

# Equity Investing In PruFunds

(Information is as at 30 June 2022, updated in August 2022, next update will be as at 31 December 2022, updated in February 2023)

## 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;

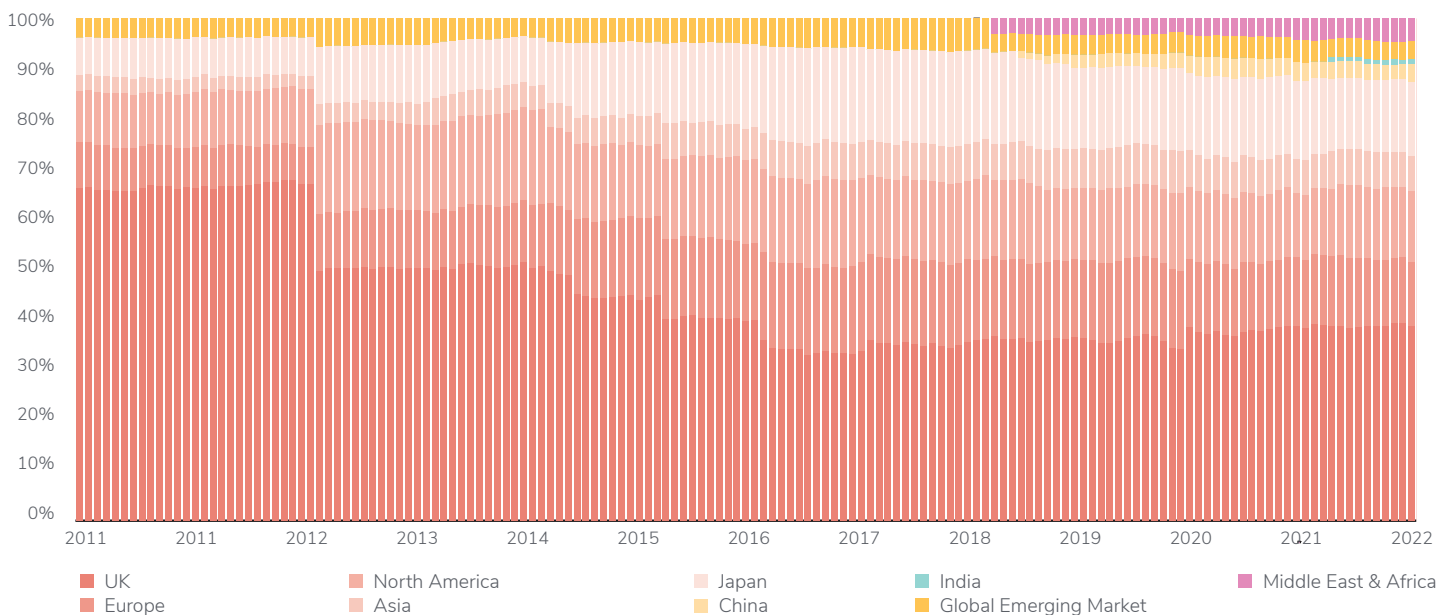
- Global exposure that can be customised based on regional allocations from developed and emerging markets
- Ability to add new asset classes as markets evolve
- Creating bespoke/customised pools of assets or internal funds to best capture opportunities
- Delegating stock selection and sector allocation 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 60% 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 30 June 2022

## Characteristics of equity portfolios within the PruFund range of funds

- Globally diversified across all the major developed and emerging markets
  - Indian, African and Chinese equities added in recent years as direct country allocations as we see them as important emerging/frontier economies
  - The portfolio has more broadly increased its exposure to Asia
- 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, UK, Europe and Japan
- Preference is for active management but passive management when appropriate
  - The US is often a hard market to beat because it is so efficient, which is a function of high analyst coverage. Therefore, a proportion of the US equity allocation is passively managed via an enhanced index vehicle, with extra built-in exclusions from an ESG perspective.
- A balanced approach regarding investment styles
  - Different investment styles (growth, value etc) used to try and benefit from different market conditions
  - Asian markets can be considered less efficient than more developed markets and require additional macro capabilities due to the “multi-country” nature of the region. This also applies to various other equity allocations
  - Operational factors considered, especially when allocating to less liquid markets, or assessing a manager’s ability to access new markets, for example, onshore and offshore Chinese equities
- Large percentage held in bespoke/customised pools of assets or internal funds which has several benefits;
  - The T&IO Manager Oversight team work with the fund managers to set guidelines, objectives and risk parameters
  - The team also form close and collaborative working relationships with fund managers which provides market insights and new investment ideas
  - Benchmarks are 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 bias to concentration or China All Shares to capture both onshore and offshore exposure together
  - Adjustments can be made as markets change and new ones evolve.
  - Adjustments can be made to match manager skillset
  - T&IO will seek to ensure that ongoing fund management costs are competitive
  - Can ensure that the underlying fund manager’s ESG beliefs and policies align with the M&G plc Asset Owner ESG policy
  - Can integrate various exclusions and weightings to certain ESG characteristics, for example working with Black Rock Solutions to create various bespoke equity fund solutions
- Different specialist regional equity exposures with varied risk and return profiles
  - **Asia** – longer-term tilt remains in place as we foresee a continued shift in the global economic centre of gravity
  - **India** – well placed to benefit from a globalisation of services, having been steadily transitioning to a service-led economy for several decades with established players in the global outsourcing space.
  - **China** – bespoke access to world’s 2nd largest economy, still higher potential economic growth than developed markets
  - **Africa** – significant growth opportunity driven by favourable demographics and rapidly developing infrastructure

## Portfolio breakdown of PruFund Growth and PruFund Cautious

### PruFund Growth

Asset	Strategic Asset Allocation		Fund Name	Investment Style	Internally or Externally managed
UK Equity	18.78	2 x segregated mandates 2 x bespoke mandate	M&G UK Absolute Return Fund M&G (ACS) UK Listed Mid Cap Equity Fund M&G (ACS) BlackRock UK All Share Index Fund BlackRock UK 200 Passive Segregated Mandate	Active Active Index Enhanced Index Enhanced / evenly weighted	Internal Internal External External
Europe excluding UK Equity	6.14	3 x bespoke mandates	M&G (Lux) European Active Fund M&G (Lux) European Small Cap Fund M&G (Lux) European Passive Fund	Active Active Passive	Internal Internal Internal
US Equity	6.55	4 x bespoke mandates	M&G (ACS) BlackRock US Equity Fund M&G (ACS) Granahan US Small Cap Growth Fund M&G (ACS) Earnest Partners US Small Cap Value Fund M&G (ACS) Canada Index Fund	Index Enhanced Active Active Passive	External External External Internal
Japan Equity	3.30	2 x bespoke mandates	M&G (ACS) Japan Equity Fund ESI Japanese Smaller Companies Mandate	Active Active	Internal Internal
Asia ex.Japan Equity	7.03	1 x segregated mandate	M&G APAC ex Japan Equity Mandate	Active	Internal
China Equity	1.67	2 x bespoke mandates	M&G (ACS) Value Partners China Equity Fund M&G (ACS) China Equity Fund	Active Index Enhanced	External Internal
Global Emerging Markets Equity	1.71	1 x pooled fund 4 x bespoke mandates	ESI Global Emerging Markets Equity Fund M&G (GSAM) Global Emerging Market Equity Fund M&G (MFS) Global Emerging Markets Equity Fund M&G (INVESCO) Global Emerging Markets Equity Fund M&G (LAZARD) Global Emerging Markets Equity Fund	Active	External External External External
Indian Equity	0.47	1 x segregated mandate	M&G India Equity Mandate	Active	Internal
Middle East and Africa Equity	2.18	2 x pooled funds	M&G South Africa South Africa Unit Trust ESI (PIMSA) Africa Equity Fund	Active Active	Internal internal

Source T&IO and Pru Actuarial team as at 30.06.2022

## PruFund Cautious

Asset	Strategic Asset Allocation		Fund Name	Investment Style	Internally or Externally managed
UK Equity	10.40	4 x bespoke mandates	M&G (ACS) UK Absolute Return Fund	Active	Internal
			M&G (ACS) UK Listed Mid Cap Equity Fund	Active	Internal
			M&G (ACS) UK All Share Index Mandate	Passive	Internal
			M&G (ACS) UK 200 Index Mandate	Passive (evenly weighted)	Internal
Europe excluding UK Equity	3.58	3 x bespoke mandates	M&G (Lux) European Active Fund	Active	Internal
			M&G (Lux) European Small Cap Fund	Active	Internal
			M&G (Lux) European Passive Fund	Passive	Internal
US Equity	4.14	4 x bespoke mandates	M&G (ACS) BlackRock US Equity Fund	Index Enhanced	External
			M&G (ACS) Granahan US Small Cap Growth Fund	Active	External
			M&G (ACS) Earnest Partners US Small Cap Value Fund	Active	External
			M&G (ACS) Canada Index Fund	Passive	Internal
Japan Equity	1.80	2 x bespoke mandates	M&G (ACS) Japan Equity Fund	Active	Internal
			ESI Japanese Smaller Companies Fund	Active	Internal
Asia ex. Japan Equity	4.38	1 x bespoke mandate	M&G APAC ex Japan Equity Mandate	Active	Internal
China Equity	1.17	2 x bespoke mandates	M&G (ACS) Value Partners China Equity Fund	Active	External
			M&G (ACS) China Equity Fund	Index Enhanced	Internal

Asset	Strategic Asset Allocation		Fund Name	Investment Style	Internally or Externally managed
Global Emerging Markets Equity	6.41	1 x pooled fund 4 x bespoke mandates"	ESI Global Emerging Markets Equity Fund	Active	External
			M&G (GSAM) Global Emerging Market Equity Fund		External
			M&G (MFS) Global Emerging Markets Equity Fund		External
			M&G (INVESCO) Global Emerging Markets Equity Fund		External
			M&G (LAZARD) Global Emerging Markets Equity Fund		External
Indian Equity	0.94	1 x segregated mandate	M&G India Equity Mandate	Active	Internal
Middle East and Africa Equity	1.42	2 x pooled funds	PIMSA South Africa Unit Trust	Active	Internal
			ESI (PIMSA) Africa Equity Fund	Active	Internal

Source T&IO and Pru Actuarial team as at 30.06.2022

## 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 responsibility to decide the most appropriate approach also lies with the T&IO Manager Oversight team.

This update introduces some of the underlying managers that the team have selected to manage the underlying equity allocations with the PruFund range of funds and why they have been chosen.

## M&G Investment Management Limited (M&G Investments)

Have built an equities business and reputation around investment integrity, original thinking and innovation.

The team take a conviction led, long-term approach to investing in equities. They believe that company fundamentals, rather than economic cycles or market sentiment, drive prices over time.

- Across asset classes, M&G believes that ESG factors can have a material impact on long-term investment outcomes
- M&G Investments seek to add value for their clients by pursuing an active investment policy through portfolio management decisions, by maintaining a continuing dialogue with company management and by voting on resolutions at investee company general meetings.
- In 2021, M&G's Equities team attended 2,071 company meetings, of which 716 were with the management of UK companies and 1,290 international companies. Source M&G Investments.

## M&G Investments and integrating ESG into their processes

- Across asset classes, M&G believes that ESG factors can have a material impact on long-term investment outcomes
- ESG issues are systematically integrated into company research and portfolio decisions wherever they are material to the investment case
- M&G Investments and integrating ESG – [mg-investments-annual-stewardship-report-2021.pdf](#) (mandgplc.com)

- M&G's Stewardship and Sustainability (S&S) team are advocates of responsible share ownership and oversee the stewardship of the companies in which M&G Investments invest. Regular meetings with M&G's investment teams and company directors allow them the S&S team to identify whether a company's strategy is aligned with M&G's interests as long-term shareholders.

## Global Emerging Markets (GEM) managers

There is clear evidence that skilled managers can differentiate themselves and add value within GEM.

As such, the overall mandate has an alpha target of 2-3% pa. based on a 'core' approach.

As part of the Manager Oversight team's ongoing IDD, a recent review of the GEM equity mandate pointed towards the need for a different approach.

Following a review of the market, and analysis of a shortlist of managers, the decision was taken to allocate the mandate across four complementary 'external' managers, with the preferred structure of two 'core' (style neutral) managers, alongside 'value' and 'growth' satellites.

Transition to the new managers will happen over time to minimise transaction costs.

Core exposure is via two highly rated, but differentiated core funds:

- Goldman Sachs (GSAM) is marginally tilted towards 'growth', and 'size' (small/mid cap bias)
- Massachusetts Investment Management (MFS) has a slight tilt towards 'value'

For the satellite funds:

- Invesco Canada were selected for their depth of coverage and strong stock picking ability, to provide a 'quality growth' style
- Lazard Asset Management brings balance to the overall portfolio with a more 'traditional value' approach.

### **GSAM and integrating ESG**

GSAM state that they provide holistic solutions that are designed to combine the positive impacts of ESG and impact investing with the rigor and risk-return standards of investment management. They believe they have a unique commitment to ESG and impact capabilities with over 40 individuals focused full time on ESG and impact investing.

### **MFS and integrating ESG**

MFS's core purpose is to create value responsibly, a purpose they believe is synonymous with sustainable investing. They believe that incorporating ESG into their investment process is integral to skilled asset management and an essential part of their ability to achieve our clients' objectives. Their goal is for ESG considerations to impact their investment decision-making process in every instance that such factors could materially affect the long-term value of a business. They are convinced that our robust ESG integration framework, carefully considered proxy voting policies and thoughtful issuer engagement improves our ability to achieve their clients' objectives and fulfil their fiduciary duty.

### **Invesco Canada and integrating ESG**

Invesco's ESG approach is based on four key pillars. Firstly they want to be a trusted partner and committed to ESG by incorporating ESG as part of their core investment process. The next two pillars are around being an engaged investor and an active owner which involves voting at shareholder meetings and engaging with the senior management of listed companies to address ESG issues. The final part of their approach is being a solutions led investor around ESG.

### **Lazard Asset Management and integrating ESG**

Lazard believe that unpacking the risks and opportunities created by ESG and sustainability themes requires an active, fully integrated approach. Lazard believe their greatest differentiator is their longstanding commitment to research, which helps them generate forward-looking insights that position their investments ahead of a changing world, rather than reacting to it.

## 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.

*This content has been prepared by M&G Treasury and Investment Office (T&IO) and is prepared for information purposes only and does not contain or constitute investment advice. Information provided herein has been obtained from sources that T&IO believes to be reliable and accurate at the time of issue but no representation or warranty is made as to its fairness, accuracy or completeness. The views expressed herein are subject to change without notice neither T&IO, nor any of its associates, nor any director, or employee accepts any liability for any loss arising directly or indirectly from any use of this document. The value of investments and any income from them may go down as well as up and are not guaranteed. Investors may get back less than the original amount invested and past performance information is not a guide to future performance.*

'M&G Treasury and Investment Office (T&IO)' includes the team formally known as Prudential Portfolio Management Group (PPMG). Prudential Portfolio Management Group Limited, is registered in England and Wales, registered number 2448335.