

Statement of Investment Principles – January 2017

1 Introduction

1.1 Purpose of Statement

This statement (the “Statement”) sets out the principles governing decisions about the investment of the assets of the Parliamentary Contributory Pension Fund (“the Fund”) and is made by the Trustees (the “Trustees”) of the Fund. As required by the Rules which govern the Fund, the Statement complies with the provisions of Section 35 of the Pensions Act 1995 (as amended) and is subject to review at least every three years and immediately on any significant change in investment policy. In preparing the Statement, the Trustees consulted with IPSA and the MCS.

1.2 Advice

In preparing the Statement, the Trustees obtained and considered written advice from Hymans Robertson LLP, the Investment Adviser appointed by the Trustees. The Investment Adviser provides both strategic and other investment advice as agreed with the Trustees from time to time.

1.3 Investment Powers

The investment powers of the Trustees are set out in Schedule 6 to the Constitutional Reform and Governance (CRaG) Act 2010. This Statement is consistent with those powers. Neither the Statement nor the CRaG Act restrict the Trustees’ investment powers by requiring the consent of IPSA or the MCS or any other party.

1.4 Myners Principles

The Trustees are aware of the Myners Principles in relation to the governance of pension schemes. In conjunction with the Fund’s officers and Investment Adviser, they aim to adhere to the guidance within the Principles with regard to the Fund’s investments.

2 Choosing Investments

2.1 Process for Choosing Investments

The Trustees have delegated day to day investment decisions to a number of investment managers who are authorised under the Financial Services and Markets Act 2000 to undertake investment business.

2.2 Investment Objectives

To guide them in their strategic management of the assets and to control the various risks to which the Fund is exposed, the Trustees have considered their objectives and have adopted the following:

- To invest predominantly in long term growth assets reflecting the investment time horizon of the Fund.
- To achieve a rate of return over the long term that is at least equivalent to the discount rate assumptions used when calculating the long term cost of the benefits. The most recent actuarial valuation (2014) used a discount rate of 3.5% p.a. above changes in the Consumer Prices Index (CPI), and the 2013 review carried out by IPSA used a discount rate of 3% p.a. above changes in the CPI.”
- To have due regard to the risk of incurring large and sustained deficits in the future with resulting increases in contribution levels and reducing these risks where possible.

- To ensure that there are always sufficient assets of the Fund available and of sufficient liquidity to meet benefit payments as they fall due.
- To manage the investments as efficiently as possible. It is anticipated that investment management costs (excluding performance related fees) should not exceed 0.4% of the Fund's assets.
- To achieve and maintain a funding level of 100%.

2.3 Investment Policy

The Trustees have translated their objectives into a suitable strategic asset allocation benchmark for the Fund. The strategic benchmark has been translated into benchmarks for the individual managers which are consistent with the Fund's overall strategy. The Fund benchmark is consistent with the Trustees' views on the appropriate balance between seeking an enhanced long-term return on investments and accepting greater short-term volatility and risk.

The investment strategy takes due account of the maturity profile of the Fund (in terms of the relative proportions of liabilities in respect of pensioners and non-pensioners), together with the level of disclosed surplus or deficit (relative to the funding bases used). It is intended that investment strategy will be reviewed at least every three years following actuarial valuations of the Fund, and more frequently if required. In reviewing strategy, the Trustees will seek written advice as required.

The current strategic benchmark for the Fund is shown below.

Asset Class	Total Fund Benchmark %	Target Lower Range %	Target Upper Range %
Total Equities	66.0	62.0	70.0
UK Equities	19.8	17.3	22.3
Overseas Equities	46.2	43.2	49.2
Total Bonds	24.0	20.0	28.0
UK Property	10.0	-	-
Total	100.0		

The Trustees' general policy is to invest surplus cash (or raise cash, where necessary) from managers in such a way that the actual asset allocation remains within the target ranges in the table above. It may also be appropriate on occasion to arrange transfer of assets between managers where deviations from the target have become extreme. The target ranges above are designed to act as a guide in this process and not be an automatic trigger for such transfers.

Based on historical experience, the Trustees expect the long term return on the majority of investments held by the Fund to exceed both price inflation and general salary growth.

3 Management of Fund Assets

3.1 Kinds of Investments

The Trustees may invest in quoted and unquoted securities of UK and overseas markets including equities and fixed interest & index linked bonds, cash and property directly and / or through pooled funds. The Trustees may also make use of derivatives and contracts for difference for the purpose of efficient portfolio management. The Trustees consider all of these classes of investment to be suitable in the circumstances of the Fund.

Assets are managed on both active and passive (index tracking) bases. The manager of an active fund seeks to exceed the performance of the stated benchmark or target of the fund. The manager of a passive fund seeks to match, rather than exceed, the performance of a benchmark index by investing in stocks in such a way as to replicate, as closely as possible, the composition of the benchmark index.

3.2 Balance between different types of investment

The Managers will hold a mix of investments which reflects their views relative to their respective benchmarks. Within each major market, each Manager will maintain a diversified portfolio of stocks through direct investment or pooled vehicles. The Trustees are satisfied that the portfolio of investments is adequately diversified in terms of asset class, geographic spread and manager selection.

3.3 Monitoring the Investment Managers

The performance of the investment managers and the combined assets for the Fund is measured by the Fund's custodian. The Investment Advisor and Fund officers, on behalf of the Trustees, meet the investment managers at least annually and, if circumstances require, more frequently review the managers' mandates together with the reasons for, and background behind, their investment performance. The Investment Advisor produces quarterly reports for the Trustees which provide an update on business and people developments at the various managers.

4 Investment Restrictions

The Managers have discretion over the investment of the Fund's assets, subject to the restrictions set out in each Investment Management Agreement. The Trustees are satisfied that the spread of assets by type and the Managers' policies on investing in individual securities provides adequate diversification of investments.

Within categories of investment permitted by the Trustees, the Managers can purchase any new investments, as long as they do not breach the provisions of the fund manager agreements.

5 Investment beliefs

This section sets out the investment beliefs of the Fund. This seeks to set out the Fund's key investment beliefs and demonstrate how these principles are reflected in the Fund's investment strategy. It is the intention that these beliefs will create a framework for the Trustees' investment decisions, underpinning discussions and assisting decisions regarding the structure of the Fund, strategic asset allocation and the selection of investment managers.

Belief: Clear and well defined objectives are essential to achieve future success

The Trustees are aware that there is a need to generate a sufficient level of return from the Fund's assets, while at the same time having a clear understanding of the potential risks and ensuring there is sufficient liquidity available to pay members' benefits as they fall due.

Belief: Strategic asset allocation is a key determinant of risk and return, and thus is typically more important than manager or stock selection

The Trustees understand that having the appropriate strategy in place is a key driver of the Fund's future success. As a result, priority is given to more strategic investment matters.

Belief: Long term investing provides opportunities for enhancing returns

The Trustees believe that investors with long term time horizons are typically less constrained by liquidity requirements and able to better withstand periods of price volatility. As a long term investor, the Fund may choose to gain additional compensation by investing in assets that are illiquid or may be subject to higher levels of volatility (a premium return is required for any such investments).

Belief: The strength of employer covenant allows the Fund to take a long term view of investment strategy

The Trustees believe that the strength of employer covenant (the UK Government) means that the Fund can take advantage of the benefits associated with a long term investment horizon, as set out above.

Belief: Equities are expected to generate superior long term returns

The Trustees believe that, over the longer term, equities are expected to outperform other liquid assets, in particular government bonds. The Trustees are therefore comfortable that the Fund maintains a significant target allocation to equities.

Belief: Alternative asset class investments provide diversification

The Trustees believe that diversification across asset classes can help reduce the volatility of the Fund's overall asset value and improve its risk-return characteristics. The Trustees believe that investing across a range of asset classes (including (but not restricted to) equities, government bonds, corporate bonds and property) will provide the Fund with diversification benefits.

Belief: Fees and costs matter

The Trustees recognise that fees and costs reduce the Fund's investment returns. The Trustees consider the fees and costs of its investment arrangements to ensure the Fund is getting value for money and to minimise, as far as possible, any cost leakages from its investment process. The Trustees have undertaken industry benchmarking of the Fund's investment management fees and the Fund's overall costs and will continue to review this on a regular basis.

Belief: Passive management has a role to play in the Fund's structure

The Trustees recognise that passive management allows the Fund to access certain asset classes (e.g. equities and bonds) on a low cost basis and have, over time, increased the proportion of assets managed on a passive index-tracking basis within the Fund.

Belief: Active management can add value but is not guaranteed

The Trustees recognise that certain asset classes can only be accessed via active management. The Trustees also recognise that active managers may be able to generate higher returns for the Fund (net of fees), or similar returns but at lower volatility, than equivalent passive exposure. By carefully selecting and monitoring active managers, the Trustees seek to minimise the additional risk from active management, and continue to monitor active managers to ensure their mandates remain appropriate for the Fund.

Belief: Environmental, social and corporate governance ('ESG') issues can have a material impact on the long term performance of its investments

The Trustees recognise that ESG issues can impact the Fund's returns, and the Trustees aim to be aware of, and monitor, financially material ESG-related risks and issues including climate change through the Fund's investment managers. Further detail on the Fund's approach to ESG issues is provided in the Fund's separate statement on responsible investment.

6 Responsible Investment

The Trustees consider the Fund's approach to responsible investment in two key areas:

- **Sustainable investment / ESG factors** – considering the financial impact of environmental, social and governance (ESG) factors on its investments.
- **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.

The following principles set out the Fund's approach:

- The Trustees recognise that their duty is to act in the best financial interests of the Fund's beneficiaries.
- The Trustees believe that environmental, social and corporate governance ("ESG") issues can have a material impact on the long term performance of its investments.
- The Trustees encourage engagement by its investment managers with investee companies on ESG issues to positively influence company behaviour and enhance shareholder value.
- The Fund's investment managers are expected to take account of ESG-related risks and issues as part of their investment analysis and decision-making process. Further, the Fund's investment managers are expected to incorporate reporting on ESG-related issues into their regular reporting. This includes information on voting and engagement, in addition to details on how they are assessing and managing ESG-related risks in relation to their respective mandates.
- The Trustees aim to be aware of, and monitor, financially material ESG-related risks and issues through its investment managers, by reviewing each individual manager's activities in relation to ESG issues on an ongoing basis through regular reporting (as noted above). The Trustees take responsible investment factors into account when monitoring and selecting investment managers.
- The Fund and all of its investment managers are signatories to the FRC's UK Stewardship Code. The Trustees monitor the investment managers' compliance with the UK Stewardship Code and their track record of engaging with companies on issues such as climate change risk, fossil fuels and broader ESG issues on an ongoing basis.
- All of the Fund's investment managers are signatories to the UN Principles of Responsible Investment ("UNPRI"). The Trustees monitor the investment managers' compliance with the UNPRI.
- The Fund encourages its investment managers to publish a Stewardship Disclosure Framework, which provides a common reporting template for assessing manager approaches to stewardship and engagement. Explanation is sought from those managers who have not published a response.

- Where the assets are invested on an index-tracking basis (which requires close replication of the appropriate index), it is understood by the Trustees that these factors will not be given priority by the manager when selecting investments for purchase, retention or sale.

7 Exercising voting rights

The Trustees believe that failing to exercise voting or other rights attached to shares could be contrary to the interest of the beneficiaries of the fund. They have therefore instructed the investment managers to take this into account in exercising such rights on their behalf. The Trustees have instructed the managers to provide them with a statement on their corporate governance and voting policy.

The Trustees have a commitment to monitoring the adherence of their fund managers to the policies contained in this statement and they have instructed their fund managers to provide annual reports outlining the impact of these policies.

8 Realisation of Investments

The majority of the Fund's investments may be realised quickly if required. However, the Fund's investments in pooled property funds (which represent approximately 10% of total assets) may take some time to realise quickly in certain market conditions.

9 Diversification and Risk Control

The following measures have been implemented to reduce the risks associated with making investments. These are subject to review by the Trustees from time to time.

9.1 Number of Managers

The Fund assets are divided between several Managers to reduce the risks of underperformance from any one. The Fund also has approximately 42% of the assets managed on a passive (index-tracking) basis.

9.2 Risk versus the Liabilities

The majority of the Fund's liabilities are linked to inflation and nominal salary growth. The policy is therefore to invest the majority of the assets in investments that are expected to exceed price inflation and general salary growth over the long term. The Trustees monitor the returns relative to the liabilities through regular funding updates.

9.3 Range of Assets

The Trustees have set a scheme specific benchmark. This contains a wide range of assets suitable for a pension scheme. The Trustees review the distribution of assets quarterly.

9.4 Manager Restrictions

The Trustees' agreement with each Manager contains a series of restrictions on the way the portfolio is managed. Agreements may be amended from time to time. Each Manager is obliged to comply with the restrictions set out in the agreement. The purpose of the restrictions is to limit the risks arising from a single Manager and from the Managers in aggregate.

9.5 Manager Controls

Powers of investment delegated to the Managers must be exercised with a view to giving effect to the principles contained in this Statement so far as is reasonably practicable within the provisions of the Investment Management Agreement. The Managers will also ensure that suitable internal operating procedures are in place to control individuals making investments for the Fund.

9.6 Trustee Controls

The Trustees are responsible for ensuring that appropriate systems of control are in place to safeguard the Fund's assets and to prevent and detect fraud and other irregularities. Suitable systems have been set in place in consultation with the Managers, the Fund's custodian (Northern Trust) and the External Auditor (The Comptroller and Auditor General).

9.7 Custody

Northern Trust act as custodian for the Fund's assets. Northern Trust are responsible for the safekeeping of the Fund's segregated investments and will also provide accounting services for all of the Fund's investments.

For those investments in pooled funds, custody arrangements are the responsibility of the relevant Manager.

9.8 Currency risk

The Fund invests in a range of overseas markets which provides a diversified approach to currency markets; the Trustees also assess the Scheme's currency risk during their risk analysis.

10 Additional Voluntary Contributions (AVCs)

The Trustees give members an opportunity to make Additional Voluntary Contributions to the Fund.

The Trustees periodically review the performance of the AVC investment vehicles and any material comments arising from this review are provided to the members contributing to the Fund.

The Trustees acknowledge the Pension Regulator's Code of Practice 13, "Governance and administration of occupational defined contribution trust based pension schemes" that was published in November 2013. They will assess the Fund's AVCs relative to the quality features associated with this Code.

11 Compliance with and Review of this Statement

11.1 Frequency of Review

The Trustees will review the investment strategy with advice from the Investment Adviser at least every three years in conjunction with the Actuarial Valuation or more frequently as required (and immediately on any significant change in investment policy).

11.2 Review of investment managers

The Trustees will consider whether or not each investment manager:

- has the appropriate knowledge and experience for their mandate,
- is carrying out its work competently,

- has had regard to the need for diversification of investments, and
- has had regard to the suitability of each investment and each category of investment.

This will be assessed informally as part of the quarterly update on investment performance and business development at each of the managers and also as part of the annual meetings with the managers. If a Manager is not able to satisfy the Trustees about issues that arise, the Trustees will consider replacing the Manager.

11.3 Information

Where required to do so under the relevant investment management agreement, the Managers will inform the Trustees as soon as practicable of:

- any breach of the Investment Management Agreement which has come to their attention,
- any serious breach of internal operating procedures, which may affect the Fund, or
- any material change of the personnel managing the Fund's investments.

The Managers will supply the Trustees with sufficient information each quarter to facilitate the review of their activity, including:

- a report of the strategy followed during the quarter,
- the rationale behind past and future strategy,
- a full valuation of assets,
- a transaction report, and
- a cash reconciliation.

In order to allow the Trustees to carry out their annual review of the Managers, each will supply to the Trustees the following, in an agreed format:

- evidence of their knowledge and experience for managing the investments of the Fund,
- a description of their approach to making decisions about the suitability and diversification of the investments delegated to them, and
- an overview of operating procedures used by the fund manager and controls over the individuals making investments for the Fund.

Version	Effective Date
1.1	10 December 1999
1.2	22 February 2000
1.3	22 March 2000
1.4	3 April 2000
1.5	3 July 2000
1.6	12 July 2000

1.7	25 March 2004
1.8	30 July 2004
1.9	7 December 2004
1.10	17 March 2006
1.11	26 September 2006
1.12	6 June 2007
1.13	12 March 2009
1.14	13 January 2011
1.15	13 June 2013
1.16	January 2014 (DRAFT)
1.17	October 2014 (DRAFT)
1.18	TBC

Signed

Date

Name