

INVESTMENT STRATEGY STATEMENT

Introduction

1. The County Council is an administering authority of the Local Government Pension Scheme (the “Scheme”) as specified by the Local Government Pension Scheme Regulations 2013 (the LGPS Regulations). It is required by Regulation 53 of the LGPS Regulations to maintain a pension fund for the Scheme.
2. The Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016 (the “Investment Regulations”) govern the management of the pension fund and the investment of fund money. According to Regulation 7 of the Investment Regulations an administering authority must formulate an investment strategy which must be in accordance with guidance issued from time to time by the Secretary of State. It must publish a statement of its investment strategy and must review and if necessary revise its investment strategy at least every 3 years.
3. The investment strategy statement must include:
 - a) a requirement to invest fund 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 assessed 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 and corporate governance considerations are taken into account in the selection, non-selection, retention and realisation of investments
 - f) the authority’s policy on the exercise of the rights (including voting rights) attaching to investments.

Purpose and Principles

4. The purpose of the Fund is to:
 - Pay pensions, lump sums and other benefits provided under the LGPS Regulations
 - Meet the costs associated in administering the Fund
 - Receive contributions, transfer values and investment income
 - Invest any Fund money not needed immediately to make payments.
5. The following principles underpin the Fund’s investment activity:
 - The Fund will aim to be sufficient to meet all its obligations on a continuing basis
 - The Fund will be invested in a diversified range of assets

- Proper advice on diversification and the suitability of types of investment will be obtained and considered
- The Fund will aim to conduct its business and to use its influence in a long term responsible way.

Key Parties

6. The key parties involved in the Fund's investments and their responsibilities are as follows.

The Administering Authority

7. The Administering Authority for the Pension Fund is Nottinghamshire County Council. Under the terms of the Council's constitution, the functions of the Council as administering authority are delegated to the Nottinghamshire Pension Fund Committee supported by two Sub-Committees. The full governance arrangements of the Fund are detailed in the Fund's Governance Compliance Statement.
8. The members of the Committees are not trustees (as the LGPS is a statutory scheme) but do have fiduciary duties towards the scheme members and employers.

Committee Members

9. The Committee Members recognise their full responsibility for the oversight of the Fund, and operate to a Code of Conduct. They shall:
 - Determine the overall asset allocation and investment strategy of the Fund
 - Determine the type of investment management to be used and, until LGPS Central is operational, appoint and dismiss fund managers
 - Receive regular reports on performance from the main fund managers and question them regularly on their performance
 - Receive independent reports on the performance of fund managers on a regular basis
 - Be encouraged to receive suitable training to help them discharge their responsibilities and attend such training courses, conferences and meetings that deliver value for money to the Fund.

Chief Finance Officer

10. Under the Council's constitution, the Service Director (Finance, Procurement & Improvement) is designated the Council's Chief Finance Officer (also known as the Section 151 Officer). The Group Manager (Financial Management) is the deputy Section 151 Officer. Financial Regulations specify that the Section 151 Officer is responsible for arranging the investment of the Pension Fund. Operational matters falling under this responsibility are exercised by the Senior Accountant (Pensions & Treasury Management).
11. Authorised signatories for operational matters relating to pension fund investments are:
 - Service Director (Finance, Procurement & Improvement)
 - Group Manager (Financial Strategy & Compliance)
 - Group Manager (Financial Management)
 - Senior Accountant (Pensions & Treasury Management)
 - Investments Officer

12. Representatives of the Service Director (Finance, Procurement & Improvement) provide advice to the Trustees and attend meetings of the Pension Fund Committees as required.

Independent Adviser

13. The Fund has an Independent Adviser who attends meetings of the Pensions Investment Sub-Committee, Pensions Sub-Committee and Pensions Working Party as required. This is considered best practice in accordance with the requirements for “proper advice” in the governing regulations.
14. The independent adviser is engaged to provide advice on:
- the objectives and policies of the fund
 - investment strategy and asset allocation
 - the fund’s approach to responsible investment
 - choice of benchmarks
 - investment management methods and structures
 - choice of managers and external specialists
 - activity and performance of investment managers and the fund
 - the risks involved with existing or proposed investments
 - the fund’s current property portfolio and any proposals for purchases, sales, improvement or development
 - new developments and opportunities in investment theory and practice.

LGPS Central

15. LGPS Central is the asset pool in which the Nottinghamshire Fund is participating in order to meet the government’s criteria for investment reform issued in November 2015. The County Council jointly owns LGPS Central Ltd, the operating company which is intended to achieve FCA regulation and manage collective investment vehicles on behalf of the participating funds.

Asset Allocation

16. It is widely recognised that asset allocation is the most important factor in driving long term investment returns. The balance between different asset classes depends largely on the expected risk/return profile for each asset class and the target return for the Fund. It is also recognised that investment returns play a significant role in defraying the cost of providing pensions by mitigating the contributions required from employers.
17. Employers’ contributions are determined as part of the triennial actuarial valuation of the Fund. The actuarial valuation involves a projection of future cash flows to and from the Fund and its main purpose is to determine the level of employers’ contributions that should ensure that the existing assets and future contributions will be sufficient to meet all future benefit payments from the Fund. This is the main funding objective as set out in the Funding Strategy Statement.
18. The Fund Actuary estimates the future cash flows which will be paid from the Fund for the benefits relating to service up to the valuation date. They then discount these projected cash flows using the discount rate to get a single figure for the value of the past service liabilities. This figure is the amount of money which, if invested now, would be sufficient to make these

payments in future provided that the future investment return was equal to at least the discount rate used.

19. The discount rate is based on the expected long term future investment returns from various asset classes. At the latest valuation, these were as follows:

Asset Class	Expected Return (pa)
Equities	7.4%
Gilts	2.4%
Other Bonds	3.3%
Property	5.9%
Cash	1.8%
Discount Rate	5.4%
Fund Target Return	6.0%

20. At the latest valuation, the Fund was assessed to have a deficit of £621m and a funding level of 87%. Deficit recovery contributions have been certified for the majority of employers but any returns in excess of the discount rate will help to recover the Fund to a fully funded position. The Fund will therefore target an annual return rate of 6%.
21. The agreed asset allocation ranges for the Fund are shown below along with the Fund's strategic benchmark and liability based benchmark.

Asset Class	Allocation Ranges	Strategic Benchmark	
Equities	55% to 75%	FTSE All Share World	65.0%
Property	5% to 25%	IPD annual	15.0%
Bonds	10% to 25%	FTSE UK All Stock	17.5%
Cash	0% to 10%	LIBID 7 Day	2.5%
Liability Based Benchmark		FTSE UK Gilts (5 Yrs)	100.0%

22. These ranges are aimed at achieving appropriate returns to meet the funding objective within acceptable risk parameters. The Fund will vary between the asset classes according to market circumstances, relative performance and cash flow requirements. The ranges will be kept under regular review and, if it appears likely that these limits might be breached because of market movements, reference will be made to a meeting of the Pensions Working Party for advice.
23. The asset allocation currently favours "growth assets" (equities and property) over "defensive assets" (bonds and cash) as the former are expected to outperform the latter over the long term. Although net additions from members (contributions received less benefits paid) are now expected to be negative for the foreseeable future, the Fund receives significant investment income and a recent report by the Fund Actuary shows that the Fund is unlikely to need to sell assets to pay benefits for at least 20 years. This allows the Fund to continue to implement a long term investment strategy.

24. As the funding level approaches 100%, the asset allocation will be reviewed to consider whether it is appropriate to change the mix of growth versus defensive assets.

Investment Strategy

Requirement to invest fund money in a wide variety of investments

25. The Fund will be invested in a diversified range of assets. The fund will be diversified across multiple asset classes with different risk return expectations and correlations to deliver the targeted return of the Fund. The Fund may invest in quoted and unquoted securities of UK and overseas markets including equities and fixed interest and index linked bonds, cash, property, infrastructure and commodities either directly or through pooled funds. These asset classes are only examples of the types of investments that may be held, and are not intended to be an exhaustive list.

Assessment of the suitability of particular investments and types of investments

26. Subject to the LGPS regulations on allowable investments the fund may invest in a wide range of assets and strategies including quoted equity, Government and Non-Government bonds, currencies, money markets, commodities, traded options, financial futures and derivatives, alternative strategies, private equity and debt markets, Infrastructure and Property. Investment may be made in-house, indirectly (via funds) in physical assets or using derivatives. The fund will also use external managers to carry out stock lending ensuring suitable controls/risk parameters are put in place to prevent losses. Where an asset class/strategy is not expected to help in delivering the risk adjusted investment return required it will not be held.

Approach to risk, including the ways in which risks are to be assessed and managed

27. The risk tolerance of the Fund is agreed with the Pensions committee, the investment team and independent advisor through the setting the investment beliefs, funding and investment objectives. The Fund will only take sufficient risk in order to meet the target return set out in paragraph 19 of 6%.
28. The fund is exposed to Investment, operational, governance and funding risks. These risks are identified, measured, monitored and then managed. This is carried out using risk registers with section responsibility and over sight from the Head of Governance/CRO.

Approach to pooling investments

29. The Fund is entering the LGPS Central pool with the understanding that the pooled investments will benefit from lower investment costs, greater investment capability and access to more uncorrelated asset classes. Becoming an FCA registered investment manager will lead to improved governance, transparency and reporting giving the Pension Fund assurance that it's investments are being carried out effectively.
30. It is expected that virtually all of the Fund's assets will be transferred to the Pool on 1st April 2018, although it will take some time for the Pool to restructure the assets into appropriate sub-funds within the Pool. These sub-funds are likely to be set-up over a period of 2 – 3 years, with the timing being dependent on market conditions and operational circumstances, and

until such time as the appropriate sub-fund is set up the assets transferred into the Pool will be overseen by LGPS Central on behalf of the Fund.

31. The detailed business case for LGPS Central demonstrates how the proposal will meet the four key assessment criteria laid down by the government:
 - Asset pool(s) that achieve the benefits of scale (>£25billion)
 - Strong governance and decision making
 - Reduced costs and value for money
 - Improved capacity and capability to invest in infrastructure
32. The business case outlined the proposed governance, oversight and management structure of the pool and this has been reviewed by Eversheds, the legal advisers appointed by the pool.
33. The structure will allow participating funds to exercise control (both individually, and collectively) over the new arrangements, not only as investors in the pooled funds, but also as shareholders of the operator company, LGPS Central Ltd.
34. Whilst assets will be managed on a pooled basis, each fund will be able to exercise their investor rights independently, although benefits of scale will be most effectively harnessed where parties work together in a co-ordinated way to align their decision making. An important example of this is responsible investment and voting policies where cross-voting between funds within the same pool would be both costly to administer and counter-productive.
35. The Shareholders Forum, governed by a Shareholders Agreement and operating under company law, will have formal decision making powers. Nottinghamshire County Council will have equal voting rights alongside the other participating funds, and unanimous decisions will be required on key strategic matters. These will be specified in the Shareholders Agreement and Articles of Association and will include the appointment and dismissal of the company's senior executives, approval of the company's strategic plan and any significant financial transactions, such as major acquisitions, lending or borrowing.
36. The degree of control to be exercised by the Shareholders through their reserve powers will be greater than is generally the case, in order to satisfy the Teckal exemption criteria and allow the company to undertake services on behalf of the investor funds without a formal procurement process.
37. The Joint Committee, established by an Inter-Authority Agreement, will be the forum for dealing with common investor issues, and for collective monitoring of the performance of the pool against the agreed objectives of LGPS Central. It will however, have no formal decision making powers and recommendations will require the approval of individual authorities, in accordance with their local constitutional arrangements.
38. The government has made clear their expectation that pooled entities should be regulated by the Financial Conduct Authority (FCA) to ensure appropriate safeguards over the management of client monies. As such, LGPS Central Ltd will be subject to on-going oversight by the FCA and key management positions, including the company directors, will need to be 'approved persons', able to demonstrate appropriate knowledge, expertise and track record in investment management. These positions also carry significant personal liability for their actions and decisions.

39. The detailed business case has been reviewed by a joint DCLG/HMT Review Panel, and Ministerial consent to proceed has been received.
40. Comprehensive programme governance arrangements are in place to ensure that the statutory deadline for the implementation of pooling is achieved and that costs and savings are managed in accordance with the agreed business case. The s151 officers of each of the participating funds sit on the LGPS Central Programme Board and regular joint meetings are held between the Chairs and Vice-Chairs of the respective Pension Fund Committees to ensure effective member oversight of progress and delivery. The Nottinghamshire Pension Fund Committee, the Pensions Sub-Committee and the Local Pensions Board are also being updated regularly on key developments and decisions.
41. Expert advisers have been appointed to provide support on legal matters, FCA registration, taxation and overall programme management.

Policy on social, environmental and corporate governance considerations

42. Social, environmental and corporate governance considerations are taken into account in the selection, non-selection, retention and realisation of investments.
43. It is recognised that ESG factors can influence long term investment performance and the ability to achieve long term sustainable returns. The Committee consider the Fund's approach to ESG in two key areas:
- a. Sustainable investment / Environmental and social factors – considering the financial impact of environmental, social and governance (ESG) factors on its investments.
 - b. Stewardship and governance – acting as responsible and active investors/owners, through considered voting of shares, and engaging with investee company management as part of the investment process.
44. In combination these two matters are often referred to as 'Responsible Investment', or 'RI' and this is the preferred terminology of the fund. The Committee takes RI matters seriously and will not appoint any manager unless they can show evidence that RI considerations are an integral part of their investment decision-making processes. Following appointment managers are required to report any changes in their approach to RI to Officers.

Policy on the exercise of the rights (including voting rights) attaching to investments

45. The policy of the Fund will be to treat the equity allocation as a block aimed at maximising the financial returns to the funds (and thus minimising employers' contributions) consistent with an acceptable level of risk. The block of Bonds, Property and Cash is aimed at lowering overall risk (at the cost of anticipated lower return).
46. The Trustees have agreed an allocation to private equity and infrastructure. This will be effected principally through fund of funds arrangements to increase diversification and reduce risk. The allocation is based on *committed* amounts and, owing to the nature of these funds, the actual net investment level will be significantly lower. New investments will be made over time to target a commitment level of 10% of the Fund (within an allocation range up to 15% to allow for movements in market value).

47. Investments, such as private equity and infrastructure, that fall outside the high level asset classes will be included within the most appropriate class for reporting purposes and assessed against the relevant part of the strategic benchmark.
48. Cash will be managed and invested on the Fund's behalf by the County Council in line with its treasury management policy. The policy is to invest surplus funds prudently, giving priority to security and liquidity rather than yield. If losses occur, however, the Fund will bear its share of those losses.
49. Pension fund cash is separately identified each day and specific investment decisions will be made on any surplus cash identified, based on the estimated cash flow requirements of the Fund. As the majority of cash is allocated to individual investment managers and may be called by them for investment at short notice, it is expected that the majority of cash will be placed on call or on short-term fixed deposits. Unallocated balances may be placed directly with the Fund's custodian.
50. Joint investments using a combination of Fund cash and County Council cash may be made where this is in the best interests of the Fund. In considering such investments, guidance issued by the Department for Communities and Local Government will be followed and the Fund will receive its fair share of interest in proportion to the share of cash invested.
51. Other asset classes, such as hedge funds and currency, will be reviewed as part of the regular asset allocation strategy review and, if a decision to invest in other assets is made, the Investment Strategy Statement will be revised accordingly.

Risk Management

52. The Fund has adopted a Risk Management Strategy to:
- a) identify key risks to the achievement of the Fund's objectives
 - b) assess the risks for likelihood and impact
 - c) identify mitigating controls
 - d) allocate responsibility for the mitigating controls
 - e) maintain a risk register detailing the risk features in a)-d) above
 - f) review and update the risk register on a regular basis
 - g) report the outcome of the review to the Nottinghamshire Pension Fund Committee.
53. The Risk Register is a key part of the strategy as it identifies the main risks to the operation of the Fund, prioritising the risks identified and detailing the actions required to further reduce the risks involved.
54. A key part of managing the investment risk is by ensuring an adequate number of suitably qualified investment managers and by requiring managers to hold a diversified spread of assets, which will be reviewed regularly by the Pensions Investment Sub-committee. The level of risk in the equities block will be managed by a balance between passive and active management that may be varied from time to time, according to performance and emerging knowledge and experience of the market. This will continue as the Fund moves to pooled investments, with asset allocation decisions remaining with the Pensions Investment Sub-committee.

55. It is believed that active management can add value to the Fund but only over the long term, and decisions to appoint or dismiss fund managers will be given careful consideration. It is accepted that investment performance (particularly from equities) can be volatile but, as a long term investor, the Fund can ride out this volatility as long as projected net cash flow continues to be positive.
56. The correlation between UK and overseas markets has increased significantly over recent time, reflecting the increasing globalisation of the market. The Fund will take into account exchange rate risks when deciding the balance between holding of UK and overseas equities.. As a long term investor, the Fund does not undertake currency hedging. Individual managers may hedge currency risks but only with prior approval from the Fund. The Fund will only take risks commensurate with meeting the overall 6% return target.
57. In addition, the following advisory guidelines will apply. These guidelines will be reviewed from time to time, and if changes are made, these will be incorporated into a revised Investment Strategy Statement, and amendments will be published.
- Not more than 10% of the Fund to be invested in unlisted securities.
 - Not more than 10% of the Fund to be invested in a single holding.
 - Prior to pooling, not more than 25% of the Fund to be invested in securities which are managed by any one body, i.e. in a unit trust type arrangement.
 - Not more than 15% of the Fund to be invested in partnerships, with not more than 2% in any one partnership.
 - Not to enter into any stock lending arrangements.
 - No underwriting without prior approval.
 - No involvement in derivatives (including currency options) without prior approval.

Other Issues

58. The Fund's assets are held in custody by a combination of an independent custodian, investment managers and in-house. The performance of fund managers will be measured against individual benchmarks, and the overall fund, including cash returns, against the strategic benchmark. Performance will be measured by an independent agency. The statement of accounts will be audited by the County Council's external auditors.
59. The investment management arrangements of the Fund can be found in the latest annual report (available on the Fund's website, www.nottspf.org.uk). The Fund also publishes details of its holdings on the website on a quarterly basis.
60. This Investment Strategy Statement will be kept under review and will be revised following any material changes in policy.