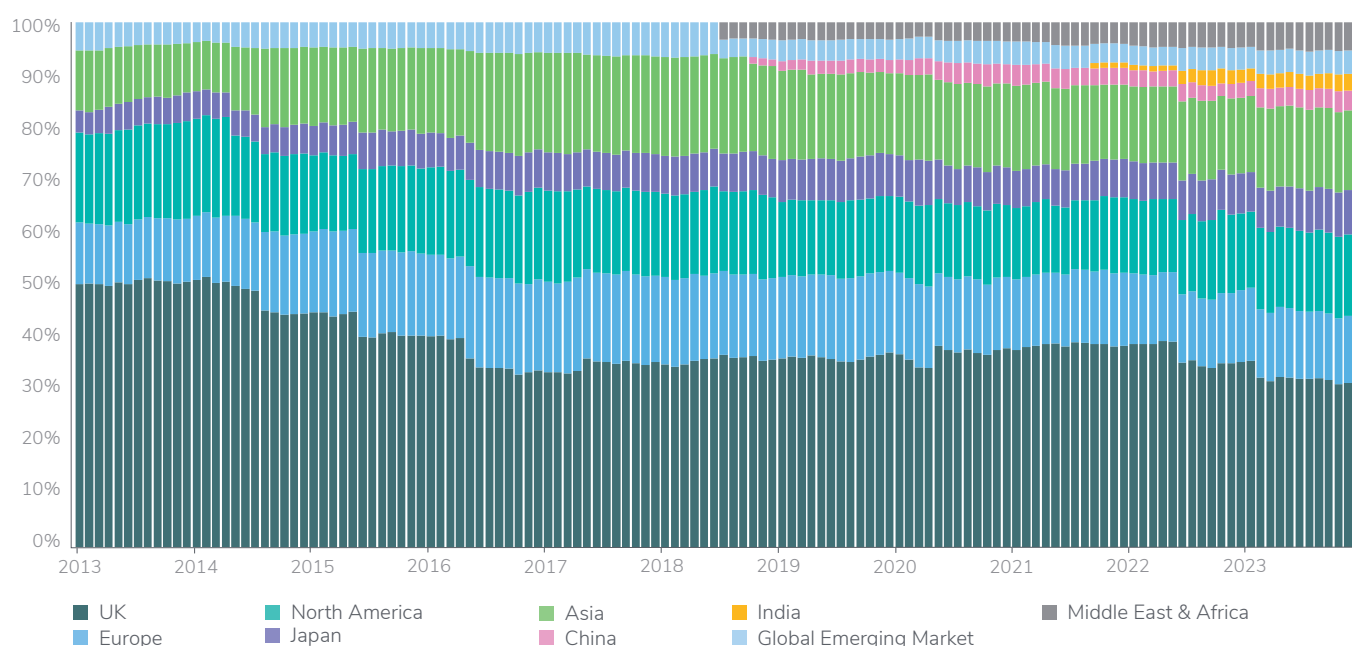
- Global exposure that can be customised based on regional allocations from developed and emerging markets
- Ability to add new asset classes as markets evolve
- Creating bespoke/customised pools of assets or internal funds to best capture opportunities
- Delegating stock selection and sector allocation to well-resourced specialist skilled asset managers

From a regional perspective, PruFunds are well diversified across all the major developed and emerging markets with overseas exposure representing more than 65% of the overall allocation to equities, having diversified more into Asia and Emerging Markets over recent years.

This allocation is informed by the T&IO Long Term Investment Strategy (LTIS) team's forward-looking views on potential growth in the productive capacity for each economy.

The below chart represents the changes in the equity exposure across PruFund Growth over the last ten years and highlights that asset allocation continues to evolve as capital markets evolve. Some key changes in the past ten years include the reduction in UK equities, the addition of Chinese and Indian equities and the growing exposure to Asia and Africa.

Historical equity allocation by region:



Source: T&IO as at 31 December 2023

Characteristics of equity portfolios within the PruFund range of funds

- Globally diversified across all the major developed and emerging markets such as India, Africa and China
- The underlying building blocks are managed by very well-resourced and experienced teams
- Generally, favour larger cap stocks although specific smaller cap exposure has been added to regions like the US, Europe and Japan
- Preference is for active management but passive management when appropriate
- A balanced approach regarding investment styles
 - Different investment styles (growth, value etc). Used to try and benefit from different market conditions
- Large percentage held in bespoke/customised pools of assets or internal funds. This has several benefits such as allowing the T&IO Manager Oversight team to work with fund managers to set guidelines, objectives and risk parameters. Close and collaborative working relationships are formed with managers providing market insights and new investment ideas
- Bespoke/ customised building blocks allows their benchmarks to be broad and diverse, and in some cases can be customised. For example, equally weighted indices to remove bias to mega-caps (e.g., FTSE equally weighted index); capped indices to remove concentration bias or China All Shares to capture both onshore and offshore exposure together
- Different specialist regional equity exposures with varied risk and return profiles. For example, the strategic asset allocation has a direct exposure to the Middle East and Africa as we see significant growth opportunity here driven by favourable demographics and rapidly developing infrastructure.

Portfolio breakdown of PruFund Growth and PruFund Cautious

PruFund Growth

| Asset Class | Fund Name | Investment Style | Internally or Externally managed |
|--------------------------------|--|------------------------------------|----------------------------------|
| UK Equity | M&G UK Absolute Return Fund | Active | Internal |
| | M&G (ACS) UK Listed Mid Cap Equity Fund | Active | Internal |
| | M&G (ACS) BlackRock UK All Share Index Fund | Index Enhanced | External |
| | M&G (ACS) BlackRock UK 200 Index Fund | Index Enhanced/ evenly weighted | External |
| Europe excluding UK Equity | M&G (Lux) European ex UK Equity Fund | Active | Internal |
| | M&G (Lux) Pan-European Smaller Companies Fund | Active | Internal |
| | M&G (Lux) BlackRock Europe ex UK Equity Fund | Index Enhanced | External |
| | M&G European Sustainable Paris Aligned Fund | Active | Internal |
| US Equity | M&G (ACS) BlackRock US Equity Fund | Index Enhanced | External |
| | M&G (ACS) Granahan US Small Cap Growth Fund | Active | |
| | M&G (ACS) Earnest Partners US Small Cap Value Fund | Active | |
| | M&G (ACS) Manulife US Equity Fund | Active | |
| | M&G (ACS) William Blair US Large Cap Equity Fund | Active | |
| | M&G (ACS) MFS US Large Cap Equity Fund | Active | |
| | M&G (ACS) BlackRock Canada Index Fund | Index Enhanced | |
| Japan Equity | M&G (ACS) Japan Equity Fund | Active | Internal |
| | M&G (ACS) Japan Smaller Companies Fund | | |
| Asia ex.Japan Equity | M&G APAC ex Japan Equity Mandate | Active | Internal |
| China Equity | M&G (ACS) China Equity Fund | Active | Internal |
| | M&G (ACS) Value Partners China Equity Fund | Active | External |
| | M&G (ACS) Matthews Asia China Equity Fund | Active | External |
| Global Emerging Markets Equity | M&G Funds (1) GSAM Global Emerging Market Equity Fund | Active | External |
| | M&G Funds (1) MFS Global Emerging Markets Equity Fund | | |
| | M&G Funds (1) Lazard Global Emerging Markets Equity Fund | | |
| Indian Equity | M&G India Equity Mandate | Active | Internal |
| Middle East and Africa Equity | M&G South Africa Equity Fund | Active | Internal |
| | M&G Africa Equity Fund | | |

PruFund Cautious

| Asset Class | Fund Name | Investment Style | Internally or Externally managed |
|--------------------------------------|--|------------------------------------|----------------------------------|
| UK Equity | M&G (ACS) UK Listed Mid Cap Equity Fund | Active | Internal |
| | M&G (ACS) BlackRock UK All Share Index Fund | Index Enhanced | External |
| | M&G (ACS) BlackRock UK 200 Index Mandate | Index Enhanced/ evenly weighted | External |
| Europe excluding UK Equity | M&G (Lux) European ex UK Equity Fund | Active | Internal |
| | M&G (Lux) Pan-European Smaller Companies Fund | Active | Internal |
| | M&G (Lux) BlackRock Europe ex UK Equity Fund | Index Enhanced | External |
| US Equity | M&G (ACS) BlackRock US Equity Fund | Index Enhanced | External |
| | M&G (ACS) Granahan US Small Cap Growth Fund | Active | |
| | M&G (ACS) Earnest Partners US Small Cap Value Fund | Active | |
| | M&G (ACS) Manulife US Equity Fund | Active | |
| | M&G (ACS) William Blair US Large Cap Equity Fund | Active | |
| | M&G (ACS) MFS US Large Cap Equity Fund | Active | |
| | M&G (ACS) BlackRock Canada Index Fund | Index Enhanced | |
| Japan Equity | M&G (ACS) Japan Equity Fund | Active | Internal |
| | M&G (ACS) Japan Smaller Companies Fund | | |
| Asia ex. Japan Equity | M&G APAC ex Japan Equity Mandate | Active | Internal |
| China Equity | M&G (ACS) China Equity Fund | Active | Internal |
| | M&G (ACS) Value Partners China Equity Fund | Active | External |
| | M&G (ACS) Matthews Asia China Equity Fund | Active | External |
| Global Emerging Markets Equity | M&G Funds (1) GSAM Global Emerging Market Equity Fund | Active | External |
| | M&G Funds (1) MFS Global Emerging Market Equity Fund | | |
| | M&G Funds (1) Lazard Global Emerging Markets Equity Fund | | |
| Indian Equity | M&G India Equity Mandate | Active | Internal |
| Middle East and Africa Equity | M&G South Africa Equity Fund | Active | Internal |
| | M&G Africa Equity Fund | | |

Source of underlying holdings data: M&G Treasury and Investment Office as at 29 February 2024.

Underlying equity managers for PruFund

T&IO is responsible for the strategic asset allocation of the PruFund range of funds as well as the selection and ongoing monitoring of the various underlying investment managers. Stock selection is carried out by these investment managers, selected by the T&IO Manager Oversight team following a thorough due diligence process.

There are several factors to consider when allocating to equity markets. Different regional markets require different approaches and skill sets (active, passive, size, style, etc) and the team decide the most appropriate approach.

The below provides an insight into the underlying managers within the equity allocation of the PruFund range of funds.

M&G Investments

The Manager Oversight team believe that there are benefits to using our internal manager, M&G Investments, as long as they meet the required threshold of being in the top quartile of their investment universe.

- Greater accessibility, increasing depth of due diligence
 - Increased transparency, ease of access and continuous interaction allows for deeper due diligence
 - Allows T&IO to have greater conviction on their views
- Greater interaction between T&IO and M&G Investments
 - Ability to react earlier to opportunities within the market by changing the mandate or advanced sight of any potential problems or concerns within the team or strategy
 - New investment opportunities and opportunities to work with the underlying manager for new mandates
- Greater ability to influence the design of mandates
 - Greater flexibility to change mandates to suit T&IO requirements

- For example, reducing/increasing the relative risk of the portfolio, changing individual stock/sector limits and implementing ESG restrictions which are largely already aligned given the Asset Owner/ Asset Manager relationship

- Greater ability to bring about change with a mandate
 - T&IO can, in some cases, enhance or develop a strategy rather than replace a manager, significantly reducing transaction costs
- Competitive fee rates
 - Ability to negotiate better fees when choosing an internal manager

External Managers

T&IO will however select external managers when the internal skillset does not meet the required threshold. Mandates have been awarded to external managers despite the presence of teams within M&G Investments who run such strategies.

BlackRock Regional ESG Optimised Equity

All passive equity mandates are run by BlackRock Solutions after the team worked closely with them to create regional building blocks which will allow T&IO to run their regional Strategic Asset Allocation (SAA) process, aim for an ESG uplift whilst seeking to reflect the risk and return characteristics of the benchmark without sacrificing financial returns. The strategy will:

- take the T&IO's parent index i.e. the index typically utilized as part of the SAA process
- apply the T&IO ESG exclusion policy
- leverage BlackRock's bespoke ESG scoring methodology.

The strategy uses BlackRock's systematic equity dedicated portfolio management team to build an optimized portfolio that provides better ESG scores while targeting only a c.1% tracking error to the parent index.

The funds therefore generate financial returns that are broadly in line with the parent index but with significant ESG enhancement. They access best-in-class systematic equity management from BlackRock and are bespoke to M&G in that they are built to our ESG policy exclusions and can be updated should there be any changes.

Current exclusions include:



Coal



Controversial weapons



Adult entertainment



Global norms violators



Tobacco



Gambling

Other external managers

Although M&G Investments and BlackRock Solutions run the majority of the equity allocation within the PruFund range of funds, various other external managers have been selected:

- US Equity: Granahan Investment Management, EARNEST Partners, William Blair International, MFS Investment Management and Manulife Investment Management
- China Equity: Value Partners and Matthews Asia
- Global Emerging Markets Equity: Goldman Sachs Asset Management, MFS Investment Management, Lazard Asset Management

Summary

T&IO continue to believe the equity allocations within PruFunds are well-diversified and well-placed to add value in continually evolving market conditions. We maintain a UK bias across all asset classes given sterling liabilities but have increasingly moved overseas in the past decade to access an increased opportunity set which has helped maximise risk-adjusted returns.

The longer-term tilt towards Asia remains in place as T&IO foresee a continued shift in the global economic centre of gravity.

Outside of the main regions, T&IO have also built exposure in new areas, like China and India, as markets have evolved, and new fund managers have been selected to implement them.

As well as the long-term strategic positioning of equity portfolios, the team feel that the fundamental, valuation and technical analysis carried out across the whole of M&G, and relevant external managers, will continue to help capture market opportunities over the long-term.

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