

**Friends of The Elderly Pension and Life Assurance Scheme  
(1978) (Closed)**

**Statement of Investment Principles**

**September 2019**

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| <b>Glossary</b> |   |
|-----------------|---|
| LGIM            | Legal & General Investment Management Limited   |
| AVCs            | Additional Voluntary Contributions  |
| ESG             | Environmental, Social and Governance<br>(including, but not limited to, climate change) |
| Members         | Members and beneficiaries of the Scheme   |
| Scheme          | Friends of The Elderly Pension and Life Assurance<br>Scheme (1978) (Closed)             |
| Trustees        | The Trustees of the Scheme  |
| UNPRI           | United Nations Principles for Responsible Investment                                    |

## 1. Introduction

This statement is made in accordance with the requirements of legislation<sup>1</sup> and, in determining a suitable investment strategy for the Scheme, the Trustees have considered the Pension Regulator's Investment Guidance for defined benefit pension schemes.

The main body of this statement sets out the principles and policies that govern investments made by the Trustees of the Scheme. Details of the specific investment arrangements in place are set out in the Appendices.

Upon request, a copy of this statement will be made available to members, the Scheme Actuary and any investment managers used by the Trustees.

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<sup>1</sup> In particular, the Pensions Act 1995, the Occupational Pensions (Investment) Regulations 2005 and the Pension Protection Fund (Pensionable Service) and Occupational Pension Schemes (Investment and Disclosure) (Amendment and Modification) Regulations 2018.

## **2. Investment Governance Structure**

### **Investment Advice**

As required by legislation, in the preparation and maintenance of this statement and when considering the suitability of any investments, the Trustees will obtain and consider written advice from their investment adviser.

The Trustees are advised on investment matters by First Actuarial LLP. First Actuarial LLP is regulated by the Institute and Faculty of Actuaries and is qualified to provide the required advice through knowledge and practical experience of financial matters relating to pension schemes.

### **Legal Advice**

Whenever deemed necessary, the Trustees will seek advice from their legal adviser on investment matters.

### **Employer Consultation**

Under legislation, the ultimate responsibility for determining the investment strategy rests with the Trustees. However, the Trustees must consult with the sponsoring employer and consultation must comprise a sharing of views, not simply notification of intent.

### **Investment Managers**

Day-to-day management of the Scheme's assets is delegated to one or more investment managers.

To ensure safekeeping of the assets, ownership and day to day control of the assets is undertaken by custodian organisations which are independent of the sponsoring employer and the investment managers. Where pooled investment vehicles are used, the custodians will typically be appointed by the investment manager.

### **Members' Views and Other Non-Financial Matters**

In the relevant regulations "non-financial matters" refers to the views of the members. This includes, but is not limited to, ethical views, views on ESG factors and views on the present and future quality of life of the members.

The Trustees recognise that it is likely that members will hold a broad range of views. However, the Trustees do not take non-financial matters into account in the selection, retention and realisation of investments. The Trustees will review their policy on whether or not to take account of non-financial matters as appropriate.

The Trustees believe that their duty to members will be best served by ensuring that all benefits can be paid as they fall due and the Trustees' Investment Objectives are designed to ensure this duty is achieved.

### **Conflicts of Interest**

The Trustees are satisfied that the investment strategy described in this Statement meets their responsibility to invest the assets in the best interests of the members and, in the case of a potential conflict of interest, in the sole interest of the members.

### **3. Investment Beliefs**

The investment beliefs stated below have been developed by the Trustees and are reflected in the Scheme's investment strategy.

#### **Appropriate Time Horizon**

In determining investment objectives and a suitable investment strategy for the Scheme, the Trustees take into account an appropriate time horizon. The Trustees believe that an appropriate time horizon will be the period over which benefits are expected to be paid from the Scheme.

#### **Risk versus Reward**

Targeting higher levels of investment return requires increased levels of investment risk which increases the volatility of the funding position.

#### **Asset Allocation**

Long-term performance of the Scheme's assets is attributable primarily to the strategic asset allocation rather than the choice of investment managers.

#### **Diversification**

Asset diversification helps to reduce risk.

#### **Use of Pooled Funds**

Taking into account the size of the Scheme's assets, it is expected that pooled funds will typically be a more practical way of implementing the Scheme's investment strategy than establishing segregated mandates with investment managers.

#### **Use of Active Management**

Active management has the potential to add value either through offering the prospect of enhanced returns or through the control of volatility. In addition, it is recognised that active management may help to mitigate the financial impact of ESG risks.

For each asset class, the Trustees will consider whether the higher fees associated with active management are justified.

#### **ESG and Other Financially Material Considerations**

The Trustees believe that financially material considerations, including ESG factors and the risks related to such factors, can contribute to the identification of both investment opportunities and financially material risks. Consequently, financially material considerations can have a material impact on investment risk and return outcomes.

The Trustees also recognise that long-term sustainability issues, particularly climate change, present risks and opportunities that increasingly may require explicit consideration.

Assessment of how ESG risks are mitigated will be one of the factors considered by the Trustees when selecting and monitoring investment managers.

#### **Stewardship**

The Trustees believe that good stewardship can help create, and preserve, value for companies and markets as a whole.

## **4. Investment Objectives and Strategy**

### **Defined Benefit Assets – Investment Objectives**

The Trustees' primary investment objectives are:

- to ensure that the assets are sufficient and available to pay members' benefits as and when they fall due;
- to generate an appropriate level of investment returns – to improve the funding position and thereby improve security for members; and
- to protect the funding position – limiting the scope for adverse investment experience reducing security for members.

The Trustees' investment approach is designed to strike a balance between the above primary objectives but also considers:

- the nature and timing of benefit payments;
- expected levels of investment return on different asset classes;
- expected levels of investment return variability and, specifically, the expected level of short-term volatility of the funding position;
- the sponsoring employer's ability to withstand additional contribution requirements that may arise from volatility in the funding position; and
- the full range of available investments (within the bounds of practicality).

### **Defined Benefit Assets – Investment Strategy**

The Trustees have taken advice from their investment advisor to construct a portfolio of investments consistent with these objectives. In doing so, consideration is given to all matters which are believed to be financially material over the appropriate time horizon.

The Trustees do not take account of non-financial matters when determining the Scheme's investment strategy.

### **AVCs**

To date the Scheme has not operated an AVCs arrangement.

## 5. Use of Investment Managers

### Investment Manager Selection

The Trustees delegate the day to day management of the assets, including selection, retention and realisation, to professional investment managers.

When considering the suitability of an investment manager, the Trustees (in conjunction with their investment adviser), will take account of all matters which are deemed to be financially material. In particular, the Trustees will:

- ensure that the investment manager has the appropriate knowledge and experience;
- ensure that the investment manager's mandate is appropriate; and
- consider the investment manager's approach to ESG factors.

When selecting investment managers, the Trustees may also take into account matters which are not financially material such as the investment manager's administrative capabilities and the liquidity of the investments.

Where pooled investment vehicles are used, it is recognised that the mandate cannot be tailored to the Trustees' particular requirements. However, the Trustees ensure that any pooled investment vehicles used are appropriate to the circumstances of the Scheme.

The Trustees will normally select investment managers who are signatories to the UNPRI and who publish the results of their annual UNPRI assessment. This principle may be waived if a fund offered by a non-signatory manager is deemed to have investment characteristics which are particularly important for meeting the Trustees' investment objectives.

### Manager Implementation

Assets are invested predominantly on regulated markets, as so defined in legislation. Any investments that do not trade on regulated markets are kept to a prudent level.

#### *Use of Derivatives*

The investment managers are permitted to use derivative instruments to reduce risk or for efficient portfolio management. Risk reduction would include mitigating the impact of a potential fall in markets or the implementation of currency hedging whilst efficient portfolio management would include using derivatives as a cost-effective way of gaining access to a market or as a method for generating capital and/or income with an acceptable level of risk.

## 6. Stewardship

The Trustees' policy in relation to the exercise of rights attaching to investments, and undertaking engagement activities in respect of investments, is that they wish to encourage best practice in terms of stewardship.

However, the Trustees invest in pooled investment vehicles and therefore accept that ongoing engagement with the underlying companies (including the exercise of voting rights) will be determined by each investment manager's own policies on such matters. For that reason, the Trustees recognise that their ability to directly influence the action of companies is limited.

Nevertheless, the Trustees expect that each investment manager will discharge its responsibilities in respect of investee companies in accordance with that investment manager's own corporate governance policies and current best practice, including the UK Corporate Governance Code and UK Stewardship Code.

The Trustees also expect that each investment manager will take ESG factors into account when exercising the rights attaching to investments and in taking decisions relating to the selection, retention and realisation of investments.

When considering the suitability of an investment manager, the Trustees (in conjunction with their investment adviser) will take account of any particular characteristics of that manager's stewardship policy that are deemed to be financially material.

The Trustees recognise that members might wish the Trustees to engage with the underlying companies in which the Scheme invests with the objective of improving corporate behaviour to benefit the environment and society. However, the Trustees' priority is to select investment managers which are best suited to help meet the Trustees' investment objectives. In making this assessment, the Trustees will receive advice from their investment adviser. The Trustees recognise that each investment manager's own policies are likely to be focussed on maximising financial returns and minimising financial risks rather than targeting an environmental or societal benefit.



## **7. Risk Mitigation**

When determining suitable investment objectives and when designing the Scheme's investment strategy, the Trustees (in conjunction with their investment adviser) will take into account all risks that are assessed to be financially material.

### **Risk Capacity and Risk Appetite**

In determining a suitable investment strategy, the Trustees consider how the volatility of the funding position is likely to be affected by changes to the asset allocation. An important consideration for the Trustees is whether a potential investment strategy is consistent with the ability of the sponsoring employer to address any future increase in deficit that may arise due to market movements.

### **Self-Investment Risk**

Legislation imposes a restriction that no more than 5% of a pension scheme's assets may be related to the sponsoring employer. The Trustees do not hold any direct employer-related assets and any indirect exposure is expected to be less than 5% of total assets.

### **ESG Risks**

The Trustees (in conjunction with their investment adviser) have considered the likely impact of the financially material ESG risks associated with all of the Scheme's investments and have assessed the mitigation of such risks implemented by each of the investment managers. In making this assessment, the Trustees recognise that, where pooled investment vehicles are held, the extent to which ESG factors will be used in the selection of suitable underlying investments will be determined by the investment managers' own policies on such matters.

### **Liquidity Risk**

The majority of the Scheme's investments will be liquid and will be realisable for cash at relatively short notice without incurring high costs. However, the Trustees recognise that the liabilities are long-term in nature and that a modest allocation to less-liquid investments may be appropriate.

Details of the liquidity characteristics of the funds held are provided in Appendix 2.

## **8. Monitoring**

The Trustees regularly review the Scheme's investments for all matters considered to be financially material over the future period for which benefits are expected to be paid from the Scheme. This includes reviewing that the assets continue to be managed in accordance with each manager's mandate and that the choice of managers remains appropriate.

Furthermore, the Trustees regularly monitor the position of the investment managers with regards to ESG matters.

**9. Future Amendments**

This statement will be reviewed at least every three years and without delay after any significant change in circumstances or investment strategy.

The Trustees have consulted with the sponsoring employer as part of the work preparing this statement.

Signed:..... Date: .....

For and on behalf of the Trustees of the Friends of The Elderly Pension and Life Assurance Scheme (1978) (Closed).

## Appendix 1: The Trustees' Investment Strategy

### Strategic Asset Allocation

In determining the strategic asset allocation, the Trustees view the investments as falling into two broad categories:

1. **Growth Assets** – Assets that are expected to deliver long-term returns in excess of liability growth. The use of Growth Assets is expected to deliver a level of investment returns deemed appropriate by the Trustees given the risk involved.
2. **Liability Matching Assets** – Assets that are expected to react to changes in market conditions in a similar way to the liabilities. The use of Liability Matching Assets is expected to protect the funding position of the Scheme.

At the time of preparing this statement, the split of the Scheme's assets between Growth and Liability Matching Assets was 14%% Growth and 86%% Liability Matching. This split is not regularly rebalanced and will vary over time as market conditions change.

The Trustees will review the strategic asset allocation periodically, and at least every three years, to ensure that the investment strategy remains consistent with the Trustees' funding objectives. As part of such a review, the Trustees will consider the risks associated with the investment strategy.

### Investment Strategy Implementation

The Trustees have selected funds managed by LGIM to implement the Scheme's investment strategy.

Further details of the investment strategy and the funds used are provided below.

### Design of the Growth Asset Portfolio

The structure of the Scheme's Growth Assets has been designed to offer diversification across a range of underlying asset classes.

The strategic allocation for the Scheme's Growth Assets is as follows:

| Pooled Fund                | Strategic Allocation of the Growth Assets |
|----------------------------|---|
| LGIM Diversified Fund      | 100%                                      |
| <b>Total Growth Assets</b> | <b>100%</b>                               |

## **Appendix 1: The Trustees' Investment Strategy (continued)**

### **Design of the Liability Matching Portfolio**

The Scheme's Liability Matching Assets are invested in the LGIM Over 15 Years Gilts Index Fund.

### **Cashflow Management Policy**

Any investments or disinvestments will be made at the discretion of the Trustees, but will normally be made in the following proportions:

- 15% LGIM Diversified Fund
- 85% LGIM Over 15 Years Gilts Index Fund.

## Appendix 2: Fund Details

This Appendix provides a summary of the funds selected to implement the Scheme's investment strategy. The details provided below were correct as at September 2019.

The following points should be noted:

- AMC – the Annual Management Charge applicable to each fund represents the fee payable to the fund manager.
- Additional expenses – these are third party costs associated with the operation of a fund such as fees paid to the administrator, the custodian and the auditor and the costs associated with the use of third-party funds where these are used. The level of the additional expenses may vary over time.
- T – the trade date at which the fund is sold, notice and settlement periods are expressed in days relative to the trade date.

| LGIM Diversified Fund |  |
|-----------------------|--|
| Objective             | To provide long-term investment growth through exposure to a diversified range of asset classes. The long-term rate of return is expected to be broadly similar to that of a developed market equity fund. |
| Legal Structure       | Unit-linked insurance policy   |
| Trading Frequency     | Weekly   |
| Notice Period         | T-2  |
| Settlement Period     | T+3  |
| Fee                   | AMC: 0.30% p.a.  |
|                       | Additional Expenses (approx.): 0.01% p.a.  |

| LGIM Over 15 Year Gilts Index Fund |   |
|------------------------------------|---|
| Objective                          | To replicate the performance of the FTSE A Government (Over 15 Year) Index to within +/- 0.25% p.a. for two years out of three. |
| Legal Structure                    | Unit-linked insurance policy  |
| Trading Frequency                  | Weekly  |
| Notice Period                      | T-2   |
| Settlement Period                  | T+3   |
| Fee                                | AMC: 0.10% p.a.   |