

**RHONDDA CYNON TAF PENSION FUND**

**INVESTMENT STRATEGY STATEMENT**

**1. Overall Responsibility**

Rhondda Cynon Taf County Borough Council is the designated statutory body responsible for administering the Rhondda Cynon Taf Pension Fund on behalf of the constituent Scheduled and Admitted Bodies. The Council is responsible for setting investment policy, appointing suitable persons to implement that policy and carrying out regular reviews and monitoring of investments.

The Council has created a politically balanced Pension Fund Committee consisting of elected members to oversee the Council's responsibility with regard to the administration of the Pension Fund. This committee is responsible for the strategic management of the Pension Fund

The Council has appointed the Group Director - Corporate and Frontline Services as the officer with Section 151 responsibilities to exercise delegated powers to make decisions in respect of operational matters of the Pension Fund investments and administration. An Investment and Administration Advisory Panel has been formed to support him in this capacity. This is made up of:

- The Deputy Section 151 Officer
- Head of Finance (Education and Financial Reporting)
- Head of Service (Pension, Payroll and Payments)
- Principal Accountant, Treasury and Pension Fund Investments
- Senior Accountant, Treasury and Pension Fund Investments
- Independent Advisors

Both the Committee and the Panel meets quarterly. The Council is not strictly a trustee (technically, this is the Ministry for Housing, Communities and Local Government) but acts in a quasi - trustee role.

In accordance with the requirements of the Public Service Pensions Act 2013, a Pensions Board has been established in order to assist Rhondda Cynon Taf C.B.C. as "Scheme Manager" with achieving effective and efficient governance and administration of the Rhondda Cynon Taf Pension Fund.

The role of the Pension Board as defined by sections 5(1) and 5(2) of the Public Service Pensions Act 2013, is to assist Rhondda Cynon Taf County Borough Council Administering Authority as Scheme Manager to: -

- Secure compliance with the Principal Regulations and any other legislation relating to the governance and administration of the LGPS;
- Secure compliance with the requirements imposed in relation to the LGPS by the Pensions Regulator; and
- Ensure the effective and efficient governance and administration of the LGPS by the Scheme Manager.

The Pension Board will provide oversight of the above matters and accordingly it is not a decision making body in relation to the management of the Fund itself.

Full details of governance arrangements can be found on the following link:  
[Governance Policy](#)

## **2. Primary Objective**

The Fund's objective is to provide for members' pension and lump sum benefits on their retirement or for their dependants' benefits on death before or after retirement, on a defined basis in accordance with LGPS regulations.

## **3. Funding Objectives**

Rhondda Cynon Taf C.B.C. should manage the Fund in such a manner that, in normal market conditions, all accrued benefits are fully covered by the actuarial value of the Fund's assets and that an appropriate level of contribution is agreed by the Authority to meet the cost of future benefits arising.

The Funding Strategy Statement and the Investment Strategy Statement are intrinsically linked and together aim to deliver stable contribution rates for employers.

The investment objective is to maximise returns subject to an acceptable level of risk whilst increasing certainty of cost for employers, minimising long term cost.

The Fund's objective is to achieve a return on Fund assets which is sufficient, over the long-term, to meet the funding objectives on an ongoing basis.

The Group Director – Corporate and Frontline Services supported by the Investment and Administration Advisory Panel will ensure that one or more investment managers are appointed who are authorised under the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016 to manage the assets of the Fund. Contracts / mandates are in place giving instructions to the Managers as to how the investment portfolio is to be managed.

The Pension Fund Committee having taken account of advice from the Group Director – Corporate and Frontline Services may give specific directions as to the strategic asset allocations and will ensure the suitability of assets in relation to the needs of the Fund. The investment managers (each of which will have a benchmark and target to reflect their mandate) will be given full discretion over

the choice of individual stocks and will be expected to maintain a diversified portfolio within the restrictions specified in each mandate.

#### **4. Diversification Policy : Requirement to invest fund money in a wide variety of investments**

The fund invests in a range of asset classes to help reduce overall portfolio risk. This will ensure that if a single asset class is not performing well, this underperformance is balanced by other better performing assets at that time. The portfolio is also diversified to reduce volatility in performance.

The fund is diversified into the following asset classes:

- Equities
- Bonds
- Property
- Cash

The Fund commissioned an Asset / Liability review in 2017, the fundamental aim of which was to position the Fund's investments in order to :-

- Reduce risk
- Maintain (as far possible) return expectations
- Minimise long term costs
- Increase diversification
- Optimise the transitioning of assets into the Pool
- Infrastructure (align to Pool aspiration)

thus ensuring the pension Fund is being invested in the most efficient way.

Aon Hewitt was appointed to give their view on the risk/return of the Pensions Fund's current investment strategy. Following on from this they were requested to comment and recommend alternative constructs that could deliver the Fund's long term objectives.

Using a computerised model approach, simulations were undertaken for different portfolio asset strategies. The model estimated the probability of achieving a variety of funding outcomes over different time periods given the current asset allocation strategy. The majority allocation to equities in the portfolio gave a potentially high return, but was also the most significant contributor to overall risk.

Alternative asset allocation strategies were reviewed as a potential means of increasing diversification and reducing risk. Options were reviewed by the Panel and Committee. It was noted that the Rhondda Cynon Taf Pension Fund was not particularly high risk compared to other LGPS funds and that some of the potential alternatives resulted in entering into asset classes that were expensive and difficult markets to enter.

The Committee concluded that the Fund should move toward the following asset allocation strategy with steps set out to achieve the desired allocation.

Asset Class	Current Allocation	Proposed Step 1	Proposed Step 2	Proposed Step 3
		Current Benchmark	Strategy (1)	Strategy (2)
<b>Total Equities</b>	<b>74.80%</b>	<b>63%</b>	<b>63%</b>	<b>58%</b>
<b>Total Alternatives</b>	<b>5.40%</b>	<b>10%</b>	<b>20%</b>	<b>25%</b>
Absolute Return Bonds			10%	10%
Infrastructure				5%
Property	5.40%	10%	10%	10%
<b>Total Bonds &amp; Cash</b>	<b>19.80%</b>	<b>27%</b>	<b>17%</b>	<b>17%</b>
Fixed Interest	8.50%	12.50%	7.50%	7.50%
UK Corporate Bonds	9.40%	12.50%	7.50%	7.50%
Cash	1.90%	2%	2%	2%

Following the above, the target and maximum percentages of total value of all investments that we will invest in particular investments or asset classes was as follows:

Asset Class	Target % of Fund	Max. % of Fund
Equities	58%	75%
Fixed Interest (Bonds)	15%	25%
Absolute Return Bonds	10%	15%
Property	10%	15%
Infrastructure	5%	10%
Cash	2%	5%

The above target forms the basis of a customised benchmark which the Fund's performance is monitored against. The customised benchmark moves in line with market volatility. The asset allocation of the portfolio is not rebalanced on a routine basis but is reviewed annually to ensure the target return is not adversely impacted.

We may not permit more than 5% of the total value of all investments of fund money in entities which are connected with the Authority in line with Section 212 of the LG and Public Involvement in Health Act 2007.

In assessing the diversification policy, the Fund will consult with independent advisors.

##### **5. Asset Allocation Policy : Assessment of the suitability of particular investments and types of investments**

Investments are selected with their suitability to meet the fund's overall objective of meeting pension obligations as they fall due. The level of return required is informed by the triennial actuarial valuation.

In the long term, low volatility assets such as gilt edged investments behave in a similar manner to pension liabilities and would therefore "match" the attributes of

pension obligations. However the requirement to achieve a longer term higher rate of return is, on average, achieved by other classes of assets such as stocks or property.

The current portfolio has been constructed with actuarial and independent advisor advice to achieve a specified level of return within risk parameters.

A management agreement is in place for each investment manager which sets out the relevant benchmark, performance target, asset allocation ranges and any restrictions as determined by the Pension Fund Committee.

The following demonstrates the allocation of the Fund as at March 2018 :-

	<b>% of Fund Invested</b>
UK Equities	20%
Overseas Equities	
US	25%
Continental Europe	13%
Other Int'l Equities	16%
Total Bonds	18%
Property	5%
Cash & Deposits	3%

The Pension Fund Committee has agreed not to invest in private equity at the present time.

The Pension Fund Committee has agreed not to stock lend at the present time.

The Asset Allocation Strategy is reviewed annually to ensure that returns, risk and volatility are managed and consistent with overall investment strategy.

**6. Policy On Risk : Approach to risk, including the ways in which risks are measured and managed**

The Fund maintains a Risk Register that is agreed by the Investment and Administration Advisory Panel and reported to the Pensions Board and Pensions Committee on a quarterly basis. The risk register examines funding, investment, operational, governance and regulation issues, ranks risks in terms of likelihood and impact and details mitigation measures.

**Investment Risk**

This covers items such as the performance of financial markets and the Fund's investment managers, asset reallocation in volatile markets, leading to the risk of investments not performing (income) or increasing in value (growth) as forecast. Examples of specific risks would be:

- assets not delivering the required return (for whatever reason, including manager underperformance)
- systemic risk with the possibility of interlinked and simultaneous financial market volatility
- insufficient funds to meet liabilities as they fall due
- inadequate, inappropriate or incomplete investment and actuarial advice is taken and acted upon
- counterparty failure

The specific risks associated with assets and asset classes are:

- equities – industry, country, size and stock risks
- fixed income - yield curve, credit risks, duration risks and market risks
- alternative assets – liquidity risks, property risk, alpha risk
- money market – credit risk and liquidity risk
- currency risk
- macroeconomic risks

The adoption of an asset allocation benchmark and the monitoring of performance relative to a performance target constrains the investment managers from deviating significantly from the intended approach, while permitting flexibility to manage the Fund in such a way to enhance returns.

The overall investment objective is to maximise investment returns and to minimise employer contributions over the long term within agreed risk tolerances.

The requirement is to move towards 100% funding over a period of time. The funding level is calculated triennially, following an actuarial review.

The Fund's assets are managed on an active basis (except the Global Passive Equity mandate) and are expected to outperform their benchmarks over the long term. In this way the investment performance achieved by the Fund is expected to exceed the rate of return assumed by the Actuary within the valuation.

The Fund's investment managers have been given weighted average benchmarks and targets to reflect their mandates. Both asset allocation and stock selection is monitored. The current targets for each mandate are as follows:-

<b>Portfolio</b>	<b>Portfolio Benchmark Index</b>	<b>Portfolio Target</b>
Traditional equity manager	UK - FTSE All Share US – FTSE All World Europe – FTSE All World Europe Far East – FTSE All World Developed Asia Other Intl – MSCI Emerging Index	Composite Index +1% pa over rolling 3 year period
Global passive equity manager	FTSE A W All World	Index
Global high alpha managers	MSCI All Countries World Index	Index + 2% over rolling 3 year period
UK equity high	FTSE All Share Index	Index +2%

alpha managers		over rolling 3 year period
Fixed Interest Manager	UK Govn Bonds – FTS UK Govn All Stocks UK Corporate – IBoxx GBP Non Gilts	Composite Index +0.5% pa over rolling 3 year period
Property Manager	CPI	Index +4.5%

Review of the investment managers is ongoing based on the quarterly and annual performance data supplied to the Panel by external performance management agencies.

The appointment of more than one investment manager introduces diversification of manager risk as discussed above.

Each manager is expected to maintain a diversified portfolio of investments and adhere to restrictions imposed within their agreement.

Fund Managers also have investment restrictions as follows:



### Investment Restrictions per Mandate

	Total Gov. Bond Expos. Min 30% Max 70%	Non Gov Exp min 30% max 70%	Over-seas Exp 30% limit	Max. Hold'g of 15% on pooled vehicles	Max. 10% in any one single hold'g	Max. of 10% held in cash	Max. of 5% held in cash	No single overs's equity exceed 5% of total value of fund	Max. holding of 25% in trust scheme	Max 25% in Emerg Markets	Max. holding of 25% in OEIC scheme	Max. 10% in any overseas holding (added jan 16)
<b>BMOGAM Bonds</b>	X	X	X	X								
<b>Baillie Gifford Traditional</b>					X	X		X	X			
<b>Baillie Gifford High Alpha</b>					X	X			X			
<b>Newton High Alpha</b>					X				X	X		
<b>BlackRock UK Equity</b>					X				X		X	X
<b>Invesco UK Equity</b>	NO LIMITS AS POOLED FUND											
<b>Blackrock Passive Eqs</b>	NO LIMITS AS POOLED FUND											
<b>CBRE Property</b>					X		X					



The performance of both markets and managers is reviewed regularly by the Investment Advisory Panel, which has the appropriate skills and training required to undertake this task. The Panel is also supported by Independent Advisors providing advice to enable the Panel to robustly fulfil its functions.

## **7. Approach to pooling investment, including the use of collective investment vehicles and shared services.**

The Wales Pension Partnership (WPP) has appointed Link Fund Solutions Ltd (Link) to establish and run a collective investment vehicle for the sole use of the LGPS funds in Wales. This will enable the pooling of assets across a range of asset classes.

Link have established and will run an Authorised Contractual Scheme (a tax efficient UK collective investment vehicle) on behalf of the WPP. The ACS will have sub-funds in a range of asset classes that will meet the needs of the LGPS funds in Wales, to allow them to execute their differing asset allocation strategies.

With the support of Russell Investments, and in consultation with the eight individual LGPS funds, Link have begun the process of appointing a number of investment managers. The LGPS funds will retain full control over strategic asset allocation decisions. Northern Trust will have custodian duties.

By using fewer investment managers with larger mandates, it is expected that the WPP will deliver fee savings, one of the primary aims of Government policy. A summary of the pooling objectives of the WPP are:

- Generate consistent net of fee excess returns.
- Diversify manager risk.
- Reduce average manager fees.
- Achieve tax efficiency by reclaiming withholding tax on dividends (for non-UK equity sub-funds).
- Equitably share the costs of transitioning into sub-funds.

Progress continues to be made by the Wales Pension Partnership (WPP) in the establishment of the first two sub funds for the collective investing of assets. The prospectus for Global High Alpha Equities, comprising 2 sub funds with differing risk / return characteristics, has been approved by the FCA (24<sup>th</sup> July 2018). The proposals for the second sub fund for UK and European Equities was agreed by the Joint Governance Committee on the 25<sup>th</sup> September 2018. The third phase relates to Fixed Interest with options in the process of being reviewed.

**8. How social, environmental and corporate governance considerations are taken into account in the selection, non-selection, retention and realisation of investments.**

The overriding principle of the Fund's investment policy is to obtain the best possible financial return using the full range of investments authorised under the Local Government Pension Scheme regulations.

Although the pursuit of a financial return is our predominant concern, where possible, the Fund is committed to include Responsible Investment factors (environmental, social and corporate governance factors) into the investment process. These non financial factors are considered to the extent that they are not detrimental to the Fund's investment returns.

The incorporation of these factors into investment managers' stock selection decisions should serve to enhance the process, rather than restrict choice in any way. The Fund does not negatively screen stocks from the investment universe available to managers.

The Fund requires its investment managers to integrate all material financial and non-financial factors, into the decision-making process for all investments. Furthermore, it expects its managers to proactively engage, influence and promote good corporate governance in the companies and markets to which the Fund is exposed. The Fund's Investment Managers provide updates on their activities in this regard.

All of the Fund's investment managers are signed up to the United Nations Principles of Responsible Investment (UNPRI), which encourages asset owners and asset managers to incorporate environmental, social and governance (ESG) issues into investment analysis and decision making, be active owners, seek disclosure of ESG issues and promote the principles within the industry.

The six principles are:

- We will incorporate Environmental, Social and Governance issues into investment analysis and decision-making processes;
- We will be active owners and incorporate Environmental, Social and Governance issues into our ownership policies and practices;
- We will seek appropriate disclosures on Environmental, Social and Governance issues by the entities in which we invest;
- We will promote acceptance and implementation of the Principles within the investment industry;
- We will work together to enhance our effectiveness in implementing the Principles; and

- We will each report on our activities and progress towards implementing the Principles.

The Pension Fund is a member of the Local Authority Pension Fund Forum (LAPFF). LAPFF exists to promote the investment interests of local authority pension funds, and to maximise their influence as shareholders while promoting corporate social responsibility and high standards of corporate governance among the companies in which they invest.

The Fund is committed to an orderly carbon transition and believes active engagement with investee companies is the preferred option to bring about change whilst managing overall investment risk issues.

The fund is also committed to adhering to the principles of the Stewardship Code.

## **9. Exercise of Voting Rights attached to investments.**

Long term investment interests are enhanced by the highest standards of corporate governance and corporate responsibility. Poor governance can negatively impact shareholder value.

This Fund recognises the importance of stewardship and engagement via the equity fund managers is exercised to exert a positive influence on companies.

All the Fund's active equity investment managers are expected to exercise their voting rights to promote good corporate governance and social and environmental responsibility.

The Fund has agreed a voting template which incorporates best practice governance guidelines. An independent voting agency is employed to monitor and compare the voting records of the managers against this template.

## **10. Myners Principles of Good Investment Guidance.**

The Fund assesses and reviews its own compliance with the Myners Principles annually. The Fund has assessed itself to be fully compliant with the principles below:

- Principle 1. Effective Decision Making
- Principle 2. Clear Objectives
- Principle 3. Risk and liabilities
- Principle 4. Performance assessment
- Principle 5. Responsible ownership
- Principle 6. Transparency and reporting