# WORCESTERSHIRE PENSION FUND

## INVESTMENT STRATEGY STATEMENT

**March 2024**

**Find out more online: www.worcestershirepensionfund.org.uk**

# Contents

## 1. Introduction

This is the Investment Strategy Statement (the 'Statement') of the Worcestershire Pension Fund (the Fund) as required by regulation 7 of the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016 (the "Regulations"). In preparing this Statement, the Pensions Committee has consulted with such persons as it considered appropriate.

Worcestershire County Council is the administering authority for the Fund under the regulations. Worcestershire County Council delegates responsibility for the administration and management of the Fund to the Pensions Committee. The Pensions Committee has oversight of the implementation of the management arrangements for the Fund's assets and comprises of elected members and one employee representative and two employer representatives. In addition, the Fund has a Pensions Board whose role is to assist with good governance by ensuring compliance with statutory and regulatory duty. Finally, the Pensions Investment Sub Committee advises the Pensions Committee on investment issues relating to the Fund. The Pensions Board has no decision-making powers whereas the Pensions Investment Sub Committee does.

The Fund's Strategic asset allocation benchmarks and ranges are shown in Appendix A.

The Statement is subject to review at least annually and from time to time on any material changes to any aspects of the Fund, its liabilities, finances, and its attitude to risk which is judged to have a bearing on the stated investment policy. In preparing this statement, the Committee has considered advice from the Funds independent investment adviser.

The responsibilities of relevant parties are set out in the Governance Policy Statement. Governance Policy Statement

The Funds List of Advisers are set out at Appendix B

The Fund's Statement of Investment Beliefs are set out in Appendix C.

The following are publicly available on the Fund's website:

- Funding Strategy Statement
- Investment Risk Management Statement
- Policy Statement on Communications

## 2. The Fund's Objectives

The primary objectives of the Fund are to:

- Ensure that sufficient assets are available to meet liabilities as they fall due.
- Maximise returns at an acceptable level of risk.

The level of employer contribution is assessed every three years through an actuarial valuation of the Fund. This valuation establishes the solvency position of the Fund, that is, the extent to which the assets of the Fund are sufficient to meet the Fund's pension liabilities accrued to date. The objective is that the Fund should be at least 100% funded on an ongoing basis, taking account of any additional contributions paid by employer bodies to cover any past service deficit. The full funding projection is achieved over a 12-year time frame.

In addition, the Fund has the following objectives:

- To be a leading performer in the LGPS sector
- To provide excellent customer service

The Funding Strategy Statement (FSS) and this Investment Strategy Statement (ISS) are intrinsically linked and together aim to deliver stable contribution rates for employers and a reduced reliance on employer contributions over time.

All Local Government Pension Scheme (LGPS) funds must produce, consult on, and publish a document called a "Funding Strategy Statement" (FSS). The purpose of the FSS is:

- To establish a clear and transparent fund-specific strategy which will identify how employers' pension liabilities are best met going forward.
- To support the regulatory framework to maintain as nearly constant employer contribution rates as possible; and
- To take a prudent longer-term view of funding those liabilities.

However, there will be conflicting objectives which need to be balanced and reconciled. For example, for most employer's objective a) implies low contribution rates, because they would see pension liabilities being "best met" by gaining as much help as possible from the investment strategy over the long term, which would lead you towards an equity-biased investment strategy. By contrast, objectives b) and c) imply stability and prudence of employer contribution rates, which would lead you towards a bond biased investment strategy.

Therefore, the best that can be achieved is a sensible balance between these different objectives.

## 3. Risk

The risk tolerance of the Fund is determined through working with the Pensions Committee, investment managers, officers, and independent advisers to set investment beliefs, funding, and investment objectives. This is incorporated into the Strategic Investment Allocation Benchmark (SIAB), benchmarks and ranges. Risk is monitored by the Pensions Committee using a risk register and risk management tools as advised by the Fund's fund managers, investment advisers and the actuary.

The Fund is exposed to Investment, operational, governance and funding risks. These risks are identified, measured, monitored, and then managed. This is carried out using risk registers with section responsibility and oversight from the Chief Financial Officer.

The principal risks affecting the Fund are as follows:

### 3.1 Funding Risks Liabilities versus the Strategic Investment Allocation Benchmark (SIAB)

- *The risk of deterioration in the funding level of the Fund*. This could be due to assets failing to grow in line with the developing cost of meeting liabilities or economic factors such as unexpected inflation increasing the pension and benefit payments.

  The Fund manages this risk by setting a strategic asset allocation benchmark assisted by the Fund's investment advisor. The strategic asset allocation benchmark seeks to achieve the appropriate balance between generating the required long-term return, while taking account of market volatility and the nature of the Fund’s liabilities. It assesses risk relative to that benchmark by monitoring the Fund’s asset allocation and investment returns relative to the benchmark.

- *The risk of changing demographics* such as improvement in longevity and other demographic factors, increasing the cost of benefits.

  The Fund monitors this by reviewing mortality and other demographic experience and assumptions which could influence the cost of the benefits. These assumptions are considered formally at the triennial valuation.

- *Systemic risk*, i.e., the possibility of failure of asset classes and/or active investment managers results in an increase in the cost of meeting the liabilities.

  The Fund mitigates systemic risk through having a diversified portfolio with exposure to a wide range of asset classes, portfolio holdings and different management styles.

- *Inflation risk*. The Fund mitigates inflation risk through holding a portfolio of growth and inflation linked assets.

  Inflation risk is considered at least triennially in the setting of the SIAB and triennially as part of the actuarial valuation.

- *Future Investment Returns (Discount rate) risk*. The Fund's funding and investment strategies are inter-linked.

  Discount rate risk is mitigated by reviewing them at least triennially in the setting of the SIAB and triennially as part of the actuarial valuation.

- *Currency risk that the currency of the Fund's SIAB underperforms relative to sterling (the currency of the liabilities)*.

  The currency risk of the benchmark is considered at least triennially in the setting of the SIAB. Recommended changes will be expressed through changes in the benchmark and implemented by the investment managers.

### 3.2 Asset Risks (the portfolio versus the SIAB)

- Concentration risk that a significant allocation to any single asset category and its underperformance relative to expectation would result in difficulties in achieving funding objectives.

- Illiquidity risk i.e., that the Fund cannot meet its immediate liabilities because it has insufficient liquid assets.

- Currency risk i.e., that the currency of the Fund's assets underperforms relative to the SIAB.

- Manager underperformance, i.e., when the fund managers fail to achieve the rate of investment return assumed in setting their mandates.

- Responsible Investment (RI) risks, i.e., including climate-related risks, that are not given due consideration by the Fund or its investment managers.

The Fund manages these asset risks by: -

- Constraining how far its investments deviate significantly from the SIAB by setting diversification guidelines and the SIAB strategic ranges.
- Investing in a range of investment mandates each of which has a defined objective, performance benchmark and manager process which, taken in aggregate, constrain risk within the Fund's expected parameters.
- Investing across a range of liquid assets, including quoted equities and bonds; the Fund has recognised the need for some access to liquidity in the short term.
- Robust financial planning and clear operating procedures for all significant activities including regular review and monitoring manager performance against their mandate and investment process.
- Appointing several investment managers, the Fund has considered the risk of underperformance by any single investment manager.
- Actively addressing environmental, social and governance (ESG) risks through implementation of its Responsible Investment (RI) beliefs.

The Fund is aware that investing in overseas equities introduces an element of currency risk, but given the level of diversification within the Fund, the Pensions Committee is comfortable taking this risk in general but may act to mitigate potentially significant risks as and when they are identified.

The Fund invests in accordance with the investment restrictions stipulated by the Local Government Pension Scheme Regulations.

**3.2 Operational Risk**

- Transition risk of incurring unexpected costs in relation to the transition of assets amongst managers.

- When carrying out significant transitions, the Fund takes professional advice and considers the appointment of specialist transition managers to mitigate this risk when it is cost effective to do so.

- Risk of a serious operational failure by asset managers and/or LGPSC

- These risks are managed by having robust governance arrangements with LGPSC and by quarterly monitoring with asset managers.

- Custody risk of losing economic rights to Fund assets, when held in custody or when being traded.

  These risks are managed by use of a global custodian for the custody of assets and formal contractual arrangements for all investments. Where the Fund's investments are pooled through LGPSC, the asset servicer contract includes depositary protection over investment vehicles.

- Risk of unanticipated events such as a Pandemic on normal operations

  These risks are managed by back up arrangements for computer operations, including the ability to work remotely.

- Credit default with the possibility of default of a counterparty in meeting its obligations.

  The Fund monitors this type of risk by maintaining a comprehensive risk register with regular reviews and performing in-depth due diligence prior to making any investment.

- Cashflow management risks.

  As the Fund matures the need for adequate liquidity can become increasingly important. Although its cashflow remains positive after taking into account investment income, managing cashflow is an important consideration in setting the investment strategy. Actions are being taken to manage the cashflow by investing in income-generating assets that continue to produce cashflows such as Property, Infrastructure and fixed income that can be used to meet these payments. The table below sets out the estimated cashflow position of the Fund for the current and following three fiscal years. The cashflow forecast is continually monitored.

| Cashflow Forecast | FY23/24 £'m | FY24/25 £'m | FY25/26 £'m | FY26/27 £'m |
|---|---|---|---|---|
| Opening Balance | 42.5 | 35.9 | 41.3 | 51.1 |
| **Receipts** | | | | |
| Contributions | 152.7 | 159.0 | 159.5 | 166.1 |
| Investment Income | 55.6 | 57.0 | 57.9 | 48.2 |
| Disinvestment | 319.9 | 136.0 | 50.0 | 0.0 |
| Overpaid pension refund | 0.2 | 0.1 | 0.1 | 0.1 |
| Other Receipts | 0.9 | 0.2 | 0.2 | 0.2 |
| Fee Rebate | 0.6 | 0.0 | 0.0 | 0.0 |
| ***Total Receipts*** | 529.9 | 352.3 | 267.8 | 214.6 |
| **Payments** | | | | |
| Benefits Paid | -124.0 | -132.6 | -141.2 | -150.5 |
| HMRC Payments (include Fire) | -15.0 | -16.7 | -17.4 | -18.1 |
| Draw Down notifications | -370.0 | -179.8 | -80.4 | 0.0 |
| Fund Manager Fees / other | -27.4 | -17.8 | -18.9 | -20.0 |
| ***Total Payments*** | -536.5 | -346.9 | -258.0 | -188.6 |
| Closing Balance | 35.9 | 41.3 | 51.1 | 77.1 |



## 4. Investment Strategy

*Funding Policy*

The objectives of the funding policy are expressed in its FSS. The Fund has a strong employer covenant, being funded largely by tax-raising local authorities. Therefore, the Committee can adopt a long-term view, without concern about the ability of its sponsors to meet their liabilities.

Given the on-going restructuring of public bodies the Fund is now maturing increasingly faster. Positive cashflow are declining (although investment income is available if the Fund does go Cashflow negative) and this position is being closely monitored. However, at this time it is not felt necessary to change the investment strategy of the Fund.

Although the Fund has a surplus of assets against liabilities (100.1% funded at the 2022 Triennial Valuation), the Committee wishes to achieve the maximum assistance from investments in maintaining this surplus. This would suggest maintaining a higher risk strategy to generate returns, but this is moderated by the realisation that such a strategy can also lose significant amounts of money in the short-medium term.

It is the Fund's employers who would feel the result of unstable employer rates, and for the precepting authorities, ultimately the local taxpayer either through Council Tax or through service levels. Therefore, another very important consideration is the need for relative stability of investment returns, given that employee rates are fixed by statute and the tools available in the actuarial valuation process for smoothing of returns are limited. This can be achieved by investments that are inherently more stable, such as bonds. However, it is also aided by diversification (so that the ups and downs on particular investments do not arise together), and by seeking returns from both markets ("beta") and investment managers ("alpha") whose returns are skill based and relatively independent of the market. Consequently, the Committee has set an overall investment goal that reflects these four factors.

The Fund's approach to 'Pooling' is detailed in section 9, but alongside this approach the Fund will also consider 're-upping' with existing Fund Managers should these investments meet the Funds key objectives.

The Fund will consider having a shaped equity strategy in place as part of its future investment strategy and use this as a strategic tool to be implemented as and when the need arises.

*Investment Strategies / Pots*

In order that the Fund delivers on its key objectives (ensuring that each employer takes the appropriate level of investment risk, giving each the best opportunity possible to achieve its long-term funding objective whilst increasing certainty of cost), the Fund has introduced three distinct investment strategies (Growth, Medium and Cautious risk). These are detailed in Appendix A

Each investment strategy has its own strategic asset allocation benchmark. The strategic benchmark is consistent with the Fund's views on the appropriate balance between generating the required long-term returns, whilst taking account of market volatility, risk, and the nature of the Fund's liabilities.

The Fund is required to monitor its investment strategy relative to the agreed asset allocation benchmark in order to ensure that it remains consistent with the overall objective. The Fund undertakes a fundamental review of the strategic asset allocation every three years following actuarial valuations. The Fund also monitors compliance with this statement at least quarterly and monitors progress towards the long-term funding objective for relevant groups of employers on a regular basis.

In addition to the fundamental review of the strategic asset allocation undertaken every three years, the Fund monitors the progress of employers within the Growth and Medium Strategies on a regular basis. This gives the Fund the opportunity to adjust the strategic asset allocation in the event that a group of employers are ahead or behind their funding plan.

This is an important mechanism used by the Fund to ensure that each employer continues to take the appropriate level of investment risk, giving each the best opportunity possible to achieve its long-term funding objective whilst increasing certainty of cost. The progress of employers in Cautious Risk Strategy will be monitored every year as these employers are already invested in their “target funding plan”.

A full explanation of the process undertaken to assess employer funding progress is provided in the Fund’s Investment Risk Management document.

*Investment Goal*

The Fund’s investment objective is to achieve a relatively stable “real” return above the rate of inflation over the long term, in such a way as to minimise and stabilise the level of contributions required to be paid into the Fund by employer bodies in respect of both past and future service liabilities.

*Process for ensuring suitability of investments*

The Committee has translated its objectives into a suitable strategic investment allocation benchmark (SIAB) and structure for the Fund (see Appendix A) considering both the liability structure and the objectives set out above. The Fund’s benchmarks are consistent with the Pensions Committee’s views on the appropriate balance between generating a satisfactory long-term return on investments whilst taking account of market volatility and risk and the nature of the Fund’s liabilities. The Investment beliefs in appendix C also assist in formulating the investment strategy.

The Pension Committee monitors investment strategy relative to the agreed asset allocation benchmarks and strategic ranges. If ranges are breached, then appropriate action is taken by the Chief Financial Officer. In addition to ongoing monitoring the investment strategy is formally reviewed annually by Pensions Committee. Furthermore, specific consideration is given to the investment strategy in the light of information arising from each triennial actuarial valuation. The Pension Investment Sub Committee monitors the asset allocation on a quarterly basis.

## 5. Diversification

The Fund is diversified across multiple asset classes with different risk return expectations and correlations to deliver the targeted return of the Fund. Appendix A shows the Strategic Investment Allocation Benchmark (SIAB) and strategic ranges.

## 6. Day-to-day Management of the Assets

### 6.1 Investment management structure

The Pensions Committee retains responsibility for the investment strategy of the Fund but has delegated oversight of its implementation to the Chief Financial Officer. The day-to-day management of the Funds' investments is delegated to the Fund's external investment managers.

### 6.2 External Investment Managers

The Fund has appointed a number of investment managers all of whom are authorised under the Financial Services and Markets Act 2000 to undertake investment business. The investment managers are required to comply with LGPS investment regulations.

### 6.3 Suitable Investments

Subject to the LGPS regulations on allowable investments the Fund may invest in a wide range of assets and strategies including quoted equity, Government and Non-Government bonds, money markets, traded options, financial futures and derivatives, alternative strategies including Infrastructure and property Pooled funds. The fund uses external managers to carry out stock lending ensuring suitable controls/risk parameters are put in place to prevent losses. Where an asset class/strategy is not expected to help in delivering the risk adjusted investment return required it will not be held.

When new asset classes are considered and are not listed above then approval will be sought from the Pensions Committee after receiving advice on its suitability and diversification benefits.

The Fund may also make use of contracts for difference and other derivatives either directly or in pooled funds when investing in these products, for the purpose of efficient portfolio management or to hedge specific risks.

The Fund, after seeking appropriate investment advice, has agreed specific benchmarks with each manager so that, in aggregate, they are consistent with the overall asset allocation benchmarks for the Fund. The Fund's investment managers will hold a mix of investments which reflects their views relative to their respective benchmarks. Within each major market and asset class, the managers maintain diversified portfolios through direct investment or pooled vehicles and a mix of asset types across a range of geographies in order to provide diversification of returns.

### 6.4 Expected Return on the Investments

Over the long-term, it is expected that the investment returns will be at least in line with the assumptions underlying the actuarial valuation (the discount rate). The individual mandates are expected to match or exceed the specific targets set for each portfolio over time.

### 6.5 Investment Restrictions

The investment management arrangements prohibit the holding of investments not defined as 'investments' in the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016. Operating within the investment regulations, the Fund determines investments that are acceptable and approved as such by the Pensions Committee.

### 6.6 Additional Assets

Assets in respect of members' additional voluntary contributions are held separately from the main Fund assets. These assets are held with Scottish Widows and Utmost Life. The Fund monitors, from time to time, the suitability and performance of these vehicles.

### 6.7 Realisation of Investments

In general, the Fund's investment managers have discretion in the timing of realisations of investments and in considerations relating to the liquidity of those investments. The Fund's liquidity characteristics are monitored on a regular basis and the majority of the Fund's investments may be realised quickly if required. A number of the Fund's alternative investments in pooled Infrastructure and property funds, may be difficult to realise quickly in certain circumstances. The Fund will ensure that the liquidity of the investments is suitable to meet future cash flow requirements.

### 6.8 Monitoring the Performance of Fund Investments

The performance of the external investments is independently measured. In addition, officers of the Fund meet external investment managers (both segregated and pooled) regularly to review their arrangements and the investment performance. The Pensions Committee meets at least quarterly to review markets, asset classes and funds.

## 7. Day-to-Day Custody of the Assets

The Fund has appointed a global custodian with regard to the safekeeping of the assets in the Fund and other investment administrative requirements.

## 8. Stock Lending

Stock lending is undertaken in respect of the Fund's quoted equities holdings through the custodian / asset servicer. There is a formal stock lending agreement and approved collateral. Stock lending may also take place in pooled investment vehicles held by the Fund.

For the assets managed by LGPSC on the Funds behalf, LGPSC has an active securities lending programme. To ensure that LGPSC can vote its shares at important meetings, it has worked with service providers to establish procedures to restrict lending for certain stocks and recall shares in advance of shareholder votes. LGPSC monitors the meetings and proportion of the securities on loan and will restrict and/ or recall lent stock in select circumstances, with due consideration to the advantages of voting the shares versus the cost implications of recalling or restricting the loan of the stock.

## 9. Approach to Pooling

The Fund has joined the LGPSC Limited pool with the understanding that the pooled investments will benefit from lower investment costs, greater investment capability and access to more uncorrelated asset classes. Becoming an FCA registered investment manager will lead to improved governance, transparency and reporting giving the Fund assurance that its investments are being carried out effectively.

LGPSC has been set up as an arms-length company, accredited by the Financial Conduct Authority, to manage the pooled investment assets of eight LGPS funds across the centre of England. The Fund is one of the eight partner funds, all of whom hold equal shares in the company. LGPSC started trading on 3rd April 2018 and all partner funds are starting to migrate assets to LGPSC.

The Fund is participating in the pool with the belief that the Fund will benefit from lower investments costs achieved through the aggregation of assets. In addition, the Fund will have greater access to a broader range of investable asset classes, including new and innovative products and services. LGPSC and the partner funds have put in place a robust governance framework to ensure the company operates effectively and delivers timely and transparent reporting to shareholders and client funds.

The Fund will retain full responsibility and control over its strategic investment allocation policy with LGPSC being responsible for implementing the strategy via the engagement and dismissal of managers and the day-to-day monitoring of manager investment performance. Subject to satisfactory due diligence and value for money considerations being satisfied, the Fund intends to continue to invest its assets with LGPSC. Investment strategy will be determined by the Fund with advice from fund managers, operators, and the independent investment adviser.

## 10. Responsible Investment (RI) and Stewardship

**What do we mean?**

Responsible investment is an approach to investment that aims to incorporate ESG factors into investment decisions, to better manage risk and generate sustainable, long-term returns.1 It has relevance both during the selection of an investment and after an investment decision has been made, through on-going stewardship activity which covers considered voting and engagement with investee companies.

Responsible investment is a core part of the Fund's fiduciary duty. It is distinct from 'ethical investment', which is an approach to selecting investments on the basis of ethical beliefs (beliefs about what is morally right and wrong).

Effective management of financially material ESG risks should support the requirement to protect investment returns over the long term. The Fund's investment team seeks to understand relevant ESG factors alongside conventional financial considerations within the investment process, and the Fund's external investment managers are expected to do the same. Non-financial factors may be considered to the extent that they are not detrimental to the investment return.

**ESG factors include:**

**ENVIRONMENTAL**

- Climate risk
- Carbon emissions
- Energy usage
- Raw material sourcing
- Supply chain management
- Waste & recycling
- Water management

**SOCIAL**

- Community relations
- Employee relations
- Health & Safety
- Human rights
- Product responsibility
- Workforce diversity

**GOVERNANCE**

- Board structure
- Executive remuneration
- Bribery and corruption
- CEO/Chair duality
- Shareholder rights
- Vision & business strategy
- Voting procedures



**Stewardship**

We define the concept of stewardship in the same way as the Financial Reporting Council (FRC), the organisation that oversees the UK Stewardship Code which was updated in 2020:

"Stewardship is the responsible allocation, management and oversight of capital to create long-term value for clients and beneficiaries leading to sustainable benefits for the economy, the environment and society".

**Responsible Investment and LGPSC**

From 1 April 2018 the implementation of parts of the Fund's investment strategy has been undertaken by LGPSC, an investment management company set up by 8 Local Authorities (including Worcestershire County Council) in line with the latest scheme regulations. The Fund will seek to ensure that LGPSC is set up to deliver objectives of this RI policy alongside that of the other Funds involved.

LGPSC Limited has developed a Responsible Investment & Engagement Framework (LGPSC Framework) incorporating the investment beliefs and responsible investment beliefs of the eight funds within the LGPSC Limited Pool which will be applied to both internally and externally managed investment mandates. The Fund's investment beliefs can be found in Appendix C.

In collaboration with the eight Partner Funds, LGPSC has identified four themes that will be given particular attention in its ongoing stewardship efforts. The four themes, which will be reviewed after three years, are: Climate change; Single-use plastics; Fair tax payment and tax transparency; and Technology and disruptive industries. The partner funds and LGPSC believe that identifying core themes helps direct engagement and sends a clear signal to companies of the areas that the partner funds and LGPSC are likely to be concerned with during engagement meetings. WPF will monitor closely the effectiveness of LGPSC and their work in this area to support the Fund in its ongoing requirements.

LGPSC also supports the Fund through the annual preparation of a Climate Risk Report which supports the Fund in the preparation of the Fund's Climate-related Financial Disclosure Report prepared in alignment with the recommendations of the Taskforce on Climate-related Financial Disclosures (TCFD).

It is expected that the Fund's ability to invest in a responsible way will be enhanced through LGPSC due to the inherent benefits of scale, collectivism and innovation that will result from being part of the pool. In order to broaden its stewardship activities, LGPSC appointed EOS at Federated Hermes as its stewardship provider, with the remit of engaging companies on ESG issues, and executing the LGPSC Voting Principles which are also the principles agreed by the Fund (see **shareholder voting** below).

***RI Beliefs and Guiding Principles (See Appendix C)***

The Fund's RI Beliefs (see Appendix C) underpin its RI approach. Taking these beliefs as foundational, the Fund has adopted two RI aims: (1) primarily, to support the Fund's investment objectives; (2) secondarily, to be an exemplar for RI within the financial services industry and raise standards across the marketplace.

The Fund intends to realise these aims through actions taken both before the investment decision (which we refer to as the **Selection** of investments) and after the investment decision (the **Stewardship** of investments). Actions will be taken with reference to an evidence base, using the best available objective data sets. We aim to be **Transparent** to all stakeholders and accountable to our clients through regular **Disclosure** of RI activities, using best practice frameworks where appropriate. These ambitions yield the Fund's three RI pillars: Selection, Stewardship and Transparency & Disclosure.

**Climate Change**

The Committee recognises that financial markets will be impacted by climate change and by the response of climate change policy makers. Risks and opportunities related to climate change are likely to be experienced across the whole of the Fund's portfolio. The current understanding of the potential risks posed by climate change, together with the development of climate-related measurements and disclosures, are still at an early stage, and there is considerable variability in the quality and comparability of carbon emission estimates. It is recognised that it will take time for companies to adapt to the changing regulatory and market positions.

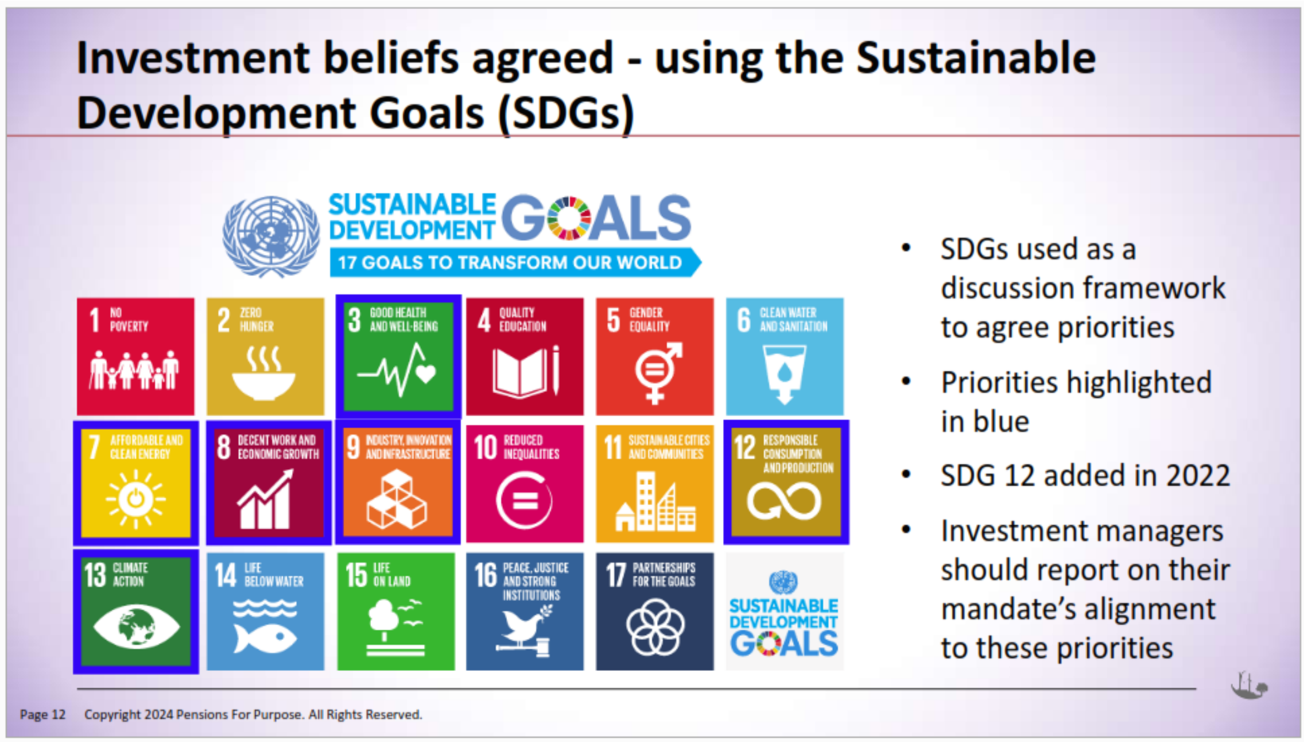
Reflecting the potential material effect of climate change, and the global response to climate change on the assets and liabilities of the Fund, a separate Climate Risk Strategy has been developed, a copy of which can be found on the Fund's website.

**Selection**

The Fund believes that effective management of financially material RI risks should support the Fund's requirement to protect returns over the long term. Investment managers will seek to incorporate RI into their investment process. With regard to climate change risks, the Fund recognises that the scale of the potential impacts is such that a proactive and precautionary approach is needed in order to address them. The Fund considers RI to be relevant to the performance of the entire Fund across asset classes.

There are some investment opportunities arising from environmental and social challenges which can be captured so long as they are aligned with the Fund's investment objectives and strategy.

The Fund believes that *Sustainable economic growth that is done responsibly should support the Fund's requirement to protect returns over the long term*.' The Fund believes that this can be achieved by focussing on the specific United Nations Sustainable Development Goals (SDGs) that the Fund wants to target from an investment perspective. The SDGs are a global footprint for achieving a more sustainable future for everyone. Developed by the United Nations they recognize that ending poverty and other deprivations must go hand-in-hand with strategies that improve health and education, reduce inequality, and spur economic growth. For further information see: https://www.un.org/sustainabledevelopment/. The targeted SDGs are as follows:-




The Fund recognises the need to operate at a market-wide level to promote improvements that will help it to deliver sustainable long-term growth.

- The Fund will set longer-term performance objectives for its investment managers.
- The Fund will seek to ensure that its long-term interests are aligned with that of its investment managers on all issues including on ESG considerations.
- Policies relating to ESG will be considered as part of the Fund's long-term investment planning process, following a thorough and robust investment appraisal.

The Fund will use an **evidence-based** long-term investment appraisal to inform **decision-making** in the implementation of RI principles across our investment strategy to make better more informed investment decisions and encourage / influence better corporate practices that lead to value creation and good risk management and:

- The Fund will consider the potential financial impact of ESG related issues on an ongoing basis (e.g., climate change or executive remuneration).
- The Fund will consider the potential financial impact of investment opportunities that arise from ESG related factors (e.g., investment in renewable energies or housing infrastructure).
- The Fund will consider investment opportunities that have positive impacts and recognises that the changing external environment presents new opportunities i.e., Renewable energy and social impact investments.
- The fund will consider investment opportunities that have positive impacts against the targeted SDGs agreed by the Fund.

**Stewardship**

*Company Engagement and Engagement through Partnership*

Investee companies with robust governance structures should be better positioned to handle the effects of shocks and stresses of future events. The Fund adopts a policy of risk monitoring and engagement with companies on financially material RI issues, in order to positively influence company behaviour and enhance shareholder value; influence that would be lost through a divestment approach. The Fund extends this principle of "engagement for positive change" to the due diligence, appointment, and monitoring of external fund managers.

As part of the external Fund manager monitoring the Fund will request a report on the portfolio's alignment to the Funds targeted Sustainable Development Goals (SDGs) detailed above in the 'Selection' part above and Carbon Risk metrics on an annual basis.

The Fund believes that it will improve its effectiveness by acting collectively with other like-minded investors because it increases the likelihood that it will be heard by the company, fund manager or other relevant stakeholder compared with acting alone. To this end, the Fund uses its membership of the Local Authority Pension Fund Forum (LAPFF) and being a partner to the LGPSC pool to assist it in pursing engagement activities.

The Fund will engage investee companies on issues, including ESG issues that are material to long term value creation and robust risk management in order to safeguard and grow the Fund.

- The Fund is committed to compliance with the UK Stewardship Code1 and working within the spirit of the Principles of Responsible Investment ("PRI").
- We will hold our investment managers to account to ensure compliance with this policy.
- The Fund is committed to collective engagement through its membership of the Local Authority Pension Fund Forum (LAPFF), the LGPSC pool and other opportunities that arise from time to time.
- The Fund will exercise its voting rights in all markets where practicable.

It should be noted that although disinvestment is not currently the Fund's policy, it could be considered in the future if a particular manager or company was not making any attempt to comply with our Fund's stated policies.

**Shareholder Voting**

On the 21st of June 2019 the Pensions Committee agreed that LGPSC would via EOS vote shares in certain discretionary and pooled funds on the Fund's behalf. These principles were updated in March 2023 and votes will be executed in line with LGPSC's published **Voting Principles**. The Fund believes that the advantage of a consistent signal and working collectively through the pool will have a positive influence on company behaviour.

Shares held in passively managed portfolios will be voted according to the voting policies of the Fund's appointed fund manager, Legal & General Investment Management (LGIM). The Pension Committee is satisfied that LGIM's approach to shareholder voting is sufficiently robust and aids in the delivery of the Fund's RI objectives.

**Transparency & Disclosure**

The Fund is fully committed to the new enhanced UK Stewardship Code which was introduced in 2020 and the Fund has been a successful Tier 1 signatory of the Financial Reporting Council's UK stewardship code since 2020.

LGPSC provides quarterly reporting for all funds managed by LGPSC detailing how votes have been cast in different markets and a vote-by-vote disclosure for full transparency. Engagement and voting disclosure is also done specifically for listed securities held across the Fund's portfolios.

**How Will We Monitor our Performance on Responsible Investment?**

The Fund will ultimately be **transparent and accountable** in terms of its performance on Responsible Investment. This will be achieved through the following approach:

- The Fund will publish its Investment Strategy Statement and its Climate Risk Strategy on its website in line with the scheme regulations.
- Decisions relating to the setting of investment policy will be explained.
- The Fund will monitor closely its appointed investment managers whom the Fund rely on to implement its RI policy.
- The Fund will undertake an annual review of corporate governance, voting and engagement activity undertaken by the Fund and its underlying managers.
- The Fund will publish an annual summary of voting and engagement activity.
- The Fund will ensure that its decision makers are properly trained and kept abreast of ESG issues to make informed decisions.
- The Fund will include ESG as standing item on Pensions Investment Sub Committee (or equivalent) agendas (with a view to reporting on manager performance in relation to ESG investing and noting any hot topics / issues arising).
- The Fund will undertake a fundamental review of any specific ESG issues that are considered by the Pension Investment Sub Committee to be of potentially material financial impact.

- The Fund will consider and respond to feedback from stakeholders in relation to issues of concern.
- Reporting annually using the recommendations of the Taskforce on Climate-related Financial Disclosures (TCFD)
- The Fund will request External Fund managers to report on their portfolio's alignment to the Funds targeted Sustainable Development Goals (SDGs) detailed above under 'Selection' and Carbon Risk metrics on an annual basis.

## 11. Compliance with This Statement

The Fund will monitor compliance with this statement. It will ensure its investment decisions are exercised with a view to giving effect to the principles contained in the statement, so far as is reasonably practicable.

# Appendix A – Strategic Allocation Investment Benchmark and Ranges

| | Growth | Medium | Cautious | |
|---|---|---|---|---|
| **Asset Allocation** | **%** | **%** | **%** | **Manager, Method & Performance Target** |
| **Actively Managed Equities** | | | | |
| Far East Developed | 10.0 | 5.0 | 0.0 | Nomura Asset Management - FTSE All World Asia Pacific Index + 1.5% |
| Emerging Markets | 10.0 | 5.0 | 0.0 | LGPSC active global emerging markets equity mandates with BMO, UBS and Vontobel - FTSE - Emerging Market Index +2.0% |
| LGPSC Global Sustainable | 6% | 3% | 0.0 | LGPSC active Global Sustainable equity mandates with Liontrust and Baillie Gifford - FTSE – All World +2.0% to 3% |
| **Passively Managed Equities - Market Capitalisation Indices** | | | | |
| United Kingdom | 12.0 | 9.0 | 0.0 | Legal and General Asset Management - FTSE All Share Index |
| North America | 11.5 | 9.0 | 0.0 | Legal and General Asset Management - FTSE All World North America - Developed Series Index |
| Europe ex - UK | 5.5 | 4.0 | 0.0 | Legal and General Asset Management - FTSE All World Europe ex UK Index - Developed Series Index |
| **Passively Managed Equities – Alternative Indices** | | | | |
| Global | 15.0 | 5.0 | 0.0 | Legal and General Asset Management:<br>60% STAJ - CSUF - STAJ MF36726/36727 (Quality Factor)<br>40% LGPSC All World Equity Multi Factor Climate Fund |
| **Fixed Income** | | | | |
| Fixed Income | 10.0 | 40.0 | 80.0 | - LGPSC Global Active Investment Grade Corporate Bond (Fidelity & Neuberger Berman) - Fund 50% GBP IG Corporate (Ex EM Issues) / 50 % Global IG Corporate ((ex IG Corporate & EM Issues) hedged to GBP +0.80%<br>- Bridgepoint Corporate Private Debt |

| | | | | |
|---|---|---|---|---|
| **Actively Managed Alternative Assets** | | | | |
| Property, Infrastructure & Private Equity | 20.0 | 20.0 | 20.0 | Through a mix of Macquarie (was Green Investment Bank), Invesco, Hermes, Walton Street, Venn Partners, Stonepeak, Igneo (was First Sentier), AEW, Gresham House, LGPS Central etc |
| **TOTAL** | **100.0** | **100.0** | **100.0** | |

NOTE:

As part of its 2022 Strategic asset allocation (SAA) review, the Fund agreed to allocate up to 5% to Private Equity. The mechanism to achieve that allocation will involve using the flexibility within the strategic asset allocation tolerance ranges, illustrated below. This will be formalised in the next SAA review in 2025.

## Tolerance Ranges

| Asset Type | Growth | Medium & Cautious | Role (s) within the Strategy |
|---|---|---|---|
| **Equities** | **+/- 5%** | **+/-2.5%** | Deliver long term growth above inflation and generate investment income i.e., dividends. |
| **Growth Fixed Income** | **+/- 5%** | **+/-2.5%** | Provide protection from changes in real yields both in terms of capital value and income |
| **Property** | **+/- 5%** | **+/-2.5%** | Diversification; generate investment income; provide some inflation-sensitive exposure; illiquidity premium |
| **Infrastructure** | | | Provides the Fund with access to a diversified (but long term, illiquid) return and a stream of inflation related income |
| **Index Linked Gilts** | **+/- 5%** | **+/-2.5%** | Provide protection from changes in real yields both in terms of capital value and income |
| **Diversified Growth / Multi Asset** | **+/- 5%** | **+/-2.5%** | Diversification and dynamic asset allocation |

# Appendix B - Advisers as at March 2024

## External Investment Advisors

**Philip Hebson**, Independent Investment Advisor

Investment policy, general investment matters.

## Actuary

**Hymans Robertson LLP**

Actuarial matters

## Custodian

Bank of New York Mellon

Custodial services, Stock lending.

## Other External Advisors

**Local Authority Pension Fund Forum (LAPFF)**

Company governance issues

**Pensions For Purpose**

Governance and ESG matters

**Hymans Robertson LLP**

Fund investment performance

## Appendix C - Statement of Investment Beliefs

The Fund's investment beliefs outline key aspects of how it sets and manages exposure to investment risk. They are as follows:

**Financial Market Beliefs**

- There exists a relationship between the level of investment risk taken and the rate of expected investment return. As taking calculated risks does not guarantee returns, investment losses or below expected returns are possible outcomes.
- Markets are dynamic and are not always efficient, and therefore offer opportunities for skilled active managers.
- In making investments in illiquid assets, a return premium should be sought.
- Diversification is a key technique available to institutional investors for improving risk-adjusted returns.
- The Fund believes that investing for the long term can add value, as it allows the fund manager to focus on long term value and use short term volatility to establish favourable investments.
- Where an asset class/strategy is not expected to help in delivering the risk adjusted investment return required it should not be held.

**Investment Strategy/Process Beliefs**

Clear investment objectives are essential. Return and risk should be considered relative to the Fund's liabilities, funding position and contribution strategy.

Risk should be viewed both qualitatively and quantitatively. Focus should be given to the risk of loss and also to the nature and likelihood of extreme events so that the Fund is not a forced seller of assets.

- Strategic asset allocation is a key determinant of risk and return, and thus is typically more important than manager or stock selection.
- Listed Equities are expected to generate superior long-term returns relative to Government bonds and our beliefs in this Listed Equities are expanded below:
  - Passively managed market cap-based investment has a balancing role to play in most pension schemes' equity allocations, bringing liquidity, transparency and reducing average fee levels.
  - Market cap weighted indices have their drawbacks; adding carefully selected systematic, factor tilted equity strategies can improve risk-adjusted returns, benefiting from disciplined rebalancing (the "rebalancing premium").

   i. Exposure to "valuation factors" can improve risk adjusted returns over time. Even if outweighed by technical factors in the short-term, diversified exposure to valuation-based factor tilts can add excess return per unit of risk over a reasonable timeframe.

   ii. Exposure to the "low volatility factor" can reduce absolute equity volatility and improve risk-adjusted returns. Strategies can be implemented which manage downside risk while achieving market returns over time.

   iii. Exposure to the "small size factor" can improve risk-adjusted returns. A diversified tilt towards medium and smaller sized businesses is generally rewarded over time.

   iv. Carefully selected exposure to actively managed growth strategies can improve the balance of overall equity exposure and improve risk adjusted returns.

  - Exposure to emerging markets provides diversification and the opportunity for higher returns due to the higher risk premium typically earned for investing in these markets.

  - With sufficient research and governance, active equity management can be incorporated to add value relative to market cap weighted indices; overall active equity exposure should be focused predominantly on stock-specific risk.

  - Currency exposure associated with investing in equities can add volatility. Whilst it can be desirable to retain exposure to some currencies, hedging a proportion of non-domestic currency exposure can reduce the volatility of equity investing.

- Alternative asset class investments are designed to further diversify the portfolio and improve its risk-return characteristics.

- Active management can add value over time, but it is not guaranteed and can be hard to access managers who consistently out-perform the relevant benchmark. Where generating 'alpha' is particularly difficult, passive management is preferred.

- Operational, counterparty, conflicts of interest and reputational risk need assessment and management, in addition to investment risk.

- Concentrated portfolios (smaller numbers of holdings or less external managers) allow for greater investment focus, lower investment costs, and enable more focused engagement with Responsible investment.

- Managing fees and costs matter especially in low-return environments. Fee arrangements with our fund managers – as well as the remuneration policies of investee companies – should be aligned with the Fund's long-term interests.

**Organisational Beliefs**

- Effective governance and decision-making structures that promote decisiveness, efficiency and accountability are effective and add value to the Fund.

- When outperformance of a desired benchmark is not possible the fund will use index funds, financial instruments, or proxies (Investments that share similar characteristics) to gain exposure to the asset class in the most cost-effective way.

- Investment costs are necessary to generate outperformance in asset classes where outperformance is achievable. Investment costs are a certain cost that should be fully transparent and managed by the operator in the best interests of the pension Fund.

**Responsible Investment Beliefs**

**Long termism**

A long-term approach to investment will deliver better returns and the long-term nature of the Fund's liabilities allows for a long-term investment horizon.

**Sustainability**

The Fund believes that *Sustainable economic growth that is done responsibly should support the Fund's requirement to protect returns over the long term*.' The Fund believes that this can be achieved by focussing on the specific United Nations Sustainable Development Goals (SDGs) as follows:-

- ***Economic Goals***
    - SDG 8. Decent Work and Economic Growth
    - SDG 9. Industry, Innovation & Infrastructure
    - SDG 12 Responsible Consumption and Production
- ***Climate Goals***
    - SDG 7. Affordable and Clean Energy
    - SDG 13. Climate Action
- ***Health Goal***
    - SDG 3 Good Health and Wellbeing

**Responsible investment**

Responsible investment is supportive of risk adjusted returns over the long term, across all asset classes. Responsible investment should be integrated into the investment processes of the Fund and its investment managers.

**Investing with impact**

The Fund will consider opportunities to make investments with a positive social or environmental impact subject to the risk and return characteristics being acceptable. Investments expected to have a "positive impact" can be considered if they are consistent with the overall objectives of the Fund's investment strategy.

**Diversification, risk management and stewardship:**

Diversification across investments with low correlation improves the risk return profile. A strategy of engagement, rather than exclusion, is more compatible with fiduciary duty and more supportive of responsible investment, because the opportunity to influence companies through stewardship is waived in a divestment approach. Even well diversified portfolios face systematic risk. Systematic risk can be mitigated over the long-term through widespread stewardship and industry participation.

**Corporate governance and cognitive diversity:**

Investee companies and asset managers with robust governance structures should be better positioned to handle the effects of shocks and stresses of future events. There is clear evidence showing that decision making, and performance are improved when company boards and investment teams are composed of cognitively diverse individuals.

**Fees and remuneration:**

The management fees of investment managers and the remuneration policies of investee companies are of significance for the Fund, particularly in a low return environment. Fees and remuneration should be aligned with our long-term interests, and value for money is more important than the simple minimisation of costs.

**Risk and opportunity:**

Risk premia exist for certain investments; taking advantage of these can help to improve investment returns. There is risk but also opportunity in holding companies that have weak governance of financially material ESG issues. Opportunities can be captured so long as they are aligned with the Fund's objectives and strategy, and so long as there is a sufficient evidence base upon which to make an investment decision.

**Climate change[1]:**

Financial markets could be materially impacted by climate change and by the response of climate policymakers. Responsible investors should proactively manage this risk factor through stewardship activities, using partnerships of likeminded investors where feasible. See also the Funds separate Climate Risk Strategy

[1]*By highlighting climate change, rather than other RI risk factors, we are not asserting that climate risk has, for all assets, greater economic significance than other factors. Our motivation for referring specifically to climate change risk derives from our recognition that it is a risk factor of particular importance to several stakeholders, and we have communicated our investment beliefs about climate change for reasons of transparency.*