THE CARDIFF & VALE OF GLAMORGAN PENSION FUND

INVESTMENT STRATEGY STATEMENT

JANUARY 2020

Introduction

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 July 2017.

The Terms of Reference of Cardiff Council's Pensions Committee ('the Committee') include determining the authority's investment strategy. This statement sets out the strategy for the 2020-21 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 – Global
- Equities – Global, UK & 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

The Asset Allocation targets and variance limits currently in force together with the portfolio benchmarks and targets are summarised in Appendix 1.

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 Pensions Partnership.

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 Committee 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 was originally set in 2004 in line with a long term Fund Objective of a 75/25 Equities/Bonds asset allocation split. The allocation to Bonds was increased in 2017 to reflect an improvement in the Fund's projected funding level. The Panel will regularly review the overall asset allocation and consider appropriate opportunities for a further asset-liability study.

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.

The individual specialist fund managers manage the risk of variation from benchmarks consistent with the targets they have been given. Relative risk levels for active managers are reported quarterly and discussed annually by the Panel. 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 held in publicly listed equities and bonds which can be readily realised. Investments in property and private equity are long term investments which the Fund is less likely to be able to realise in a short period.

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.

D Pooling of Investments

The Cardiff & Vale of Glamorgan Pension Fund is one of the eight funds participating in the Wales Pension Partnership (WPP). The proposed structure and basis on which the WPP operates 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 WPP

The Committee's intention is to invest the Fund's assets through the WPP as and when suitable pooled investment solutions become available. By 1 June 2020 it is expected that the allocations to active Global Equities, active UK Equities and Global Bonds will have been invested via WPP sub-funds. Pooling solutions for Emerging Market Equities and Alternative Assets are under development.

The Fund's allocations to passive Equities have been invested through pooled funds managed by BlackRock following a collaborative procurement carried out in 2016 with the other seven funds in Wales.

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.

Structure and governance of the Wales Pension Partnership

The WPP has appointed Link Fund Solutions to establish and operate a collective investment vehicle for the sole use of the LGPS funds in Wales. Link have established an Authorised Contractual Scheme (ACS) on behalf of the WPP and are developing a range of sub-funds in which the assets of the eight participating pension funds can be invested. Link are supported by Russell Investments who advise on sub-fund design and manager selection. Northern Trust have been appointed as the ACS Custodian.

A Joint Governance Committee (JGC) was established in 2017 to oversee the Operator. The JGC comprises one elected member from each constituent administering authority and is supported by an Officer Working Group. Carmarthenshire Council acts as Host Authority to provide administrative and secretarial support to the WPP.

The Terms of Reference of the JGC and the roles of the Officer Working Group and Host Authority have been set out in a legally binding Inter Authority Agreement approved and executed by the eight administering authorities. The responsibilities of the JGC 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 WPP
- Having responsibility for reporting on the WPP to the UK Government and other stakeholders
- Having oversight of the Officer Working Group

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

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

The Committee 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. It recognises the concerns of the Council and other stakeholders regarding climate change and will develop its investment strategy in response to those concerns. Subject to being consistent with its fiduciary duties and regular assessments by the Panel of the impact of investment decisions, the Committee will consider:

- Increasing its allocation to the Low Carbon Tracker fund
- Engaging with investment managers and companies through WPP and LAPFF
- Disinvestment from companies representing a continuing risk who do not respond positively to engagement
- Positive investment in companies developing clean technology

The Committee will expect the investment managers appointed via the WPP to adopt the relevant stewardship principles (either the UN Principles for Responsible Investing or the UK Stewardship Code) and to report on their compliance.

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.

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

The long term investment interests of LGPS funds are enhanced by the highest standards of corporate governance and corporate responsibility amongst the companies in which they invest. Poor governance can negatively impact shareholder value.

The Fund will participate in the development of voting and engagement policies for the WPP which promote high standards of corporate governance, including transparency and accountability by companies for the environmental and social impacts of their business activities.