

# Investment Strategy Statement

Flintshire County Council

Administering Authority for the Clwyd Pension Fund

## 1. Statutory Requirement for an Investment Strategy Statement

Flintshire County Council is the Administering Authority responsible for maintaining and managing the Clwyd Pension Fund (the Fund) on behalf of its stakeholders; the scheme members and employers participating in the Fund. These responsibilities are primarily set out in Local Government Pension Scheme regulations; the regulatory framework is set out below.

The Public Service Pensions Act 2013 (The Act) enables the Secretary of State to make regulations creating schemes of pensions for, amongst others, local government workers.

In England and Wales, such a scheme was created by the Local Government Pension Scheme Regulations 2013 (The Regulations). These Regulations were made by the Secretary of State exercising powers in the Superannuation Act 1972.

Under powers contained in The Act and The Regulations, the Secretary of State made the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016, which replace the 2009 Investment Regulations. These regulations came into force on 1<sup>st</sup> November 2016.

Regulation 7(1) requires administering authorities to formulate an Investment Strategy Statement (ISS) which must be in accordance with guidance issue by the Secretary of State, and replaces the existing requirement to produce and maintain a Statement of Investment Principles.

The ISS must include:

- (a) A requirement to invest money in a wide variety of investments;
- (b) The authority's assessment of the suitability of particular investments and types of investments;
- (c) The authority's approach to risk, including the ways in which risks are to be measured and managed;
- (d) The authority's approach to pooling investments, including the use of collective investment vehicles and shared services;
- (e) The authority's approach on how social, environmental or corporate governance considerations are taken into account in the selection, non-selection, retention and realisation of investments; and
- (f) The authority's policy on the exercise of rights (including voting rights) attaching to investments.

The ISS must also set out the maximum percentage of the total value of all investments that it will invest in particular investments or classes of investments. This, in effect, replaces Schedule 1 of the 2009 Regulations.

The statement must be published by 1<sup>st</sup> April 2017 and regularly reviewed and at least every three years. Under transitional arrangements key elements of the 2009 Regulations will remain in force until the ISS is published.

This document is designed to comply with the guidance given by the Secretary of State, is effective from 1 April 2017 and will be reviewed on a regular basis, with any material changes published.

The ISS should be read in conjunction with the following statutory documents:

- Funding Strategy Statement
- Governance Policy and Compliance Statement
- Communications Strategy
- Clwyd Pension Fund Annual Report and Accounts
- Clwyd Pension Fund Actuarial Valuation.

All the above statements and documents can be found on the Fund's web site at <http://www.clwydpensionfund.org.uk/>

## About the Fund

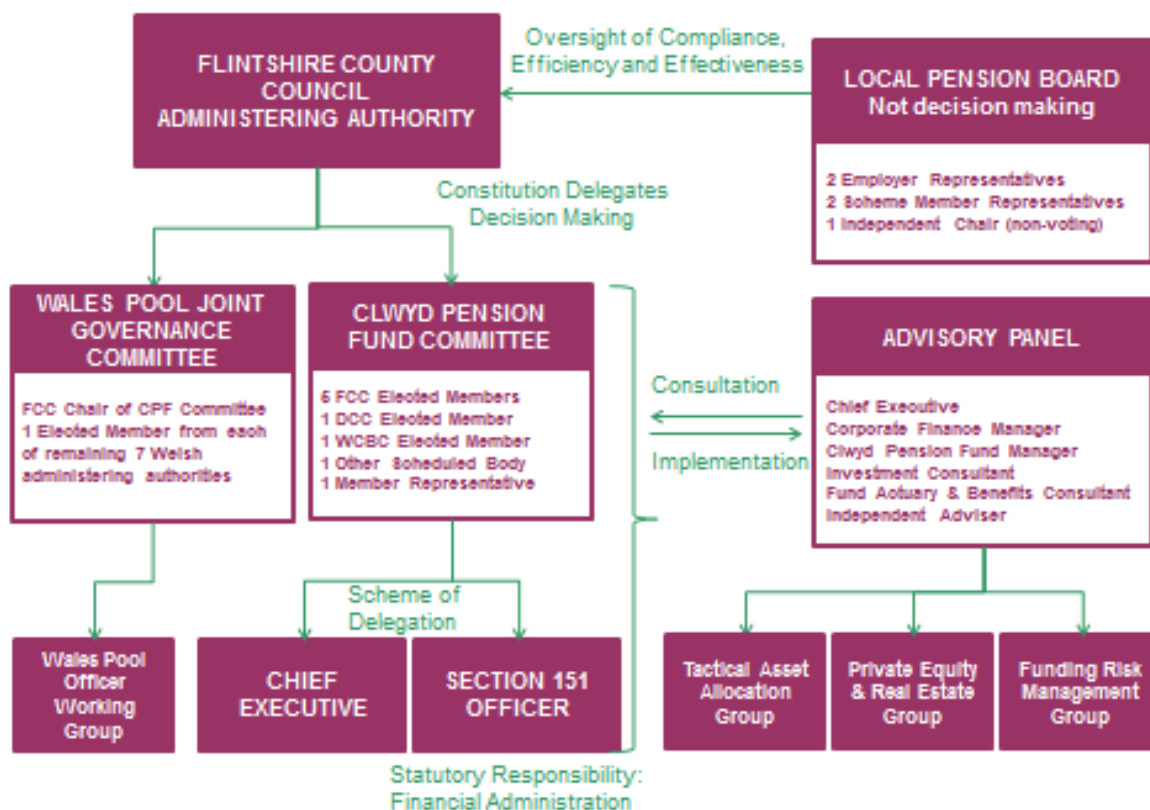
The Clwyd Pension Fund ("CPF") is a £1.4bn Local Government Pension Fund which provides death and retirement benefits for local government employees (other than teachers, police and fire-fighters) in North East Wales and employees of other qualifying bodies which provide similar services.

Total Fund membership is about 45,000 with about 16,000 active contributors from 39 contributing Employers and about 29,000 retired members, widows and deferred members.

### Governance and Management of the Fund

The key decision making and management of the Fund has been delegated by Flintshire County Council ("the Council") to a formal Pension Fund Committee ("PFC"), supported by a Pensions Advisory Panel ("AP"). Before making strategic investment decisions the Clwyd Fund takes advice from a regulated investment consultant; JLT Employee Benefits. The Fund also receives advice from the Risk Management Advisers Mercer. The County Council's Section 151 Officer (Corporate Finance Officer) has a statutory responsibility for the proper financial affairs of the Council including Fund matters. In addition, the Council has delegated specific responsibilities to the Chief Executive.

The Fund's governance structure is illustrated in the diagram below.



### Aims and Objectives for the Management of the Fund

In the Management of the Fund there is a Mission Statement and Governance Objectives (shown below). These apply to the approach to investing the Fund's monies as well as managing the overall Fund. These holistic objectives have been developed to guide the management of all aspects of the Fund.

### *Our Mission Statement is:*

- to be known as forward thinking, responsive, proactive and professional, providing excellent customer focused, reputable and credible service to all customers.
- to have instilled a corporate culture of risk awareness, financial governance, and to provide the highest quality distinctive services within the resource budget.
- to work effectively with partners, being solution focused with a 'can do' approach.

The key actions and areas of focus in the Fund's business plan are grouped into the four areas of governance, funding and investments, communications and administration, to align with the key aims and objectives of these strategies and policies. The specific aims relating to the investment management of the Fund are summarised below.

### *Governance*

- Act in the best interests of the Fund's members and employers
- Have robust governance arrangements in place, to facilitate informed decision making, supported by appropriate advice, policies and strategies
- Act with integrity and be accountable to our stakeholders for our decisions, ensuring they are robust and well based
- Understand and monitor risk
- Strive to ensure compliance with the appropriate legislation and statutory guidance, and to act in the spirit of other relevant guidelines and best practice guidance
- Clearly articulate our objectives and how we intend to achieve those objectives through business planning, and continually measure and monitor our success
- Ensure that the Fund is appropriately managed and that its services are delivered by people who have the requisite knowledge and expertise and that this knowledge and expertise is maintained within the continually changing Local Government Pension Scheme ("LGPS") and wider pensions landscape
- Ensure that those persons responsible for governing the Fund have sufficient expertise to be able to evaluate and challenge the advice they receive, that their decisions are robust and well based, and that they appropriately manage any potential conflicts of interest.

### *Funding and Investments*

- Achieve and maintain assets equal to 100% of liabilities within the 15 year average timeframe, whilst remaining within reasonable risk parameters
- Determine employer contribution requirements, whilst recognising the constraints on affordability and strength of employer covenant, with the aim being to maintain as predictable an employer contribution requirement as possible
- Recognising the constraints on affordability for employers, aim for sufficient excess investment returns relative to the growth of liabilities
- Strike the appropriate balance between long-term consistent investment performance and the funding objectives
- Manage employers' liabilities effectively through the adoption of employer specific funding objectives
- Ensure net cash outgoings can be met as/when required

- Minimise unrecoverable debt on employer termination.
- Ensure that its future strategy, investment management actions, governance and reporting procedures take full account of longer-term risks and sustainability;
- Promote acceptance of sustainability principles and work together with others to enhance the Fund's effectiveness in implementing these.

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## Investment Strategy of the Clwyd Pension Fund

The following sections details the Fund's investment strategy, which takes into account Regulation 7(2) (a) and 7(2) (b) listed below:

### 2. Investment of money in a wide variety of investments

Regulation 7(2) (a) requires that administering authorities invest in a diversified portfolio of assets to ensure that risk is appropriately managed and volatility of overall return is reduced. The guidance that accompanies the regulations does not prescribe the specific asset classes over which Fund monies must be invested.

### 3. Suitability of particular investments and types of investments

Regulation 7(2) (b) requires that in assessing the strategic allocation for the Fund, an administering authority assesses the suitability of particular investments and types of investments against the need to meet pension obligations as they fall due.

In assessing the suitability and variety of investments, and considering the risks, the starting point should be the Fund's overall objectives. These are listed in the previous section "About the Fund".

In order that these primary objectives can be achieved, the following funding and investment principles have been agreed.

#### Funding Principles

The Clwyd Pension Fund Funding Strategy implemented for three years from 1st April 2017 includes a number of investment return assumptions:

- An investment return (discount rate) for the funding target of CPI inflation plus 2.0% p.a. (assumed 4.2%).
- An investment return for the future service contribution rate of CPI Inflation plus 2.75% p.a. (assumed 4.95%).

Over a three-year period an investment return above these assumptions will contribute to reducing the funding deficit and thus employer contributions, providing that liability assumptions such as longevity and inflation remain on target. The Fund's triennial Valuation considers all these factors when determining employer contribution rates. New employer rates will be implemented from 1st April 2017. The next Actuarial Valuation will be as at 31st March 2019 with implementation from April 2020.

A Funding Strategy Statement (FSS) was prepared in accordance with Regulation 58 of the Local Government Pension Scheme Regulations 2013. The Statement outlines the strategy for recovering the funding deficit over 15 years. A copy of the FSS can be obtained from the Fund's web site at <http://www.clwydpensionfund.org.uk/>. The funding strategy will be monitored during 2017/20.

In managing the Fund, the key objectives are:

- to aim for a funding level of 100% and
- to aim for long term stability in employers' contribution rates.

The Clwyd Pension Fund was funded at 76% of liabilities (2016 Actuarial Valuation) and employers' rates are currently structured to achieve a gradual return to 100% funding by 2031.

Whilst stability of costs from the employers' rates has the higher priority, absolute cost to the employer is also important. This implies that:

- the cost of administering the Fund will be constrained by the adoption of best management practice
- employers will adopt appropriate and economic policies in those areas where they have discretion and where the costs of their actions fall on the Fund
- the Fund's overall investment policy will be aimed at superior investment returns relative to the growth of liabilities. This implies that the Fund will continue to take an active risk relative to its liability profile.

The investment principles of the Fund are stated in full below, and are intended to strike the appropriate balance between the strategy most suitable for long-term consistent performance and the funding objectives. A favourable investment performance can play a valuable role in achieving adequate funding over the longer term.

### Investment Principles

The key investment objectives for the Fund are to aim for sufficient excess investment returns relative to the growth of liabilities to meet the funding objectives set out above on an on-going basis, whilst maintaining an appropriate balance between long-term consistent investment performance and the funding objectives.

The Fund's overall strategic risk and return profile is currently determined through its strategic asset allocation. In establishing the Fund's long-term strategic asset allocation, or strategic benchmark, the key factors are the overall level of return being sought, the minimum level of risk consistent with this and the impact of diversification in reducing this risk further. At asset class or mandate level, asset class weightings, appropriate benchmarks and out-performance targets are the key building blocks in framing this overall Fund strategy.

It is Fund policy to carry out a fundamental review of the Fund's structure and management arrangements at least every four years. The review includes research on market views for the longer-term risk, return and correlation profiles for different asset classes and a more tactical view on the global economic and market environment over the next three to five years. This research is used to determine an optimum future balance between the various assets classes and hence the Fund's fixed strategic benchmark.

The latest Fund review was undertaken in 2016/17 and changes as a result of this are in the process of being implemented. Details of the investment strategy are included in following sections.

## Investment Strategy

### Setting the Strategy

The Committee have determined their investment strategy to meet the objectives outlined earlier in this Statement. This includes consideration for the Fund's liability profile and the Committee's attitude to risk.

The strategic benchmark highlighted later in this section takes account of the risk and return characteristics of each asset class and provides a reasonable long-term balance appropriate to the liabilities of the Fund. The Clwyd Pension Fund considers the mix of asset classes in forming an overall portfolio and considers the correlation in volatility and return of each.

The Committee recognise the benefits of diversification across asset classes, as well as within them, in reducing the risk that results from investing in any one particular market. Where they consider it advisable to do so, the Committee have appointed investment managers to select and manage the allocations across asset classes, in particular where it would not be practical (or appropriate) for the Committee to commit the resources necessary to make these decisions themselves.

In assessing the suitability of investments required to form the overall portfolio the Committee consider a number of characteristics of each asset class, and sub asset class. These characteristics include potential return, risk/volatility of returns, liquidity, duration and interest rate sensitivity. In setting and reviewing an overall investment strategy for the Clwyd Pension Fund the starting point is always the Actuary's assessment of the liabilities of the Fund. This assessment will include cash flow requirements and an assessment of the required return to ensure the long term solvency of the Fund, and it is essential that the investment strategy is compatible with this.

### 2016/17 Review

The 2016/17 review showed, using JLT Market Forecast Group output for Quarter 2 2016, that the expected market returns over the coming ten year period would mean that the Fund could be expected to generate a return of 6.5% p.a. (CPI inflation plus 4.5% p.a.). This is equivalent to CPI inflation plus 4.3% p.a. taking the CPI assumed in accordance with 31 March 2016 Actuarial Valuation. Investigations showed that the portfolio was well diversified and did not need a significant overhaul and the de-risking framework and Flight-path was well placed, subject to conclusion of a review by the Fund's consultants.

However, there were opportunities to reduce risk without sacrificing return.

These opportunities led to four main areas of change.

- Global Equity exposure to be split between Active and Smart Beta portfolios.
- Remove allocation to Frontier Market Equity, due to continued geo-political risk and the uncertainty of returns in the medium term;
- A new allocation to Private Credit to take advantage of the current opportunity set;
- Reduce UK Property allocation and increase investment in Infrastructure, in the longer term;

These changes meant that the expected return could be increased by 0.1%, with minimal change to the projected Deficit Risk.



Further details in relation to the investment strategy are outlined in this section.

### **Investment Decisions**

The Committee distinguish between three types of investment decision: strategic, tactical and stock-level.

#### ***Strategic Investment Decisions***

These decisions are long-term in nature and are driven by an understanding of the objectives, needs and liabilities of the Fund.

The Committee takes all such decisions themselves. They do so after receiving advice from their investment consultant. Examples of such decisions and of tasks relating to the implementation of these decisions include the following:

- Setting investment objectives
- Determining the split between the growth and the stabilising portfolios
- Determining the allocation to asset classes within the growth and stabilising portfolios
- Determining the Fund benchmark
- Reviewing the investment objectives and strategic asset allocation

#### ***Tactical Investment Decisions***

These decisions are short-term and based on expectations of near-term market movements. Such decisions may involve deviating temporarily from the strategic asset allocation and may require the timing of entry into, or exit from, an investment market or asset class.

These decisions are ultimately the responsibility of the Committee. However, where such decisions are made within a pooled fund, they are the responsibility of the investment manager of the respective fund. Furthermore, the Committee have delegated certain powers to the Clwyd Pension Fund Manager taking advice from the Tactical Asset Allocation Group. The purpose of the Tactical Allocation Portfolio, managed by the group is to take advantage of short term (approximately one year) opportunities that are consistent with the long term risk and return goals of the Fund. The Tactical Allocation Group is bound by the Tactical Allocation Portfolio Terms of Reference.

#### ***Stock Selection Decisions***

All such decisions are the responsibility of the investment managers with which the Fund invests.

## Strategic Asset Allocation

In setting the Strategic Asset Allocation for the Clwyd Pension Fund the Regulations require the Committee to invest in a wide variety of investments and in doing so assess the suitability of particular types of investments. Subject to satisfying these elements of the Regulations the Clwyd Pension Fund is not constrained to certain types of investments; the new requirement is for the Committee to set their own limits. The Fund is therefore permitted to invest across a wide range of asset classes, including, but not limited to, the following:

- Agriculture
- Cash (including currency)
- Commodities
- Convertible bonds
- Diversified growth
- Emerging market debt
- Hedge Funds and Managed Futures (including via a managed account platform)
- High yield bonds
- Infrastructure
- Liability driven investment products
- Multi –Asset Credit
- Private credit
- Private equity
- Property
- Timber
- UK and overseas corporate bonds
- UK and overseas equities
- UK and overseas government bonds, fixed and inflation-linked

### Balance between different types of investments

The Regulations require the administering authority to have regard for the diversification of the Fund's investments.

The Fund will, at all times, invest across a diversified portfolio of investments to reduce investment risk. In addition to diversifying by assets, the Fund will invest across a number of managers and via different approaches and styles to investing.

The Fund may invest via pooled and segregated portfolios based on the appropriateness of each portfolio. The Fund can invest across a combination of passive, active and absolute return investment approaches based on return potential, cost and flexibility of implementation.

The investment structure agreed in the 2016/17 investment strategy review is detailed in the table below:

Asset Class	Strategic Allocation (%)
Developed Global Equity	8.0
Emerging Market Equity	6.0
Credit Portfolio	15.0
<i>Multi-Asset Credit (liquid)</i>	<i>12.0</i>
<i>Private Credit (illiquid)</i>	<i>3.0</i>
Real Assets Portfolio *	12.0
<i>Property</i>	<i>4.0</i>
<i>Infrastructure</i>	<i>8.0</i>
Private Markets	10.0
Tactical Portfolio	21.0
<i>Diversified Growth</i>	<i>10.0</i>
<i>Best Ideas **</i>	<i>11.0</i>
Managed Account ***	9.0
Liability Hedging	19.0

**Notes:**

\* The Target allocation of the underlying asset classes in the Real Assets portfolio will take some time to achieve due to the illiquidity of the asset classes involved.

\*\*The Best Ideas portfolio is tactically allocated according to shorter-term market views. This can be implemented by increasing the allocation to any of the asset classes listed above or by separate asset classes in any type of investment. This allocation is made through consultation with the Tactical Allocation Group, which is bound by the Tactical Allocation Portfolio Terms of Reference. The objective of the Tactical Allocation Portfolio is to add value to the overall Clwyd Pension Fund return.

\*\*\* The managed account includes allocations to Managed Futures and Hedge Funds.

The Fund's investment managers are remunerated either by way of an ad valorem fee, i.e. the fee is a percentage of the value of assets under management, or a combination of an ad valorem and performance-related fee. The principle of performance-related fees is that the base fee is lower and that the manager is only paid a higher fee if the performance objective is met or exceeded.

## Asset Allocation and Long Term Expected Return on Investment

The Committee is responsible for setting the strategic asset allocation for the Fund which in turn must be consistent with the investment return assumed in the funding strategy.

The investment strategy reflects the medium to long term nature of the liabilities but must also provide flexibility to manage short term volatility in markets. In addition, the investment strategy must take account of possible changes to cash flows as the membership profile of the Fund or the benefits structure changes.

The investment strategy reflects the differing return and risk profiles of each asset class. However, long term risk and return expectations are not consistently generated over all time frames and, for all asset classes, there can be periods of under- or out-performance compared to the long term expectations.

The strategic framework includes a target allocation against which strategic performance will be monitored ('Strategic Allocation'). In addition there are ranges for each asset category that allow limited deviation within the framework ('Strategic Range'). The ranges enable the Fund to reflect changes in the market outlook and provide greater flexibility to implement cash management and rebalancing.

In addition to the Strategic Allocation and Strategic Ranges, a conditional medium term asset allocation (Conditional Range) exists, to manage major risks to the long term strategic asset allocation which may emerge between Fund reviews.

The Fund's strategic allocation, as set out below, does not assume any outperformance from the investment managers. The expected returns stated in this table are as at the date of the 2016/17 strategic review.

Asset Class	Strategic allocation (%)	Strategic range (%)	Conditional range (%) *	Expected return above Inflation (CPI) p.a.**
Developed Global Equity	8.0	5.0 – 10.0	0 – 30	+4.5%
Emerging Market Equity	6.0	5.0 – 7.5	0 – 15	+5.5%
Credit Portfolio	15.0	10.0 – 20.0	5 - 25	+2.1%
<i>Multi-Asset Credit (liquid)</i>	<i>12.0</i>	<i>10.0 – 15.0</i>	<i>5 - 20</i>	<i>+1.8%</i>
<i>Private Credit (illiquid)</i>	<i>3.0</i>	<i>2.0 – 5.0</i>	<i>0 - 10</i>	<i>+3.5%</i>
Real Assets Portfolio	12.0	10.0 – 15.0	5 - 20	+4.9%
<i>Property</i>	<i>4.0</i>	<i>2.0 – 6.0</i>	<i>0 – 10</i>	<i>+4.0%</i>
<i>Infrastructure</i>	<i>8.0</i>	<i>5.0 – 10.0</i>	<i>2 – 12</i>	<i>+5.3%</i>
Private Markets	10.0	8.0 – 12.0	8 – 12	+6.5%
Tactical Portfolio	21.0	15.0 – 25.0	10 – 30	+3.6%
<i>Diversified Growth</i>	<i>10.0</i>	<i>8.0 – 12.0</i>	<i>5 – 15</i>	<i>+4.2%</i>
<i>Best Ideas ***</i>	<i>11.0</i>	<i>9.0 – 13.0</i>	<i>5 – 15</i>	<i>+3.0%</i>
Managed Account****	9.0	7.0 – 11.0	5 - 15	+4.0%
Cash	-	0.0 – 5.0	0 – 30	+0.0%
Liability Hedging*****	19.0	10.0 - 30.0	10 - 30	+4.5%

## Notes:

\* The Conditional ranges are at a total Fund level, including the Tactical Allocation Portfolio but excluding the Liability Hedging mandate.

\*\* Expected return is expressed as an excess long-term return over CPI Inflation to reflect extra risk being taken, excluding active management. This is based on JLT Market Forecast as at the date of the 2016/17 strategic review. CPI Inflation is used as the basis for expected returns as it is a proxy for valuing the liabilities.

\*\*\* The Best Ideas allocation is a short term (12 month horizon) tactical allocation based on the JLT's (the Fund's Investment consultant) "best ideas". The portfolio should be liquid and cost efficient.

\*\*\*\* The Managed Account includes allocations to Managed Futures and Hedge Funds

\*\*\*\*\* The Liability Hedging Portfolio, a combination of Liability Driven Investment (LDI) and synthetic equity instruments, will be managed as part of a de-risking approach. Given the nature of this mandate i.e. protection against liability changes, it is not intended to rebalance the allocation, which can lead to a movement away from the initial strategic allocation of 19% at inception of the mandate.

The inclusion of a diversified range of assets and the scope for tactical allocation in the strategy is expected to reduce the overall volatility of returns without significantly altering the Fund's expected long term return. This was the case when modelling the revised investment strategy in 2016.

### LDI Flight path strategy

In March 2014, the Fund established a Liability Hedging programme covering both nominal and inflation linked interest rates.

A Flight path for increasing the level of protection of the hedges was agreed along with other funding level triggers. An LDI manager was appointed to manage this hedging portfolio in relation to market yield triggers and the Funding and Risk Management group monitors the funding level triggers relating to the overall funding and investment risk management.

As part of the 31<sup>st</sup> March 2016 actuarial valuation and investment strategy review cycle, the officers and Fund consultants (Mercer and JLT) have reviewed the Flight-path and updated the interest rate and inflation triggers.

### Realisation of investments

The Fund's investment policy is structured so that the majority of its investments (in equities, DGFs and bonds) can, except in the most extreme market conditions, be readily realised.

However, the availability of alternative investment vehicles enables the Fund to invest in less liquid asset classes and to build well-diversified portfolios. Investments such as property, infrastructure and private equity/debt are long term investments which the Fund is less likely to be able to realise in a short period. "Lock-up" periods are normal practice in hedge funds (to manage the in/out flows to

ensure existing clients' capital is protected) which means that these investments are not readily realisable either.

Notwithstanding this, the Fund maintains sufficient investments in liquid assets to meet its liabilities in the short and medium term as they fall due.

### Cash Strategy

From 1st April 2011 the 2009 Investment Regulations required the Pension Fund to have a separate bank account from the Local Authority.

The Pension Fund does not have a strategic allocation to cash for investment purposes but holds surplus cash for paying:

- Benefits and transfers as per the Regulations.
- The administration costs of the Fund.
- The Investment management fees.
- Commitments to real assets and private market investments.

However, in extreme market conditions cash could be used as part of the Conditional Asset Allocation.

The aim is to avoid requiring to borrow for liquidity purposes, although Investment Regulations allow Pension Funds to borrow for a maximum of 90 days.

The cash could be deposited in one of the following, subject to cash flow requirements:

- The Pension Fund bank account with the National Westminster bank for daily liquidity.
- A deposit account with the National Westminster Bank with access up to 180 days' notice.
- The Insight Liquidity Fund for unexpected liquidity requirements or higher rates of return.

The Clwyd Pension Fund Manager will arrange for the daily implementation of the cash strategy.

### Stock Lending

The Fund only currently invests in pooled vehicles so cannot undertake any stock lending. The stock lending policy on pooled funds is determined by the individual investment managers. Any income not retained by the fund manager and / or the lending agent is incorporated in the net asset values of each pooled fund.

## 4. Approach to risk, including the ways in which risks are to be measured and managed

Regulation 7(2) (c) requires that funds describe their approach to risk within their investment portfolio, including summarising the key risks and detailing the approach to mitigate the risk (where possible or appropriate).

### Risk Register

The Clwyd Pension Fund has a Risk Management Policy and Risk Register in place.

The Risk Register has a section dedicated to Funding & Investment Risks (including accounting and audit). Specific asset/investment risks highlighted in the risk register include those around investment markets, the failure of managers to achieve their objectives, missing out on market opportunities, and liquidity.

The risk register continually updated and key risks are considered on a regular basis at the Committee and Advisory Panel meetings.

The Committee is aware and seeks to take account, of a number of risks in relation to the Fund's investments, and these are detailed in the following paragraphs.

The main risk for the Fund is the mismatch between its assets and liabilities. As a consequence, if the investment returns are less than that required in the funding strategy the funding level will deteriorate, all else being equal. The main risks within the funding strategy are interest rate, inflation and mortality risks, and investment risk arising from the investment portfolio, which is controlled through diversification of asset holdings. The Fund has a bespoke Flightpath/Risk Management strategy that has established objectives to ensure that the Fund's exposure to interest rate risk and inflation risk is managed and monitored on an ongoing basis.

Investment, by its very nature, is a risk based activity where the returns achieved will reflect differing levels of risk. There are a number of investment risks to consider within an investment fund, namely manager, market, credit, currency and liquidity risks. Consideration of financially material non-financial risks is considered in the Fund's Sustainability Policy is later in this document.

In considering the Fund's investment strategy, one must therefore bear in mind this balance between risk and return. In practice, the investment strategy objective will be to achieve the highest possible return whilst minimising downside risk, within agreed parameters.

### Solvency Risk and Mismatching Risk

- These are measured through a qualitative and quantitative assessment of the expected development of the assets relative to the liabilities.
- These are managed by setting a Fund-specific strategic asset allocation with an appropriate level of risk.

### Manager Risk (including the All Wales Pool)

- This is assessed as the expected deviation of the prospective risk and return, as set out in the managers' objectives, relative to the investment policy.

- It is measured by monitoring the actual deviation of returns relative to the objective and factors supporting the managers' investment process, and by monitoring and replacing any managers where concerns exist over their continued ability to deliver the investment mandate.
- The aim of the investment strategy and management structure is to manage the appropriate level of risk for the return target which reflects the funding strategy. The Fund's external investment managers are required to invest in line with the investment guidelines set by the Fund. Independent custodians safe keep the assets on behalf of the Fund.

### Liquidity Risk

- This is monitored according to the level of cash-flows required by the Fund over a specified period.
- Whilst ensuring that there is the appropriate liquidity within the assets held, the Fund invests in less liquid investments to take advantage of the "illiquidity premium" offered.
- Despite this the Fund holds an appropriate amount of readily realisable investments. The Fund's assets are invested in pooled funds which are readily realisable and there is a significant amount of liquidity based upon the existing strategic asset allocation.

### Political Risk

- This is measured by the level of concentration in any one market leading to the risk of adverse influence on investment values arising from political intervention.
- The Fund manages this by regular reviews of the investments and through investing in funds which give a wide degree of diversification.

### Corporate Governance Risk

- This is assessed by reviewing the Fund's investment managers' policies regarding corporate governance.
- It is managed by delegating the exercise of voting rights to the managers, who exercise this right in accordance with their published corporate governance policies. The Fund's Sustainability Policy explains the approach in detail, and is included later in this document.

### Legislative Risk

- This is the risk that legislative changes will require action from the Committee so as to comply with any such changes in legislation.
- The Committee acknowledge that this risk is unavoidable but will seek to address any required changes so as to comply with changes in legislation.

### Market Risk

- This is the risk the fair value of future cash flows of a financial instrument will fluctuate because of changes in market prices.
- The Fund seeks to manage this risk through the strategic policy which ensures diversification of investments across a range of asset classes and markets that have low correlations with each other and across a selection of managers.
- The Fund has a significant weighting to a Tactical Allocation portfolio (TAP) which aims to take advantage of market risk, by making shorter term tactical allocations which suit the specific to characteristics of the Clwyd Fund. This is achieved with an allocation to Diversified Growth (with style diversification across two managers) and via an allocation to a Best Ideas portfolio.
- As most of the portfolio is exposed to market risk, the main risk to the Fund is a fall in market prices. Although market movements cannot be completely avoided, and indeed there are periods



when all assets become more highly correlated, the impact can be mitigated through diversifying across asset classes and approaches to investing.

- Market risk comprises of the following three types of risk:

### **Currency Risk**

- This is the risk that occurs when the price of one currency moves relative to another (reference) currency. In this context, the Fund may be invested in overseas stocks or assets, which are either directly or indirectly linked to a currency other than Sterling. There is a risk that the price of that overseas currency will move in such a way that devalues that currency relative to Sterling, thus negatively impacting the overall investment return.
- The Fund seeks to address this within the TAP but does not take a strategic view on currency movements.

### **Interest rate risk and Inflation risk**

This covers the following risks:

#### **Interest rate risk -**

- This is the risk that an investment's value will change due to a change in the level of interest rates. This affects debt instruments more directly than growth instruments.

#### **Inflation risk -**

- This is the risk that the value of the Fund's liabilities which are inextricably linked to Consumer Price Index (CPI) inflation, increase at greater rate than the assets.
- The Committee also acknowledge the interest rate risk and inflation risk related to individual debt instruments. This is managed by the underlying investment managers through a combination of strategies, such as diversification, duration and yield curve management and investing in assets that move in line with inflation such as Infrastructure.
- Since 2014 the Fund has adopted a Flight-path approach to managing the specific inflation and interest rate risk. The Flight path is regularly reviewed and the appropriate trigger levels set.

### **Risk Budgets**

In formulating the revised investment strategy, expected risk and return figures were utilised for each asset class. The figures used in the 2016/17 strategic review are as follows.

Asset Class	Expected return above inflation p.a. *	Expected Risk (Volatility) p.a. **
Developed Global Equity	+4.5%	14%
Emerging Market Equity	+5.5%	20%
Credit Portfolio	2.1%	6%
<i>Multi-Asset Credit (liquid)</i>	<i>+1.8%</i>	<i>5%</i>
<i>Private Credit (illiquid)</i>	<i>+3.5%</i>	<i>12%</i>
Real Assets Portfolio	4.9%	11%
<i>Property</i>	<i>4.0%</i>	<i>5%</i>
<i>Infrastructure</i>	<i>5.3%</i>	<i>14%</i>

Private Markets	+6.5%	28%
Tactical Portfolio	+3.6%	9%
<i>Diversified Growth</i>	+4.2%	9%
<i>Best Ideas **</i>	+3.0%	9%
Managed Account ***	+4.0%	6%
Liability Hedging	+4.5%	15%

\* Expected return is expressed as an excess long-term return over Inflation (measured by CPI) to reflect the extra risk being taken, excluding active management. This is based on JLT Market Forecast as at the date of the 2016 strategic review. CPI is used as the basis for expected returns as they are a proxy for valuing the liabilities.

\*\* Expected risk is based on 10 year historic returns and volatility

\*\*\* The managed account includes allocations to Managed Futures and Hedge Funds

### Proper advice

In assessing the Fund's strategy, including an assessment of the implicit risks, and setting the maximum limits Flintshire County Council as Administering Authority for the Clwyd Pension Fund has taken proper advice from Officers, JLT Employee Benefits (Investment Consultants) and Mercer (Actuaries and Risk Management Advisers).

As part of the Fund's governance structure, there are regular meetings between the Fund's officers, the Investment Consultants, the Actuaries and Risk Management Advisers and the Fund receives advice from these parties on a continuous basis.

## 5. Approach to pooling

Regulation 7(2) (d) requires that all authorities commit to a suitable pool to achieve benefits of scale. It also requires that administering authorities confirm the chosen investment pool meets Government's investment reform criteria, or to the extent that it does not, that Government is content for it to continue.

The Clwyd Pension Fund is participating in the development of the WALES Pool. The proposed structure and basis on which the WALES Pool will operate was set out in the July 2016 submission to the Government.

The WALES Pool received confirmation from the Minister for Local Government that he was happy that the proposals met the required criteria, with the exception of the size requirement. However, the Minister confirmed in his letter to the Welsh Funds that given the special position of Wales, and the long history of collaboration he was content with the final proposal.

The agreed objectives of the WALES Pool are:

- To provide pooling arrangements which allow individual funds to implement their own investment strategies (where practical).
- To achieve material cost savings for participating funds while improving or maintaining investment performance after fees.
- To put in place robust governance arrangements to oversee the Pool's activities.
- To work closely with other pools in order to explore the benefits that all stakeholders in Wales might obtain from wider pooling solutions or potential direct investments.

In the longer term, subject to the above mentioned objectives being met, the Clwyd Fund is committed to investing all of its assets through the WALES Pool.

### Structure and governance of the WALES Pool

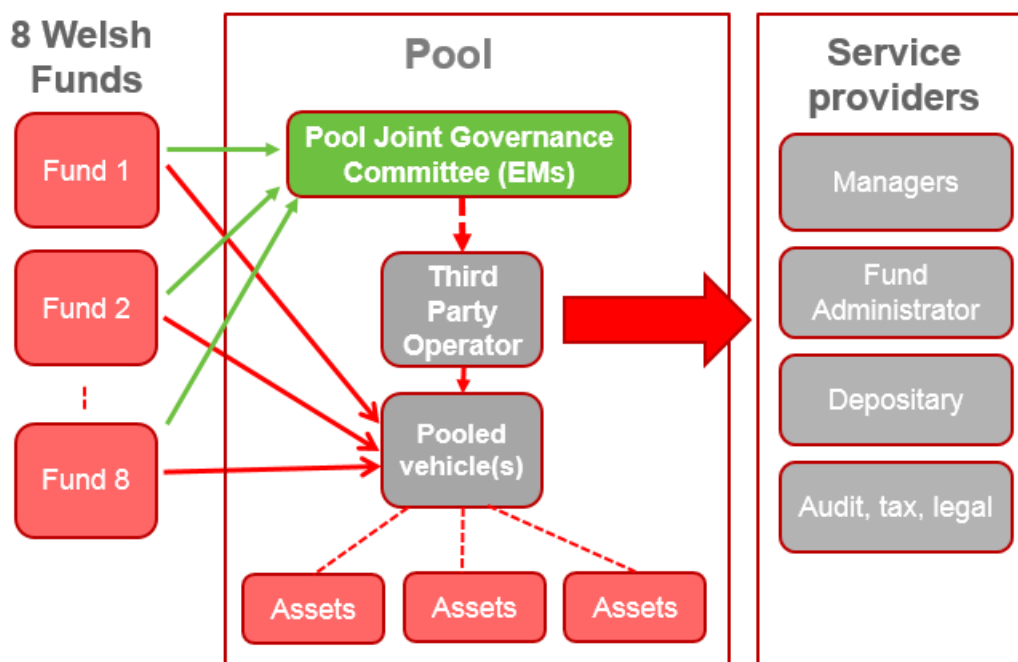
The Pool will appoint a third party operator authorised by the FCA to provide a series of investment sub-funds in which assets of the participating funds will be invested. A diagram showing the proposed structure is shown on the next page.

A Joint Governance Committee (JGC) has been established to oversee the operator. The Committee comprises elected members – one from each of the eight participating funds. It is anticipated that this may be the Chairs of the respective Pensions Committees though administering authorities may choose to nominate alternative members if appropriate. This arrangement will provide accountability for the operator back to individual administering authorities.

The JGC has been setup formally as a Joint Committee between the participating administering authorities. It will operate on the basis of "One Fund, One Vote", though the intention is that any decisions are reached on a consensus wherever possible. A formal Terms of Reference for the Committee has been drawn up.

Each authority has committed to the pool by agreeing and signing an Inter-Authority agreement. The agreement sets out the principles behind the WALES pool, and will commit the administering authorities to sharing the costs of setup.

## Governance Structure of the WALES Pool



The operator will be responsible for selecting and contracting with investment managers for each of the sub-funds as well as appointing other service providers such as a depository asset servicer, and an external valuer as necessary.

It is anticipated at this stage that listed bonds and equities are likely to be invested through a UK based Authorised Contractual Scheme (ACS) in order to benefit from the tax transparent nature of the vehicle, though this will be discussed with the appointed operator. It may be that alternative vehicles are more appropriate for some asset classes. As well as considering the options with the operator, advice will be sought of the final proposed approach from a tax efficiency and legal compliance basis.

It is likely that it will take some time for the illiquid asset classes to transition into the Pool, and the process and benefits of doing so will be discussed with the operator. Given the Clwyd Fund has a significant proportion of its assets in alternative, less liquid investments it may be some time before all of the Fund's assets are able to be pooled.

## 6. Approach to Environmental, Social and Governance issues

And

## 7. Policy on exercising voting rights

Regulation 7(2)(e) requires administering authorities to demonstrate that it considers any factors that are financially material to the performance of the fund's investments, including social, environmental and corporate governance factors, and over the long term, dependent on the time horizon over which their liabilities arise.

Regulation 7(2) (f) requires administering authorities to explain their policy on exercising rights (including voting rights) attaching to investments. The guidance refers to the Financial Reporting Council's UK Stewardship Code and requires that funds explain, where appropriate their policy on stewardship with reference to the Stewardship Code.

### Responsible Investing Policy

The Fund recognises the importance of its role as stewards of capital and the need to ensure the highest standards of governance and promoting corporate responsibility in the underlying companies in which its investments reside. The Fund recognises that ultimately this protects the financial interests of the Fund and its ultimate beneficiaries. The Fund has a commitment to actively exercising the ownership rights attached to its investments reflecting the Fund's conviction that responsible asset owners should maintain oversight of the companies in which it ultimately invests recognising that the companies' activities impact upon not only their customers and clients, but more widely upon their employees and other stakeholders and also wider society.

The Fund has delegated responsibility for voting rights to the Fund's external investment managers and expects them to actively engage with companies, and to vote. Due to the Fund investing mainly in pooled funds it is not possible to impose the Fund's own voting policy, but on appointment the Fund ensures that the fund manager has voting guidelines in line with the Clwyd Fund's policies.

The Clwyd Pension Fund recognises that there is a link between good environmental, social, ethical and governance practices and long-term sustainable business profitability and in its investment strategy aims to place a strong focus on this. It is recognised that, whilst there are links, the three main sustainability areas, environmental, social and ethical, each raise their own issues, although the approaches and guidelines appropriate to each are similar.

As part of this the Fund, subject to fiduciary duties, makes selective investments in environmentally supportive areas such as clean-technologies, clean energy, environmental infrastructure and forestry

The Fund regularly meets with existing and new managers to discuss opportunities within the environmental area.

At the strategic level, a manager's approach to identifying and managing RI risks and opportunities is evaluated as part of the tender process for appointing new managers. It is also incorporated into the on-going process of monitoring the investment managers' performance.

The Fund is a member of the Local Authority Pension Fund Forum (LAPFF) whose primary aims are to seek improvements in the corporate governance of the companies in which member funds invest, and also to promote Socially Responsible Investment (SRI) on environmental issues and issues relating to

overseas employment standards. This very much reflects the principles built into the Fund's own Sustainability Policy.

The Fund is also a member of the Pension and Lifetime Savings Association (PLSA) which also provides further guidance on Governance and Social Responsibility issues as well as the wider pension issues.

The Clwyd Pension Fund has incorporated these areas and others into its Sustainability Policy (below).

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## Sustainability Policy

### Definition

At its simplest, sustainability is about focusing attention on longer-term issues. More specifically for pension fund investors, it concerns delivering the long-term returns required to fund long-term liabilities by ensuring that the long-term risks inherent in investments are recognised and, where possible, addressed. These risks are many and varied but include environmental, social, ethical and governance issues.

### Legal Framework, Constraints & Considerations

In framing a Sustainability Policy, the following are pertinent –

- There already exists a requirement for the Fund to include within its Investment Strategy Statement (ISS) details of its policy on social, ethical and environmental issues. This Sustainability Policy encompasses such issues and will be updated as required to take account of relevant new regulatory requirements.
- The Fund is required to fulfil its overriding fiduciary duty to focus as a primary consideration on financial performance and the maximisation of Fund returns, after taking full account of all existing and future financial risks. Such risks increasingly include sustainability issues.
- Whilst the financial criterion is maintained as a key investment decision criterion, this has now been broadened to include non-financial criteria, subject to certain caveats, and the Fund is required to give an explanation of the extent to which non-financial factors will be taken into account and its approach to social investments.
- The investment industry tends to focus on short term factors in terms of company interaction, shares prices and performance, and fund managers incentives tend to reflect this rather than being aligned with the longer-term objectives of pension fund investors.

### Objective

#### Objective

Within the above legal framework, constraints and considerations, the Clwyd Pension Fund's objective aim will be to –

- Ensure that its future strategy, investment management actions, governance and reporting procedures take full account of longer-term risks and sustainability;
- Promote acceptance of sustainability principles and work together with others to enhance the Fund's effectiveness in implementing these.

## United Nations Principles for Responsible Investing (UNPRI)

Given the constraints outlined above and particularly the pooled nature of many of the Fund's investments, it would be difficult for the Fund to become a formal signatory to the UNPRI.

### United Nations Principles for Responsible Investing (UNPRI)

The Clwyd Pension Fund –

- Is committed to the principles underlying the United Nations Principles for Responsible Investing (UNPRI) and will be an active supporter of these;
- Will encourage its external managers to become signatories to the UNPRI.

The Fund Objective stated above already encompasses most of the UNPRI.

## Application of Sustainability Principles

In order to achieve its stated objective, the Clwyd Pension Fund will apply a series of guidelines covering most aspects of pension fund investment under the following headings –

- Sustainability approach
- Investment strategy (UNPRI 1)
- Company engagement & voting (UNPRI 2)
- Investment management & performance monitoring (UNPRI 3)
- Investment manager selection & contracts (UNPRI 4)
- Collaboration (UNPRI 5)
- Reporting & disclosure (UNPRI 6)
- Review

The paragraphs below set out the Fund's thought processes in establishing such guidelines and detail the guidelines adopted as part of this Sustainability Policy document.



## Sustainability Approach

In framing an approach to sustainability, the key focus has to be on the UNPRI principles 1 and 2 as these underlie most investment and governance processes. Sustainability-related issues have been considered on a regular basis for many years, with broad corporate governance policy guidelines in place from 1996. More recently these form part of the Fund's ISS and are reviewed annually.

The Clwyd Pension Fund approach has always been and continues to be based upon "active engagement". This involves the Fund's managers researching and forming a view on the sustainability credentials of companies, taking this into account in investment decisions and, where there are sustainability concerns, on environmental, social, ethical or governance grounds, engaging with companies to seek and achieve positive change.

### Sustainability Approach

The Clwyd Pension Fund believes in an active engagement approach to the pursuit of its sustainability objectives and, on this broad basis, it –

- Will not adopt a negative approach to sustainability which involves screening and excluding investment opportunities;
- Will not invest in pooled vehicles constructed using this same approach;
- Will encourage its managers to adopt a long-term approach that involves working with companies to encourage improvement in all sustainability areas;
- Will monitor the performance of managers in pursuing such objectives;
- Will invest directly in specific vehicles and investment areas that clearly match its sustainability objectives.

## Investment Strategy

The Clwyd Pension Fund recognises that there is a relationship between good environmental, social, ethical and governance practices and long-term sustainable business profitability and in its investment strategy aims to place a strong focus on this. It is recognised that, whilst there are links, the three main sustainability areas, environmental, social and ethical, each raise their own issues, although the approaches and guidelines appropriate to each are similar.

### *Environmental*

The impact of poor environmental practices on profit sustainability is very clear. There are direct costs in terms of fines for pollution etc. and increasingly now for carbon-charging and waste disposal that can have major impacts on business models. In addition there are potential indirect costs from bad publicity and reputational risk. On the positive side, however, there are opportunities to promote sustainability through investment in new technologies aimed at cleaner solutions.

### *Social*

This concerns areas such as employee relations, community relations and health & safety and again can lead to direct financial costs from health and safety breaches and strike action etc., as well as more subtle risks to company operations, reputation and long-term profitability.

### *Ethical*

This is a difficult area as ethical views can vary considerably but there are some areas that are widely accepted for inclusion. These include supply chain issues that reflect potential breaches of human rights and especially the employment of children, bribery and corruption and operations in certain world areas such as Zimbabwe.

#### Investment Strategy

On forming and implementing its investment strategy, the Clwyd Pension Fund –

- Will encourage its managers to use their own resources or specifically-focused research agencies to identify at company level actual or potential financial risks attributable to sustainability issues – environmental, social or ethical;
- Will seek, through its managers, to engage with companies that have questionable environmental, social or ethical practices in order to seek improvements;
- Will seek, through its managers, to engage with companies that have a carbon-intensive or water-intensive focus in order to promote alternative approaches and longer-term reductions;
- Will encourage the adoption of the best environmental standards amongst its property and infrastructure managers;
- Will, subject to fiduciary duties, make selective investments in environmentally supportive areas such as clean-technologies, clean energy, environmental infrastructure and forestry etc.

## Company Engagement & Voting

Getting the Board right with the right behaviours and structures means that better decisions are more likely and this adds value over the longer-term. The Fund's former broad corporate governance policy guidelines, whilst touching upon environmental, social and ethical issues, were largely designed to address these Board factors and related voting issues. Myners' Principle 5 is also relevant here. This requires that trustees adopt, or ensure their investment managers adopt, the Institutional Shareholders' Committee (ISC) Statement of Principles on the responsibilities of shareholders and agents. The Institutional Limited Partners Association (ILPA) has authored the ILPA Private Equity Principles, a document that contains best practice concepts and that speaks to issues relating to the alignment of interest between general partners and limited partners, fund governance, transparency and reporting guidelines in order that these can be taken account of in their investment management decision-making processes.

In order to monitor the performance of external managers in terms of their degree of compliance with the guidelines and the performance of underlying investments with the Fund's sustainability objectives, there needs to be regular reporting and disclosure on sustainability issues, particularly areas of concern, as well as actions taken to address these.

## Company Engagement & Voting

### The Clwyd Fund –

- Will aim to comply with the Myners' Principle 5 on shareholder activism and become more engaged as an active investor, especially with companies where sustainability factors are a matter of concern;
- Will ensure that its managers adopt or ascertain their level of compliance with the ISC Statement of Principles on the responsibilities of shareholders/agents;
- Will ensure that its managers adopt or ascertain their level of compliance with the ILPA private equity principles;
- Will, wherever practical, exercise voting rights through its managers based upon the following broad criteria –
  - The prime consideration must be financial and the protection of the Fund's assets in the long term;
  - There should be a properly structured Board including an appropriate number of contributing independent non-executive directors;
  - Unless there are strong arguments to the contrary and adequate safeguards guidelines, no director should hold the posts of Chairman and Chief Executive at the same time or be in a position of unaccountability by virtue of having absolute control;
  - All Directors should be subject to at least three-yearly re-election;
  - In view of their stewardship role, non-executive directors should normally be independent in terms of other links to the company and other directorships;
  - The issue of shares with reduced or non-existent voting rights often disadvantages the majority of shareholders and should not normally be supported;
  - Existing shareholders in a company should have a right to subscribe for new equity capital raised by a company, normally in proportion to their existing share of the company's equity capital;
  - Unless financial criteria dictate otherwise, the general policy on take-over bids should be to support incumbent management in good standing;
  - Directors' remuneration packages in different companies should reflect relative performance taking business size and complexity into account;
  - A properly constituted Remuneration Committee is the best judge of what is necessary to recruit, train and motivate;
  - If not already in place, companies should be working towards one year fixed term contracts for executives;
  - There should be a properly constituted Audit Committee;
  - No return that is rightfully the Fund's should be diverted to political donations;
  - Charitable donations are acceptable if they are reasonable and have public relations values.
- Will periodically review these criteria and inform investment managers of changes, should there be any.

## Investment Management & Monitoring of Performance

Investment managers need to be made aware of the Fund's Sustainability Policy

### Investment Management & Monitoring of Performance

The Clwyd Pension Fund –

- Will endeavour to ascertain the extent to which its fund managers are formal signatories to, support and comply with the UNPRI;
- Will encourage its fund managers to produce policy statements on sustainability issues and report formally on these.
- Will seek, through its managers, to ensure the full disclosure of environmental, social and ethical policies and practices by companies in which the Fund is invested;
- Will ask investment managers for statements on their degree of compliance with the ISC Statement of Principles on the responsibilities of shareholders and agents;
- Will request policy statements and practical evidence of the adoption of the best environmental standards amongst its property and infrastructure managers;
- Will ask private equity managers for statements on their degree of compliance with the ILPA private equity principles;
- Will ensure that investment managers regularly report records of voting on the Fund's investment and periodically produce statements on compliance or otherwise with the broad corporate governance elements of the Fund's Sustainability Policy;
- Will, subject to appropriate return targets, invest directly in funds focused upon environmental and social objectives.
- Will, where feasible, gather data on the environmental and social impact of these and other funds;
- Will assess the performance of managers both in terms of financial returns and on sustainability issues over a time frame that adequately reflects the Fund's sustainability objectives.

## Investment Manager Selection & Contracts

The Fund's standard selection process for managers has always incorporated broad questions on sustainability issues but the main focus has been on investment philosophy, process, personnel and performance. Within this process, there has been some limited focus on sustainability inputs to investment decision-making but risk has tended to be quite narrowly defined and linked to shorter-term financial rather than longer-term sustainability considerations. As a result, sustainability has never been a main factor in the comparative assessment of managers prior to appointment or in the formal appointment process itself. This approach has now been reviewed with a view to incorporating into the selection and contracting process a far greater focus on sustainability issues.

### Investment Manager Selection & Contracts

As an active part of this process, the Clwyd Pension Fund –

- Will require from potential managers formal statements of their objectives, policies and practices on sustainability and related factors;
- Will ascertain from potential managers the degree to which sustainability factors are taken into account in the investment decision-making process;
- Will seek from potential managers details and the level of in-house tools, agency inputs and other resources on sustainability factors used in their investment processes;
- Will review with potential managers the quality, integration and impact of such research on their investment processes and performance;
- Will ascertain the ability of potential managers to assess and quantify the environmental and social impact of their investments;
- Will consider the record of potential managers on active engagement with companies, voting and governance issues generally;
- Will, in the assessment of potential managers, give appropriate weight to all these sustainability and related factors;
- Will, where relevant and appropriate, build elements of the Fund's Sustainability Policy and detailed guidelines into investment management agreements.

## Collaboration

The Clwyd Pension Fund is already a committed member of the Local Authority Pension Fund Forum (LAPFF), a body that seeks improvements in corporate governance, promotes socially responsible investing (SRI) and, with the Fund's active encouragement, is devoting considerable resources to environmental issues and climate change in particular. LAPFF is already a signatory to the UNPRI. The Fund has also had contact with other relevant bodies on sustainability issues both directly and through its managers.

### Collaboration

The Clwyd Pension Fund –

- Will join and/or collaborate with organisations that are relevant to pursuit of the Fund's sustainability objectives;
- Will, subject to regulatory and operational constraints, seek relevant information from and share relevant information with such organisations in order to further the effective delivery of its Sustainability Policy.

## Reporting & Disclosure

The Clwyd Pension Fund Annual Report already includes copies of various regulatory documents, including various policy statements and the Fund's ISS. The latter includes details of the Fund's current policy statements on social, environmental and ethical considerations and corporate governance issues. The Annual Report is circulated widely and all these documents are also published on the Fund's website. It is already accepted that approaches on sustainability and other policy areas tend to evolve and develop over time. It is essential therefore to keep policies and practices under continual review so as to improve their efficacy.

### Reporting & Disclosure

The Clwyd Pension Fund –

- Will, through its quarterly meeting procedure, report regularly and as appropriate on relevant sustainability issues;
- Will, periodically, report formally on managers' level of compliance with the its Sustainability Policy, progress made in the year and areas where further progress needs to be made;
- Will, once a year, review its Sustainability Policy in the light of best practice and agree any proposed changes through its governance procedure;
- Will circulate this revised document to relevant bodies and particularly its managers;
- Will incorporate this revised document into its ISS and publish its contents both in the Annual Report and on its website.

## UK Stewardship Code

The Financial Reporting Council (FRC) first published the UK Stewardship Code in 2010, and revised it in 2012. The Code aims to enhance the quality of engagement between asset managers and companies to help improve long-term risk-adjusted returns to shareholders. The Code sets out a number of areas of good practice to which the FRC believes institutional investors should aspire. Since December 2010 all UK-authorized Asset Managers are required by the Financial Conduct Authority to produce a statement of commitment to the Stewardship Code or explain why it is not appropriate to their business model.

The Stewardship Code has seven principles, and the ISS guidance requires that administering authorities become signatories to the Code, and state how they implement the principles on a “comply or explain” basis.

The Fund is not currently a signatory to the Code, however the principles are followed, where appropriate, and there are plans to become a signatory in time. The compliance position is shown in Appendix 2.

In practice the Fund’s policy is to apply the Code both through its arrangements with its asset managers and through membership of the LAPFF. In the future as a member of the WALES Pool, the Committee expects that both the Pool and the underlying fund managers to comply with the Stewardship Code.



## Social investments

The Government guidance also addresses the issue of “social investments”; meaning those that deliver a social impact as well as a financial return. The Government considers that social investments are appropriate for LGPS funds where either the social impact is simply in addition to the financial return. It also considers that investments where some part of the financial return is forgone in order to generate the social impact are also appropriate, where the administering authorities have good reason to think scheme members share the concern for social impact, and there is no risk of significant financial detriment to the fund.

Much of the Fund’s approach is set out in the Sustainability Policy contained earlier in the document, but a specific response to this issue is set out below.

### Approach

The Clwyd Pension Fund is a strong believer in sustainability across all areas, including environmental, social and governance, and fully embodies these non-financial factors in its decision-making and monitoring processes. More specifically, it –

- Will endeavour to ascertain the extent to which potential fund managers are formal signatories to, support and comply with the UNPRI and seek to ensure full disclosure of the environmental, social and ethical policies and practices of such managers;
- Will, as part of its appointment process, give full consideration to a manager's philosophy, people and investment process, as well as its track record in terms of financial returns;
- Will give an appropriate weight to all such non-financial factors, including a manager's environmental, social and governance standing, as part of its decision-making process;
- Will encourage existing and long-standing managers to adopt the best environmental, social and governance standards and monitor progress, as appropriate;
- Will, subject to fiduciary considerations, make selective investments in environmentally supportive areas such as clean-technologies, clean energy, environmental infrastructure and forestry etc.
- Will, subject to fiduciary considerations, make selective investments in managers with a social and environment impact focus whose aim is to “do good as well as doing well commercially”.
- Will look for investment opportunities across all sectors that offer potential for catalysing economic growth, particularly in deprived areas.

### Impact

The Clwyd Pension Fund is eager to ascertain the impact of such this approach and is eager to assess and quantify, where feasible, the outcomes from its investments. More specifically, it -

- Will monitor the performance of managers in pursuing such objectives and specifically seek information on relevant environmental and social factors at all meetings with them;
- Will encourage managers to assess and quantify, where feasible, the impact of such factors in terms of employment, health and well-being and education and training, environmental impact and regeneration etc.
- Will monitor the outcome data of managers investing directly in companies and areas that match the Fund's environmental and social objectives.

## Further Information

This Investment Strategy Statement was recommended to the Clwyd Pension Fund Committee on 21 March 2017.

If you require further information about anything in or related to this Investment Strategy Statement, please email:

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## Appendix A – Myners Principles – 2016/17 Compliance

### Principle 1

Administering authorities should ensure that:

- Decisions are taken by persons or organizations with the skills, knowledge, advice and resources necessary to make them effectively and monitor their implementation, and
- Those persons or organizations have sufficient expertise to be able to evaluate and challenge the advice they receive, and manage conflicts of interest.

Key Areas and Guidance	Comment & Actions	Compliance
It is good practice to have an investment sub-committee, to provide the appropriate focus and skills on investment decision-making.	The administering authority delegates investment decisions to the Clwyd Pension Fund Committee. The Committee delegate functions to Officers who take investment advice as required from a Pension Advisory Panel who provide appropriate focus and skills on investment decision making. Further, a Tactical Allocation Group has been formed to take advantage of short term opportunities that are consistent with the long term risk and return goals of the Fund. Representatives and roles are defined in the ISS. This new governance structure was implemented from May 2014.	Full
The board should have appropriate skills for effective decision-making.	Training is given priority status through compliance with CIPFA Knowledge and Skills Code of Practice for elected members and ongoing sessions provided regularly through managers, collaboration and seminars. The Fund has produced a training policy for Members and Senior Officers. A needs assessment process will be introduced for members of the new Committee.	Partial
There should be sufficient internal resources and access to external resources for trustees and boards to make effective decisions.	The Committee has access to experienced and trained officers and an Advisory Panel of professionals qualified to provide proper advice.	Full
There should be an investment business plan with progress regularly evaluated.	The three year business plan includes an investment business plan, which is approved by the Committee who then receive updates on progress each Committee.	Full
The remuneration of trustees should be considered.	Remuneration and expenses are reviewed, considered and set by Council.	Full

<p>Particular attention should be paid to managing and contracting with external advisers (including advice on strategic asset allocation, investment management and actuarial issues).</p>	<p>The Investment Consultant, Actuary and Independent Adviser all have contracts which are regularly reviewed. Performance of the Investment Consultant and Actuary will be monitored by the Independent Adviser. The Investment Consultant and Independent Adviser contracts were tendered in 2013/14 and new provider contracts commenced in April 2014</p>	<p>Full</p>
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## Principle 2

Trustees should set out an overall investment objective(s) for the fund that takes account of the scheme's liabilities, the strength of the sponsor covenant and the attitude to risk of both the trustees and the sponsor, and clearly communicate these to advisers and investment managers.

Key Areas and Guidance	Comment & Actions	Compliance
Benchmarks and objectives should be in place for the funding and investment of the scheme.	The Fund's ISS sets out its investment and funding objectives as well as its overall strategic customized benchmark, asset class targets and Conditional Asset Allocation.	Full
Fund managers should have clear written mandates covering scheme expectations, which include clear time horizons for performance measurement and evaluation.	Fund managers operate to detailed written mandates based in the main on 3-year rolling performance objectives, some market-based with others more absolute return in nature. The Liability Hedging portfolio has a liability based benchmark.	Full
Trustees consider as appropriate, given the size of fund, a range of asset classes, active or passive management styles and the impact of investment management costs when formulating objectives and mandates.	The Fund has always looked very widely at available asset classes and its extremely diversified structure reflects this. Whilst competitive deals are always sought with managers, fee levels have been less of a consideration on the grounds that, in optimizing structures, returns have always been considered on a net basis and that such costs are anyway offset by minimal additional performance. Other fund costs are very carefully considered and monitored.	Full
Trustees should consider the strength of the sponsor covenant.	The Fund is effectively Government-backed but the Fund impact on stakeholders receives appropriate attention. The Fund monitors each of the participating LGPS employers and admitted bodies.	Full

### Principle 3

In setting and reviewing their investment strategy, trustees should take account of the form and structure of liabilities. These include the strength of the sponsor covenant, the risk of sponsor default and longevity risk.

Key Areas and Guidance	Comment & Actions	Compliance
Trustees should have a clear policy on willingness to accept underperformance due to market conditions.	Most managers have market-related benchmarks. There is clear acceptance of the fact that markets can be volatile in the short term. The setting of the Fund's strategic benchmarks is based upon the probable long-run performance of specific asset classes. Similarly, whilst the Fund's aim is that managers will outperform their benchmarks at all times, periods of under-performance are accepted as long as longer-term performance remains intact. A Tactical Allocation Portfolio, which looks to take advantage of short term opportunities that are consistent with the long term risk and return goals of the Fund, form part of the new investment strategy.	Full
Trustees should analyse factors affecting long-term performance and receive advice on how these impact on the scheme and its liabilities.	At each Fund Review exercise, optimization techniques are used that take account of probable performance and risk factors as well as asset class correlations and the Fund's actuarial position. The implementation of the flight-path strategy now requires regular monitoring of the funding position Such issues will be looked at again as part of the next Fund Structure review.	Full
Trustees should take into account the risks associated with their liabilities' valuation and management.	These risks are considered as part of the Fund's flight-path strategy for managing funding risks such as interest rates and inflation. Each Fund Review exercise is aimed at achieving an overall long-term rate of return adequate to cover liability growth (pay/price inflation, interest rate changes and mortality) and to return, in time, to full funding status.	Full
Trustees have a legal requirement to establish and operate internal controls.	Committee members receive regular independent reports from Internal Audit and External Audit on internal controls. Any actions recommended by these bodies are actioned promptly.	Full
Trustees should consider whether the investment strategy is consistent with the scheme sponsor's objectives and ability to pay.	The Fund's investment strategy is considered as part of the regular actuarial process used to review and set employers' rates of contribution and consistency between the two is an important factor.	Full

## Principle 4

Trustees should arrange for the formal measurement of the performance of the investments, investment managers and advisors. Trustees should also periodically make a formal policy assessment of their own effectiveness as a decision-making body and report on this to scheme members.

Key Areas and Guidance	Comment & Actions	Compliance
There is a formal policy and process for assessing individual performance of trustees and managers.	The performance of the Committee is assessed by the Independent Adviser and published in the Annual Report. In line with the ISS, the performance of the Fund and its fund managers is formally monitored by the Investment Consultant and Officers. The Investment Consultant provides regular performance monitoring reports to both the Advisory Panel and Committee.	Full
Trustees should demonstrate an effective contribution and commitment to the role (for example measured by participation at meetings).	Records of attendance at Committee and training events are maintained and reported in the Annual Report. Participation is recorded in the Committee minutes.	Full
The chairman should address the results of the performance evaluation.	All current performance evaluation documents (Training records, Independent Adviser, risk, Audit) are brought to Committee. The Chairman has a key role in this, but also taking input from Officers and the Advisory Panel, with appropriate actions being agreed.	Full
There should be a statement of how performance evaluations have been conducted.	Investments and Investment Managers are monitored on a quarterly basis by Committee and Advisory Panel. All advisers have fixed term contracts and the performance of contract specifications is reviewed annually as part of the overall governance review.	Full
When selecting external advisers, relevant factors including past performance and price should be taken into account.	Advisers are selected competitively, based on performance, price and other factors.	Full

## Principle 5

Trustees should adopt, or ensure their investment managers adopt, the Institutional Shareholders' Committee (ISC) Statement of Principles on the responsibilities of shareholders and agents. A statement of the scheme's policy on responsible ownership should be included in the Statement of Investment Principles. Trustees should report periodically to members on the discharge of such responsibilities.

Key Areas and Guidance	Comment & Actions	Compliance
Policies regarding responsible ownership should be disclosed to scheme members in the annual report and accounts or in the Statement of Investment Principles.	The Fund's Sustainability Policy and its Statement on Non-financial Factors and Social Investing are included as part of the ISS The Fund is also a member of the Local Authority Pension Fund Forum (LAPFF) which considers responsible investment on a collaborative basis.	Full
Trustees should consider the potential for engagement to add value when formulating investment strategy and selecting investment managers.	In formulating investment strategy, the Fund is always mindful of sustainability issues and these are an increasing focus for the Fund across all asset classes. Similarly, when appointing managers, questions are asked about engagement and sustainability although this is probably not given sufficient weight in the evaluation of managers for selection. To ensure best practice, the Fund has produced its own Sustainability Policy which is regularly monitored and managed. In all manager selection exercises undertaken, the sustainability policy that fund managers apply to their investments is reviewed.	Full
Trustees should ensure that investment managers have an explicit strategy, setting out the circumstances in which they will intervene in a company.	The Fund is aware of the voting policies of its underlying managers. A questionnaire is issued periodically to all fund managers on their sustainability policy and their replies explain their approach.	Full
Trustees ensure that Investment Consultants adopt the ISC's Statement	The Investment Consultant supports and adheres to the standard agreed with the investment consulting industry	Full



## Principle 6

Trustees should act in a transparent manner, communicating with stakeholders on issues relating to their management of investment, its governance and risks, including performance against stated objectives. Trustees should provide regular communication to members in the form they consider most appropriate.

Key Areas and Guidance	Comment & Actions	Compliance
Reporting ensures that the scheme operates transparently and enhances accountability to scheme members and best practice provides a basis for the continuing improvement of governance standards.	Details of the Fund's Communication Policy Statement and all other key reports – ISS, Annual Report, Corporate Governance Policy Guidelines, Funding Strategy Statement, Governance Compliance Statement and Myners' Principles Compliance Statement are all published on the Fund's website. A newsletter is also published periodically. The other two main Scheduled Bodies (Denbighshire and Wrexham) have representation on the Committee along with an employee representative and other employer representative to ensure transparency.	Full

## Appendix B – FRC UK Stewardship Code – 2014/15 Compliance

Principles	Comment & Actions	Compliance
<b>Principle 1</b>		
Institutional investors should publicly disclose their policy on how they will discharge their stewardship responsibilities.	<p>The Clwyd Pension Fund takes its responsibilities as a shareholder seriously. It seeks to adhere to the Stewardship Code and encourages its appointed asset managers to do so too. In practice the Fund's policy is to apply the Code both through its arrangements with its asset managers and other agents and through membership of collaborative groups. The Fund makes this explicit through its Sustainability Policy document.</p> <p>The Fund's investment strategy seeks long-term returns from investing in a highly diversified portfolio of assets and appoints asset managers who best reflect this long-term sustainability approach in their investment philosophy and process.</p>	Full
<b>Principle 2</b>		
Institutional investors should have a robust policy on managing conflicts of interest in relation to stewardship and this policy should be publicly disclosed.	Through its Sustainability Policy, the Fund encourages the asset managers it employs to have effective policies addressing potential conflicts of interest, when it comes to matters of stewardship. The Fund requires all those who are directly involved in its management and governance to disclose any interest in any company, or other entity, in which the Fund has an ownership interest.	Full
<b>Principle 3</b>		
Institutional investors should monitor their investee companies.	Day-to-day responsibility for managing our equity holdings is delegated to the Fund's appointed asset managers. The Fund expects them to monitor companies, and intervene where necessary, and to report back regularly on activity undertaken. Regular review meetings with the Fund's asset managers provide an opportunity for particular company issues to be discussed. Under the Fund's Sustainability Policy, managers are required to report any areas of concern.	Full

<b>Principle 4</b>		
Institutional investors should establish clear guidelines on when and how they will escalate their activities as a method of protecting and enhancing shareholder value.	Whilst there is broad guidance in the Fund's ISS and Sustainability Policy, as noted earlier responsibility for day-to-day interaction with companies is delegated to the Fund's asset managers, including the escalation of engagement when necessary. Their guidelines for such activities are expected to be disclosed in their own statement of adherence to the Stewardship Code.	Full
<b>Principle 5</b>		
Institutional investors should be willing to act collectively with other investors where appropriate.	The Fund seeks to work collaboratively with other institutional shareholders in order to maximize the influence that it can have on individual companies. The Fund is a member of the Local Authority Pension Fund Forum (LAPFF), which engages with companies on environmental, social and governance issues on behalf of its member authorities. The LAPFF is a signatory to the United Nations Principles for Responsible Investing.	Full
<b>Principle 6</b>		
Institutional investors should have a clear policy on voting and disclosure of voting activity.	Whilst all the Fund's holding are through pooled voting, it takes its voting responsibilities seriously and its voting policy is detailed as part of its ISS and in its Sustainability Policy document. Within this constraint, the Fund seeks to exercise the voting rights attaching to all its UK equity holdings and, where practical, its overseas stocks. A summary of manager voting is included in the Fund's Annual Report.	Full, but further improvements are possible
<b>Principle 7</b>		
Institutional investors should report periodically on their stewardship and voting activities.	The Fund reviews its ISS and Sustainability Policy document on an annual basis and publishes these both in the Annual Report and Accounts and on the Fund's web site. In addition, the activity undertaken by the LAPFF is reported to the Pension Fund Advisory Panel as are summary voting records from managers. All managers provide details of voting activity and a summary is provided in the Fund's Annual Report.	Partial