THE CARDIFF & VALE OF GLAMORGAN PENSION FUND

INVESTMENT STRATEGY STATEMENT

MARCH 2017

Introduction

City of Cardiff Council ('the Council') is the administering authority for the Cardiff & Vale of Glamorgan Pension Fund ('the Fund')

The Local Government Pension Scheme (Management & Investment of Funds) Regulations 2016 ("the Investment Regulations") require administering authorities to formulate and publish an investment strategy.

The Investment Strategy Statement (ISS) required by Regulation 7 of the Regulations 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 policy 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 of fund money that it will invest in particular investments or classes of investment.

The ISS must comply with guidance issued from time to time by the Secretary of State, currently the guidance issued in September 2016.

The Terms of Reference of City of Cardiff Council's Pensions Committee ('the Committee') include determining the authority's investment strategy. This statement sets out the strategy for the 2017-18 financial year and has been prepared in consultation with the Fund's Investment Advisory Panel ('the Panel')

A Investment of money in a wide variety of investments

A properly diversified portfolio of assets should include a range of asset classes to help reduce overall portfolio risk. If a single investment class is not performing well, performance should be balanced by other investments which are doing better at that time. A diversified portfolio also helps reduce volatility.

The Committee aims to meet the requirement for a diversified portfolio by reviewing its Strategic Asset Allocation on an annual basis. The Asset Allocation is approved by the Committee on the advice of the Panel. The Panel considers a wide range of investment opportunities before making its recommendations.

Current asset classes included in the allocation are:

- Conventional & Index Linked Fixed Interest - UK & Overseas
- Equities - UK & Overseas (USA, Europe, Far East, Emerging Markets)
- Private Equity (via pooled funds of funds)
- Property funds – UK & Global

The following investment related activities are also permitted:

- Derivatives and other financial instruments within pre-agreed limits for the purpose of efficient portfolio management or for specific purposes such as currency hedging
- Underwriting, provided the underlying stock is suitable on investment grounds and complies with existing investment criteria
- Stock lending

The Asset Allocation targets and variance limits agreed for 2017-18 are summarised below.

Asset class	**Target Allocation %**	**Variance Limits %**
UK Equities	34.0	+/- 5
Overseas Equities	35.0	+/- 5
Bonds & Cash	18.5	+/- 5
Property	7.5	+/- 5
Private Equity	5.0	+/- 2.5
Total	**100.0**	

Investment Limits

The Investment Regulations in force between 2009 and 2016 set statutory limits for different types of investments. The 2016 Investment Regulations removed these limits but the Fund will continue to operate within the limits in column 2 of Schedule 1 to the 2009 Regulations in respect of any assets not yet transitioned to the Wales Investment Pool.

B Suitability of particular investments and types of investments

The investment policy of the Fund is intended to ensure that all statutory payments made from the Fund are at minimal cost to employing bodies.

The overall investment objective is to maximise investment returns and to minimise or at least stabilise future employer contributions over the long term within an acceptable level of risk. Investment returns are defined as the overall rates of return (capital growth and income combined). It is also recognised that investments are intended to preserve and enhance the Fund's value.

The statutory requirement is to move towards 100% funding of the Fund's accrued liabilities over a period of time. This period together with the funding level is calculated every three years and agreed with the Actuary following a review that assesses the adequacy of the Fund's assets to meet its liabilities. The Panel takes the actuarial position and funding level into account in formulating its advice.

The Fund sets its own customised benchmark to ensure that the Fund's asset allocation policy reflects its own characteristics and not the average of a peer group. The benchmark is set in line with a long term Fund Objective of a 75/25 Equities/Bonds asset allocation split. The split was set in 2004, following an asset/liability study, with the aim of minimising, or at least stabilising, future employer contributions and to avoid large variations. The Panel will regularly review the overall asset allocation and consider appropriate opportunities for a further asset-liability study.

Expected Return on Investments

The investment method is to appoint expert specialist fund managers with clear targets and maximum accountability for performance. The current targets for each mandate are as follows:

Portfolio	Portfolio Benchmark Index	Portfolio Target
Cash	L Authority 7 day	Index
Global Bonds	20% FTSE UK Gilts 30% iBoxx £ Corporate Bonds 20% Citigroup World Govt Bond (£ hedged) 20% £ LIBOR 3 months 10% JPM Emerging Markets Bonds (£ hedged)	Composite Index +1% p.a. over rolling 3 yr. periods
UK Equities (Active)	FTSE All Share	Index + 2%, over rolling 3 year periods

UK Equities (Passive)	FTSE All Share	Index +/- 0.25-0.3% p.a.
USA Equities (Passive)	FTSE USA	Index +/- 0.25% p.a.
Europe Equities (Active)	FTSE Europe ex UK	Index + 2%, over rolling 3 year periods
Japan Equities (Active)	TOPIX	Index + 3%, over rolling 3 yr. periods
Asia Pacific Equities (Active)	FT AW Asia ex-Japan	Index + 3% over rolling 3 yr. periods
Emerging Market Equities (Active)	MSCI Emerging Markets	Index + 3% p.a. over rolling 4 yr. periods
UK Property	Various (balanced PUT indices)	Various
Global Property	N/A	Absolute Return of 10% p.a.
Private Equity	N/A	None set *

* Though no formal target has been set, the rationale for private equity is that it should outperform quoted equities over an equivalent period.

C Risk

A detailed schedule of the main risks to the Fund is set out in the Funding Strategy Statement. Risks arising from investments are monitored by the Investment Advisory Panel. The Fund recognises the risks arising from holding a higher proportion of equities and other return seeking assets than would be held under a liability-driven strategy but considers that these risks are mitigated by the strong covenant of the Fund's principal employers and the stable maturity profile of its membership.

Investment Risk is the risk that the Fund's managers fail to achieve the rate of investment return assumed in setting their mandates. The primary control over investment risk is the diversification of assets across markets and asset classes. Correlations amongst these will vary over time, but the underlying risk of exposure to a specific capital market is mitigated to some extent by a diversifying strategy such as that followed by the Fund.

While currency risk is inherent in a diversified strategy, it is addressed to a degree through the use of a specialist manager to hedge exposures where currencies in which the fund is invested appear to have reached extreme valuations.

The individual specialist fund managers manage the risk of variation from benchmarks consistent with the targets they have been given. Current risk measures/targets for the segregated active mandates, based on the industry standard risk methodology, are as follows:

Portfolio	**Tracking Error**
UK active equities	3 - 6%
Japan equities	Target 4%
Asia Pacific equities	3 – 6%
Emerging Market equities	Target 8%
Global Bonds	0 - 3%

Relative risk levels for active managers are reported quarterly and discussed annually by the Panel. For pooled vehicles (including passive investments) the manager reports the risk of the pooled vehicle as a whole. The Panel recognises that tracking error itself can be a volatile measure of the risks being taken by a manager and that ex post statistics may vary considerably from ex ante estimates. As such, its predictive value needs to be treated with care. The tracking error is therefore used as a guide when considering overall manager performance.

Liquidity Risk is the risk that the Fund cannot meet its immediate liabilities because it has insufficient assets. The Fund monitors its liquidity position carefully to ensure that it is not a seller of long term assets to make benefit payments. At least 80% of the Fund's assets are highly liquid. The Equity and Global Bond managers are required to hold only assets readily realisable at the time of purchase. Any material investment with an in-house or pooled fund, which is not readily tradable, would require specific approval.

Private equity is not normally easily realisable. Higher investment returns relative to conventional equities are expected, reflecting the greater risk inherent in this fact.

Operational risks arise through the implementation of the Fund's investment strategy. These risks are set out below:

- Transition risk – the Fund may incur unexpected costs in relation to the transition of assets between managers and/or asset classes. When carrying out significant transitions, the fund takes professional advice and considers the use of specialist transition managers in order to mitigate this risk when it is cost effective to do so.

- Custody risk – the Fund must ensure that it retains the economic rights to all Fund assets, when held in custody or being traded. It does this through the use of a global custodian (Northern Trust) for custody of assets, the use of formal contractual arrangements for all investments and by maintaining independent investment accounting records.

- Credit default risk – a counterparty related to a Fund investment could fail to meet its obligations. The Fund's investment managers are required under their asset management contracts to manage counterparty risk on behalf of the Fund.

- Stock-lending risk – the possibility of default and loss of economic rights to Fund assets. Stock lending is managed by the Fund's custodian and appropriate counterparty and collateral controls are in place.

D Pooling of Investments

The Cardiff & Vale of Glamorgan Pension Fund is one of the eight funds participating in the Wales Investment Pool ('the Pool'). The proposed structure and basis on which the Pool will operate was set out in the July 2016 submission to the Department for Communities and Local Government. The proposals were approved by the Minister for Local Government in November 2016.

Assets to be invested in the Pool

The Council's intention is to invest the Fund's assets through the Pool as and when suitable Pool investment solutions become available. An indicative timetable for investing through the Pool was set out in the July 2016 submission. The key criteria for assessment of Pool solutions will be as follows:

- That the Pool enables access to an appropriate solution that meets the objectives and benchmark criteria set by the Fund

- That there is a clear financial benefit to the Fund in investing in the solution offered by the Pool

At the time of preparing this statement, the Fund has already invested the following assets through a collaborative procurement carried out in 2016 with the other seven funds in Wales:

Asset class	Manager	% of Fund assets (allocation target)	Benchmark	Performance Objective
Passive UK Equities	BlackRock	19.0	FTSE All-Share	Benchmark
Passive US Equities	BlackRock	10.0	FTSE All-World USA	Benchmark

It is anticipated that the Fund's existing private equity investments will not be transitioned into the Pool but will be replaced by suitable pooled or collaborative investments as they mature over the next 10-15 years. It is intended that all other asset classes will be transitioned to the Pool as soon as practicable.

Structure and governance of the Wales Investment Pool

The Pool will appoint a third-party Operator authorised by the FCA to provide a range of investment sub-funds in which the assets of the eight participating funds will be invested.

A Joint Governance Committee (JGC) will be established to oversee the Operator. The JGC will comprise one elected member from each constituent administering authority and will be supported by an Officer Working Group. One of the eight funds will act as Host Authority to provide administrative and secretarial support to the Pool.

The Terms of Reference of the JGC and the roles of the Officer Working Group and Host Authority will be set out in a legally binding Inter Authority Agreement to be approved and signed by the eight administering authorities. The responsibilities of the JGC will include:

- Monitoring the performance of the Pool Operator
- Making decisions on asset class sub-funds to be made available by the Operator to implement the individual investment strategies of the eight funds
- Providing accountability to the participating funds on the management of the Pool

- Having responsibility for reporting on the Pool to the UK Government and other stakeholders
- Having oversight of the Officer Working Group

The eight administering authorities will continue to retain control over setting their investment strategy and asset allocation.

E How social, environmental or corporate governance considerations are taken into account

The Fund seeks to identify investment opportunities which do not conflict with its fiduciary duties to seek an optimum return, whilst wishing at the same time to take account of social, environmental and ethical concerns and issues. The Fund also directly supports the development of clean technology through its private equity portfolio.

Annual reports will be provided on managers' corporate governance policies and practices, and annual presentations from equity managers will include a reference to their corporate governance actions where appropriate (e.g. segregated mandates). All of the Fund's assets are held through fund managers that have adopted the UN Principles for Responsible Investing, or the equivalent UK Stewardship Code, and future equity tenders will refer to these criteria.

F The exercise of rights (including voting rights) attaching to investments

Where relevant, IMAs will incorporate the Institutional Shareholders Committee (ISC) principles on the responsibilities of institutional shareholders and agents to ensure managers have an explicit strategy elucidating the circumstances in which they will intervene in a company, the approach to be used, and how to measure the effectiveness of this strategy.

Currently, the passive funds and the UK active managers all use the ISC principles, including actively engaging with investee companies. The overseas managers engage via normal contacts between companies and analysts or discussions on specific concerns.

Regarding voting, all passive and active funds vote where practicable according to principles provided to the Corporate Director Resources, reporting periodically on action taken. In the case of segregated mandates, however, care will be taken to ensure that, where applicable, the Fund's policies are not overridden, negated or diluted by the general policy of a manager. In any case the Fund retains the ultimate right to override the managers' decisions at any time, and to vote according to its own wishes.

The Fund is a member of the Local Authorities Pension Fund Forum (LAPFF) to enable it to act collectively with other LGPS funds on corporate governance issues.