

NICEIC Pension Scheme

# **Statement of Investment Principles**

June 2020

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This document is the Statement of Investment Principles for the NICEIC Pension Scheme (the Scheme). The requirement for the Trustee of the Scheme to have such a Statement in place was introduced by the Pensions Act 1995. The Statement comprises the following sections and appendices:

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# Section 1: Introduction

## Pensions Acts

- 1.1 Under the Pensions Act 1995 (as amended by the Pensions Act 2004), the Trustee is required to prepare a statement of the principles governing investment decisions. This document contains that statement and describes the investment policy pursued by the Trustee of the NICEIC Pension Scheme (the Scheme).

## Background

- 1.2 Before preparing this document, the Trustee has consulted the employer and will also consult the employer before revising this document. However, the ultimate power and responsibility for deciding investment policy lies solely with the Trustee.
- 1.3 Before adopting this document, the Trustee has sought advice from the Scheme's investment consultants, Willis Towers Watson, and has consulted the Scheme Actuary. The Trustee will review this document, in consultation with the investment consultant and the Scheme Actuary, at least once every three years, or sooner following an unscheduled actuarial valuation, or where the Trustee considers a review is needed for other reasons. Before preparing this document the Trustee has had regard to the requirements of the Pensions Act concerning diversification of investments and suitability of investments and the Trustee will consider those requirements on any review of this document or any change in investment policy. The Trustee will refer to this document where necessary to ensure it exercises its powers of investment so as to give effect to the principles set out in it as far as is reasonable.
- 1.4 The assets are held in pooled funds. Under Section 36 of the Pensions Act, such investments are termed direct investments and are classed as retained investments. It is therefore the Trustee's policy to obtain appropriate advice regarding the suitability of such investments on a regular basis.

## Scheme details

- 1.5 The Scheme operates for the exclusive purpose of providing retirement benefits and death benefits to eligible participants and beneficiaries.
- 1.6 The Scheme is a registered scheme for tax approval purposes, under the Finance Act 2004.

## **Financial Services and Markets Act**

- 1.7 In accordance with the Financial Services and Markets Act 2000, the Trustee will set general investment policy, but will delegate the responsibility for selection of specific investments to an appointed investment manager or managers, which may include an insurance company or companies. The investment managers shall provide the skill and expertise necessary to manage the investments of the Scheme competently.

## Section 2: Governance

- 2.1 The Trustee has ultimate responsibility for decision making on investment matters. In order to ensure that investment decisions are taken only by persons or organisations with the skills, information and resources necessary to take them effectively, the Trustee delegates some of these responsibilities.
- 2.2 Responsibility for all day-to-day investment decisions is delegated to the Scheme's investment managers. The Trustee retains direct responsibility for other investment matters which include:
- a Reviewing at least once every three years, or following any significant change in investment policy, the content of this Statement of Investment Principles and for modifying it if deemed appropriate, in consultation with the investment consultant and Scheme Actuary.
  - b Reviewing the investment policy following the results of each actuarial review, in consultation with the investment consultant and Scheme Actuary.
  - c Appointing (and dismissing) investment managers.
  - d Assessing the quality of the performance and processes of the investment managers by means of regular, but not less than annual, reviews of the investment results and other information, in consultation with the investment consultant and Scheme Actuary.
  - e Consulting with the employer before amending this Statement.
  - f Strategically allocating the assets and the cash flow of the Scheme between investment mandates and making periodic adjustments to the portfolio allocations.
  - g Monitoring compliance with this Statement on an ongoing basis.
- 2.3 Decisions affecting the Scheme's investment strategy are taken with appropriate advice from the Scheme Actuary and investment consultant and the Trustee's other advisers as appropriate.
- 2.4 The Trustee is satisfied that it has sufficient expertise and appropriate training to evaluate critically the advice received. The Trustee is also satisfied it has an appropriate set of skills, and the right structures and processes, to carry out its role effectively.
- 2.5 Only persons or organisations with the necessary skills, information and resources are actively involved in taking investment decisions affecting the Scheme. The Trustee of the Scheme draws on the skills and expertise of external parties including the investment managers, investment consultant and Scheme Actuary.

- 2.6 The Trustee is aware that it has the flexibility to open the contracts for actuarial services and investment advice to separate competition.

# Section 3: Division of responsibilities

## Investment managers

3.1 The investment managers' responsibilities include:

- Managing the pooled funds in which the Scheme is invested in a manner consistent with the stated objectives for those funds
- Providing the Trustee with quarterly statements of the assets along with a quarterly report on actions and future intentions, and any changes to the investment processes applied to the portfolios
- Informing the Trustee of any material changes in the internal objectives and guidelines of any pooled funds used by the Scheme and managed by the investment manager or an associated company
- Having regard to the need for diversification of investments so far as appropriate and to the suitability of investments
- Giving effect to the principles contained in the Statement as far as reasonably practicable.

## Investment consultant

3.2 The role of the investment consultant is to make recommendations or give advice to the Trustee in the following areas:

- the formulation of an efficient governance structure
- the regular updating of the Statement of Investment Principles
- the development of a clear investment strategy for the Scheme
- the asset-liability modelling process
- the construction of a strategic asset allocation benchmark given the liabilities of the Scheme and the risk and return objectives of the Trustee (see Sections 5, 7 and 8)
- the construction of an overall investment management structure that meets the objectives of the Trustee
- the selection and appointment of appropriate investment management organisations

- the consultant's current views of the investment managers employed by the Scheme
- potential new areas or tools of investment
- commentary on investment performance and risk taken by the managers
- trustee education
- general advice in respect of the Scheme's investment activities.

3.3 Fees are generally calculated by reference to the time spent on a particular assignment and the relevant charge-out rates applying to the associates who provide the services in question. For larger projects, for example reviews of investment strategy, fixed projects fees may apply.

### **Scheme Actuary**

3.4 The Scheme Actuary's responsibilities include:

- Performing the triennial (or more frequently, as required) valuations of the Scheme and advising on the appropriate contribution levels for the future.
- Assessing the position of the Scheme under the Statutory Funding Requirement ("SFR") for valuations with an effective date after 22 September 2005 and advising on the appropriate response to any shortfall.
- Liaising with the investment consultant on the suitability of the Scheme's investment strategy given the financial characteristics of the Scheme.

# Section 4: Objectives and long term policy

## Objectives

- 4.1 The Trustee's longer-term objective is to achieve a level of funding which will allow it to remove the large majority of investment risk from the Scheme and to be largely self-sufficient from the employer.
- 4.2 To achieve this objective, the Trustee has formulated a Journey Plan for the Scheme which is described as follows:
- The aim is to be 105% funded on a self-sufficiency basis by early 2028.
  - The self-sufficiency basis is defined by reference to the Technical Provisions liabilities but with a discount rate of gilts+0.5% pa.
- 4.3 The 5% margin in the target funding level is to cover the removal of some longevity risk and the operating expenses of the Scheme.
- 4.4 The Trustee is also mindful of the following, which align with the achievement of the objective:
- a The acquisition of suitable assets of appropriate liquidity which will generate income and capital growth to meet, together with new contributions from the Employer, the cost of current and future benefits that the Scheme provides.
  - b To limit the risk of the assets failing to meet the liabilities over the long term, in particular in relation to the SFR, or other statutory requirement.
  - c To minimise the long term costs of the Scheme by maximising the return on the assets whilst having regard to the objective shown under b.

## Policy

- 4.5 The Trustee's policy is to seek to achieve the objectives through investing in a diversified portfolio comprising a suitable mixture of return-seeking and liability-matching assets. The Trustee recognises that the returns on return-seeking assets, while expected to be greater over the long term than those on liability-matching assets, are likely to be more volatile. A mixture across asset classes is targeted to provide the level of returns required by the Scheme to meet its liabilities at an acceptable level of risk for the Trustee and ensure the security, quality, liquidity and profitability of the portfolio as a whole. Having taken appropriate advice, the Trustee is of the opinion that the asset allocation detailed in Section 5 is appropriate in the current circumstances, but will be reviewed at least once every three years or following any major change in investment policy.

## Rates of Return

- 4.6 In setting the Scheme's asset allocation policy, the Trustee has regard to the historical rates of return earned on the various classes of assets available for investment. The Trustee also takes into account the investment consultant's assumptions for the future expected risk and return from different asset classes. The assumptions used for the most recent investment strategy review, as at 31 December 2017, are set out below:

	10-year median real return (%)	1-year volatility (%)
UK equities	1.9	17.6
Global ex UK equities	3.2	19.0
Global ex UK equities (hedged)	2.4	17.2
Corporate bonds	-0.2	7.1
Index-linked gilts	-1.6	8.5
Secure income assets	1.3	6.6

Note: The above assumptions are based on the Willis Towers Watson investment model using the "Lower for Longer" set of assumptions (vs CPI) as at 31 December 2017.

## Financially material considerations

- 4.7 The Trustee takes account of all financially material risks and opportunities when making investment decisions, in consultation with its advisors.
- 4.8 The Trustee believes that environmental, social and corporate governance (ESG) factors, including climate change, may have a material impact on investment risk and return outcomes, and that good stewardship can create and preserve value for companies and markets as a whole.
- 4.9 It is the Trustee's expectation that investment managers will take into account financially material considerations, including ESG factors, in managing the Scheme's assets. This includes consideration of all financially material factors, and other relevant matters including capital structure of investee companies, actual and potential conflicts, other stakeholders and ESG-related issues where relevant.
- 4.10 The Trustee will consider ESG factors as part of the selection of any new investment managers. The relative importance of these factors compared to other factors will depend on the asset class being considered.
- 4.11 The Trustee's policy is that day to day decisions relating to the investment of the Scheme's assets and responsibility for exercising ownership rights (including voting rights) attaching to investments are, in effect, delegated to its investment managers. The Trustee recognises the UK Stewardship Code as best practice and encourages its investment managers to comply with it or explain why they do not adhere to this policy. Responsibility for engagement in respect of investments held by the Scheme is, in effect, delegated to the investment

managers. The Trustee's expectation is that engagement will take place, either directly or as part of a collective multi-investor initiative as appropriate, with the aim of protecting or enhancing the value of the Scheme's investments.

- 4.12 The Trustee is satisfied that, where appropriate, the investment managers have an explicit strategy elucidating the circumstances in which they will intervene in a company, the approach they will use in doing so and how they will measure the effectiveness of this strategy. The Trustee will monitor how the investment managers fulfil their responsibilities with regards voting and engagement through the regular reporting provided by the managers to its advisers.

### **Non-financial matters**

- 4.13 The Trustee recognises that members and beneficiaries may have views on ethical investment or views on matters such as the social and environmental impact of the Scheme's investments. It is the Trustee's view that financial factors should take precedence in seeking to maximise the security of member benefits. As such, it is the Trustee's policy not to take into account the non-financial factors when taking investment decisions related to the Scheme.

## Section 5: Asset allocation guidelines

### Asset allocation

- 5.1 The Trustee has agreed a strategic asset allocation for the Scheme as set out in the table below:

	<b>Strategic asset allocation (%)</b>	<b>Ranges (%)</b>
<b>Return-seeking assets</b>	<b>43.0</b>	<b>38.0 – 48.0</b>
LGIM <sup>1</sup> Diversified Fund	33.0	28.0 – 38.0
TWIM <sup>2</sup> Secure Income Fund	10.0	7.0 – 13.0
<b>Matching assets</b>	<b>57.0</b>	<b>52.0 – 62.0</b>
LGIM LDI mandate	57.0	52.0 – 62.0

1. Legal and General Investment Management  
2. Towers Watson Investment Management

- 5.2 The actual asset allocation would normally be expected to lie within the ranges set out above. Should it move outside of these ranges, the Trustee will consider what action is necessary to rebalance the portfolio.
- 5.3 The Trustee has agreed to a hedging policy which targets hedging 90% of the Scheme's interest rate and inflation exposure as a % of total Scheme assets.
- 5.4 Secure Income assets are classified in the above asset allocation table as return seeking assets but do also have some hedging properties through the inflation linkage of the long term inflation linked cashflows provided by the assets. These exposures were taken into account in determining the proportion of interest rate and inflation exposure of the matching assets in the LDI mandate.
- 5.5 The Trustee has agreed to the use of certain leveraged funds within the LDI mandate managed by LGIM. Leverage is used on a controlled basis for risk management purposes. Some short-term borrowing for settlement is also allowed, but is strictly limited and for the purpose of trade settlement only (this is standard practice in investment management).

### Diversification and risk concentration

- 5.6 The Scheme's return-seeking assets are invested in a well-diversified manner, as set out in section 7. This, together with the strategic asset allocation, is designed to ensure that the Scheme's investments are adequately diversified by asset class avoiding excess reliance on any particular asset, issuer or group of undertakings and so as to avoid accumulations of risk in the portfolio as a whole. These investments consist predominantly of investments admitted

to trading on regulated markets. Since the Scheme is invested in pooled funds, the Trustee cannot influence directly the concentration of investments at a stock selection level. However, the managers' internal guidelines are designed to achieve a suitable level of diversification.

## **Suitability**

- 5.7 The Trustee has taken advice from the Scheme Actuary and the investment consultant to ensure that the asset allocation specified is suitable for the Scheme given its liability profile.

## **Liquidity**

- 5.8 The Trustee, together with the Scheme's administrators, will ensure that it holds sufficient cash to meet the likely benefit outflows from time to time. The Trustee's policy is that there should be sufficient investments in liquid or readily realisable assets to meet cashflow requirements in the majority of foreseeable circumstances so that realisation of assets will not disrupt the Scheme's overall investment policy. The Trustee's policy is that funds will be disinvested with the aim of rebalancing the portfolio towards the strategic asset allocation set out in 5.1 above.

## **Use of derivatives**

- 5.9 The Scheme does not utilise derivatives directly, although some of the pooled funds in which the Scheme is invested may use derivatives to control risk (for example in managing interest rate and inflation risk and overseas currency exposures) or for efficient portfolio management.

## Section 6: Statutory Funding Requirement

- 6.1 The Pensions Act 2004 sets out the requirements for the Statutory Funding Requirement (SFR).
- 6.2 The Pensions Act requires that pension schemes achieve a funding level of at least 100% under these calculations and sets out the requirements for dealing with shortfalls. The Trustee will consult the Scheme Actuary and reach agreement with the Principal Employer when deciding upon the appropriate response to any shortfall.
- 6.3 The Trustee considers that the investment policy described in this statement is consistent with complying with its obligations under the SFR and with the current financial position of the Scheme. In addition, the Trustee will review this investment policy in the light of actuarial valuations and certificates and schedules of contributions produced in order to comply with the SFR.

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## Section 7: Investment manager arrangements

- 7.1 The Scheme uses different managers and mandates to implement its investment policies. The Trustee ensures that, in aggregate, its portfolio is consistent with the policies set out in this Statement, in particular those required under regulation 2(3)(b) of the Occupational Pension Schemes (Investment) Regulations (2005). The Trustee will also ensure that the investment objectives and guidelines of any particular pooled vehicle are consistent with its policies, where relevant to the mandate in question.
- 7.2 The Trustee is currently using passive management for the majority of the Scheme's assets, although active management is used for elements of the portfolio, either to improve expected returns or to capture diversifying sources of return. This balance was agreed following consideration of the relative levels of risk involved, set against the efficiency, liquidity and level of transaction costs likely to prevail within each market, allowing for investment manager fees.
- 7.3 The Trustee appoints its investment managers with an expectation of a long-term partnership, which encourages active ownership of the Scheme's assets. When assessing a manager's performance, the focus is on longer-term outcomes, and the Trustee would not expect to terminate a manager's appointment based purely on short term performance. However, a manager's appointment could be terminated within a shorter timeframe due to other factors such as a significant change in business structure or the investment team.
- 7.4 For most of the Scheme's investments, the Trustee expects the investment managers to invest with a medium to long time horizon, and to use their engagement activity to drive improved performance over these periods.

### Manager Structure

- 7.5 The Scheme's return seeking assets are invested with two investment managers as follows:
- 33.0% of the Scheme's assets are invested in the LGIM Diversified Fund – this fund provides a diversified exposure to a range of return-seeking assets including equities, corporate debt, property and infrastructure.
  - 10.0% of the Scheme's assets are invested in the TWIM Secure Income Fund – this fund provides exposure to real assets (primarily property and infrastructure assets) which provide long term secure cashflows, typically with some degree of inflation linkage.
- 7.6 The Scheme's matching assets (57.0% of Scheme assets) are invested in an LDI portfolio managed by LGIM. This portfolio is invested in a range of funds which provide exposure to changes in interest rate and inflation expectations. The degree of inflation exposure and the

shape of the cashflows provided by this portfolio are designed to be similar to those of the liabilities.

- 7.7 The percentage allocations stated above represent target allocations. Actual allocations will vary over time.

## Performance objectives

- 7.8 The performance objectives of the various pooled funds in which the Scheme's assets are invested are set out below:

Fund	Objective
LGIM Diversified Fund	To deliver a longer term return consistent with the return on developed market equities, with around two thirds of the volatility of equities
TWIM Secure Income Fund	To provide long term cash flows which aim to deliver a return of inflation-linked gilts plus 3% p.a. over rolling 5-year periods and a regular income distribution of 5%.
LGIM LDI mandate	To reduce the impact of changes in interest rates and inflation on the Scheme's financial position.

- 7.9 Whilst the Trustee is not involved in the investment managers' day to day method of operation and therefore cannot directly influence the attainment of the performance objectives, it will assess how the funds perform relative to their objectives on an annual basis (or more frequently if deemed appropriate).

## Manager monitoring

- 7.10 The appointment of the investment managers will be reviewed by the Trustee from time to time, based on the results of monitoring of performance and investment process, the Trustee's confidence that the managers can continue to fulfil their mandates in the future and of the manager's compliance with the requirement in the Pensions Act concerning diversification and suitability, where relevant.
- 7.11 To maintain alignment with the Scheme's policies, the managers have been provided with a copy of this Statement on an annual basis and are required to confirm that the management of the assets is consistent with those policies relevant to the mandate in question.
- 7.12 It is expected that a review meeting will be held with each manager around once each year.
- 7.13 Should the Trustee's monitoring process reveal that a manager's portfolio is not aligned with the Trustee's policies, the Trustee will engage with the manager further to encourage alignment. This monitoring process includes specific consideration of the sustainable investment/ESG characteristics of the portfolio and managers' engagement activities. If,

following engagement, it is the view of the Trustee that the degree of alignment remains unsatisfactory, the manager will be terminated and replaced.

### **Investment Manager Fees**

- 7.14 The investment managers are paid ad valorem fees based on the market value of the assets under management, for a given scope of services which includes consideration of long-term factors and engagement. Fees were taken into consideration when reviewing and appointing the managers.
- 7.15 The Trustee, with the help of the investment consultant, reviews the costs incurred in managing the Scheme's assets regularly, which includes the costs associated with portfolio turnover. In assessing the appropriateness of the portfolio turnover costs at an individual manager level, the Trustee will have regard to the actual portfolio turnover and how this compares with the expected turnover range for that mandate.

## Section 8: Risk Management

- 8.1 The Trustee recognises a number of risks involved in the investment of the assets of the Scheme and will continue to monitor these risks, making investment adjustments as appropriate.
- 8.2 The key risks and the approach used to manage these risks is set out below.

<b>Risk</b>	<b>What is the risk and how is it measured?</b>	<b>How is the risk managed?</b>
Total investment risk	The risk that the Scheme's assets underperform the liabilities causing a deficit to emerge/increase. The risk can be measured using metrics such as Value at Risk (VaR) and Tracking Error (TE) of asset versus liabilities.	By assessing this risk using Asset Liability Modelling at least every 3 years, and ensuring the level of risk is consistent with the Trustee's and Sponsor's risk tolerance.  By understanding the investment risks to which the assets are exposed, mitigating risks which are expected to be poorly rewarded through hedging and holding a diversified exposure to those risks which are expected to be well rewarded.
Sponsor risk	The risk that the sponsor is unable or unwilling to fulfil its responsibilities to the Scheme in making good any current or future funding shortfall, at times where there are insufficient assets to fully secure the Scheme's liabilities.  The risk is measured by the level of ability and willingness of the sponsor to support the continuation of the Scheme and to make good any current or future funding shortfall.	By regularly monitoring the sponsor covenant and setting a Journey Plan targeting a level of funding at which sponsor risk is materially reduced.
Interest rate and inflation risk	The risk that changes in interest rates or inflation expectations causes an increase in the deficit due to the assets and liabilities having different exposures to these variables.  The risk is measured by quantifying the expected change in deficit when interest rates and inflation change.	By quantifying the exposure to these variables within the liabilities, agreeing how much of this exposure should be hedged and by structuring a portfolio of assets to provide this hedge.
Longevity risk	The risk that members live longer than expected causing an increase in the Scheme's liabilities.  The risk is measured by quantifying the expected change in deficit when assumptions for future mortality change.	By allowing for changes in future mortality within the actuarial valuation basis.  The risk may also be mitigated using insurance products or longevity

		hedging instruments if deemed appropriate.
Currency risk	<p>The risk that changes in the exchange rate between Sterling and a foreign currency will negatively impact the value of the Scheme's assets.</p> <p>The risk is measured by the level of overseas investment and the translation effect of currencies leading to the risk of an adverse influence on investment values.</p>	Responsibility for managing this risk is delegated to the investment managers that have discretion to invest in assets denominated in non-Sterling currencies.
Manager risk	<p>The risk that poor performance from a manager, relative to a market index or other benchmark, results in a negative impact on the Scheme.</p> <p>The risk is measured by the expected deviation of the prospective return, as set out in the managers' objectives, relative to the investment policy.</p>	By employing passive investment for the majority of the Scheme's assets and by monitoring the actual deviation of returns relative to the objective and factors supporting the managers' investment processes.
Liquidity risk	The risk that the Scheme is unable to meet shorter term cashflows as a result of being unable to redeem assets within a suitable timeframe.	<p>By the Scheme's administrators assessing the level of cash needed to meet benefit payments.</p> <p>By holding a proportion of the Scheme's assets in liquidity funds, and using income released from the Scheme's assets where appropriate.</p>
Inappropriate investments	The risk that the Scheme invests in an asset which is unsuitable for its circumstances from a legal or investment perspective.	By ensuring that all Scheme investments are considered satisfactory in the context of Section 36 of the Pensions Act and that appropriate legal advice is received before an investment is made.

- 8.3 These measures do not render the investment policy free of risk. Rather, the measures endeavour to balance the need for risk control and the need for assets which are likely to achieve the required performance target.
- 8.4 The Trustee continues to monitor these risks.
- 8.5 The Trustee also recognises that conflicts of interest can arise wherever agents (such as advisers, investment managers and the Trustee itself) are acting on behalf of the ultimate beneficiaries. The Trustee seeks to identify where conflicts or potential conflicts exist, put in place processes for managing these conflicts, and ensure they are taken into account when making investment decisions.

# Appendix A: Current advisers

<b>Scheme Actuary</b>	Alison Blay
<b>Investment consultant</b>	Willis Towers Watson
<b>Investment managers:</b>	Legal & General Investment Management Towers Watson Investment Management
<b>Administrator:</b>	Barnett Waddingham LLP
<b>Solicitors:</b>	Sacker & Partners LLP
<b>Scheme auditors:</b>	Moore Kingston Smith LLP

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