LEICESTERSHIRE COUNTY COUNCIL PENSION FUND

STATEMENT OF INVESTMENT PRINCIPLES

1.0 INTRODUCTION

1.1 This is the Statement of Investment Principles (the 'Statement') required by the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009 (the '2009 Regulations').

1.2 The Statement has been adopted by the Pension Fund Management Board (the 'Board') which acts on the delegated authority of Leicestershire County Council, the administering authority for the Leicestershire Pension Fund ('the Fund'). The Statement is subject to review from time to time and certainly within six months of any material change in investment policy or other matters as required by law. In preparing this Statement the Board has consulted with the administering authority and other major employers within the Fund and has taken advice from the Investment Practice of Hymans Robertson LLP.

1.3 In Appendix 1, the Board has set out details of the extent to which the Fund complies with the six principles set out in the Chartered Institute of Public Finance and Accountancy's publication 'Investment Decision Making and disclosure in the Local Government Pension Scheme 2009 – a guide to the application of the 2008 Myners Principles to the management of LGPS funds'.

2.0 FUND OBJECTIVE

2.1 The primary objective of the Fund is to provide pension and lump sum benefits for members on their retirement and/or benefits on death, before or after retirement, for their dependents, on a defined benefits basis.

2.2 The Board aim to fund the Fund in such a manner that, in normal market conditions, all accrued benefits are fully covered by the value of the Fund's assets and that an appropriate level of contributions is agreed by the employer to meet the cost of future benefits accruing. For employee members, benefits will be based on service completed but will take account of estimated future salary increases.

2.3 This funding position will be reviewed at each triennial actuarial valuation, or more frequently as required.

3.0 INVESTMENT STRATEGY

3.1 The Board has translated its objectives into a suitable strategic asset allocation benchmark for the Fund (Appendix 2). The strategic benchmark is reflected in the investment structure adopted by the Board; this comprises a mix of segregated and pooled, active and passive manager mandates. The Fund benchmark is consistent with the Board's views on the appropriate balance between generating a satisfactory long-term return on investments whilst taking into account market volatility and risk and the nature of the Fund's liabilities.

3.2 The Board monitors its investment strategy relative to the agreed asset allocation benchmark. It is intended that investment strategy will be reviewed at least on an annual basis.

3.3 **Limits on investments**

The Regulations set upper limits on certain types of investment. At their meeting on 15 February 2008 the Board agreed to an increase in the normal limits in respect of:

(i) All contributions to partnerships – maximum of 15% of Fund assets
(ii) All contributions to a single partnership – maximum of 5% of Fund assets
(iii) Any single insurance contract – maximum of 35% of Fund assets

Before taking this decision the Board took proper advice from its investment adviser, Hymans Robertson LLP, in relation to the impact of the increase on overall risk within the Fund and how the Board monitors that risk. The decision was taken as the additional risk involved is not significant, but the increased limits allow the Fund greater flexibility when making investment decisions. The decision does not have a time limit and, as such, is open-ended. The decision complies with the Regulations.

3.4 **Types of investment to be held**

3.4.1 The Fund may invest in quoted and unquoted securities of UK and overseas markets, including equities, fixed interest and index linked bonds, cash, currency, property and commodities, either directly or through pooled funds. This list is not intended to be exhaustive and other types of investment may be held if the Board feels that they are appropriate to the overall objective of the Fund.

3.4.2 The Fund may also use contracts for differences and other derivatives either directly or in pooled funds, for the purpose of efficient portfolio management or to hedge specific risks. The Board considers all these assets classes of investment to be suitable in the circumstances of the Fund.

3.4.3 The strategic asset allocation of the Fund includes a mix of asset types across a range of geographies in order to provide diversification of returns.

3.5 **Balance between different kinds of Investments**

3.5.1 The Board has appointed a number of investment managers all of whom are authorised under the Financial Services and Markets Act 2000 to undertake investment business.

3.5.2 The Board, having sought appropriate investment advice, has agreed specific benchmarks with each manager so that, in aggregate, they are consistent with the overall asset allocation of the Fund. The Fund’s investment managers will hold a mix of investments which reflect their views relative to their respective benchmarks. Within each major market and asset class, the managers will maintain diversified portfolios through direct investment or within pooled vehicles.

4.0 RISK

4.1 The Fund is exposed to a number of risks which pose a threat to the Fund meeting its objectives. The principal risks affecting the Fund are:

4.2 Funding Risks

4.2.1 - Financial mismatch
1. The risk that Fund assets fail to grow in line with the developing costs of meeting Fund liabilities.
2. The risk that unexpected inflation increases the pension and benefit payments and the Fund assets do not grow fast enough to meet the increased cost.

- Changing demographics
The risk that longevity improves and other demographic factors change increasing the cost of Fund benefits.

- Systemic risk
The possibility of an interlinked and simultaneous failure of several asset classes and/or investment managers, possibly compounded by financial 'contagion', resulting in an increase in the cost of meeting Fund liabilities.

4.2.2 Having set a strategic asset allocation the Board monitors the Fund's asset allocation and investment returns relative to the benchmark. Risk is also addressed by monitoring the way in which the Fund's assets move relative to its liabilities.

4.2.3 Mortality and demographic assumptions are kept under review and these assumptions are considered formally as part of the actuarial valuation.

4.2.4 The Board seeks to mitigate systemic risk through maintaining a portfolio which is diversified by asset class and geography. It is, however, not possible to make specific provision for all possible eventualities that may arise under this heading.

4.3 Asset Risks

4.3.1 - Concentration
The risk that significant allocation to any single asset class category and its underperformance relative to expectation would result in difficulties in achieving funding objectives.

- Illiquidity
The risk that the Fund cannot meet its immediate liabilities due to the fact that it has insufficient liquid assets.

- Manager underperformance
The failure by the investment managers to achieve the rate of investment return assumed in setting their mandates.

4.3.2 The Board ensures that the Fund’s assets are diversified between different asset classes, different geographic regions and different investment managers. Investment management agreements all include specific objectives and individual benchmarks, and account is taken of manager process in order to constrain risk within the Board’s expected parameters. The Board recognises the need to have access, on occasions, to short-term liquidity and the strategic asset allocation reflects this.

4.4 Other provider risk

4.4.1 - Transition risk
The risk of incurring unexpected costs in relation to the transition of assets between different investment managers. When carrying out significant transitions the appointment of specialist transition managers is considered.

- Custody risk
The risk of losing economic rights to fund assets, when held in custody or when being traded.

- Credit default
The possibility of default of a counterparty in meeting its obligations.

4.4.2 It is expected that the Director of Corporate Resources and his staff will take account of these risks when proposing a particular course of action within these areas.

5.0 EXPECTED RETURN ON INVESTMENTS

5.1 Over the long term, the overall level of investment returns is expected to exceed the rate assumed by the actuary in funding the Fund.

6.0 REALISATION OF INVESTMENTS

6.1 The majority of investments within the Fund may be realised quickly if required.

7.0 SOCIAL, ENVIRONMENTAL AND ETHICAL CONSIDERATIONS

7.1 The Board recognises that social, environmental and ethical considerations are amongst the factors which investment managers need to take into account , where relevant, when selecting investments for purchase, retention or sale. The Board also recognises that governance procedures within companies also need to be taken into account.

7.2 The Board has considered the environmental, social and governance (ESG) policies of its appointed managers and is comfortable that they are an integral part of the decision making processes. As a result the Board has asked the investment managers to act according to their policies, and to take action which they feel safeguards the best long-term economic interests of the Fund.

8.0 EXERCISE OF VOTING RIGHTS

8.1 Voting rights are recognised as an asset of the Fund and the Board has considered the policies of its investment managers in this respect. The exercise of voting rights has been delegated to the investment managers, and it is expected that these rights will be exercised in a manner which seeks to preserve and enhance long term shareholder value. It is expected that managers will vote at all annual and extraordinary general meetings of companies, where it is practical and cost-effective to do so. The Fund has specifically instructed all managers to vote against political donations.

9.0 STOCK LENDING

9.1 The Fund carries out a stock lending programme via its custodian, on which commissions are received. High-quality collateral is held by the custodian to cover approximately 105% of the value of stock out on loan, and this collateral can be used to buy back the Fund’s holdings in the event of a default by the borrower. Furthermore, the Fund has a full indemnity from the custodian against any losses and the risks involved are, therefore, considered to be small and well managed. Stock lending is limited to 25% of the Fund’s assets at any time.

10.0 ADDITIONAL VOLUNTARY CONTRIBUTIONS (AVCs)

10.1 Fund members are able to invest AVC’s via an arrangement with Prudential Assurance.

Signed For and on Behalf of the Pension Fund Management Board of Leicestershire County Council (acting as Administering Authority of the Leicestershire Pension Fund)

Chairman

Vice Chairman

APPENDIX 1

MYNERS PRINCIPLES

1. Effective Decision Making

a All decisions taken by the Pension Fund Management Board or the Investment Subcommittee (ISC) are taken in the context of attempting to achieve an acceptable level of return, within acceptable levels of risk, over the medium and long-term. The achievement of an acceptable level of return will allow employers' contribution rates to remain at manageable and relatively stable levels.

b It is recognised that if effective decisions are to be made by the Pension Fund Management Board/Investment Subcommittee they must, as a group and individually, have sufficient support and training to be able to make decisions with an appropriate level of expertise and to challenge the advice they receive. The Board/ ISC will receive advice from the investment practice of Hymans Robertson, an Independent Investment consultant and from the Director of Corporate Resources and his staff. Trustee training will be offered to the members of the Board on an on-going basis, with the expectation that this will be at least annually.

c No significant decision will be made by the Board unless all eleven voting members have been invited to attend a meeting. For the Investment Subcommittee no significant decision will be taken unless all five voting members have been invited to attend. Decisions will be on a majority of attendees basis. Administrative matters to do with the Fund (e.g. appointment of a Custodian of the Fund's assets) will be dealt with by the Director of Corporate Resources and reported to the Board, if necessary, at one of the regular meetings.

d The current structure of the Board and the Investment Subcommittee is such that it allows representation to all major employer groups whilst being sufficiently small to remain effective. The structure of the Board and Investment Subcommittee will be kept under review.

e The current structure of the Local Government Pension Scheme means that there are unlikely to be significant conflicts of interest, but members of the Board/ISC must declare them if a conflict exists.

2. Clear Objectives

a The overriding objective of the Board is to put into place a portfolio and asset structure which seeks to achieve a return on Fund Assets which is sufficient, over the long-term, to meet the cost of all benefits due for payment by the Fund.

b As employers' contributions into the Fund are variable and are set every three years as part of the actuarial valuation process, it is important that these contribution rates are not overly volatile. In an attempt to produce an asset mix which is expected to achieve acceptable long term returns, but without significant volatility, the Fund will normally commission an asset/liability study every three years (to coincide with the timing of the actuarial valuation). The asset/liability study assesses the likely future outcome in the event of various economic and financial scenarios, and from these outcomes a strategic asset allocation is proposed.

c It is accepted that the proposed strategic asset allocation derived from an asset/liability study will not be the one which best 'matches' assets to known liabilities (e.g. the best match for pensioner liabilities is UK index-linked gilts). The strategic asset allocation has been agreed by taking into account the opportunities and risks of investing in different asset classes, with the intention of allowing employers' contribution rates to remain relatively low and stable. The Fund's strategic asset allocation takes a pragmatic approach to the mismatch of assets and liabilities.

d The strength of covenant for non-local authority employers is taken into account in the setting of employers' contribution rates, and smoothing/phasing of required contribution rate changes will take account of the covenant strength. It is impractical to take account of each separate employer's attitude to risk when setting investment strategy, but the nature of the different employers who are represented on the Board allows different views to be taken into account. Advisors and investment managers are aware of the attitude to risk, the latter reinforced via the limits and performance objective included within their investment management agreements.

3 Risk and Liabilities

a The strategic asset allocation agreed by the Pension Fund Management Board is by far the most critical aspect of achieving an acceptable level of investment return, within acceptable levels of volatility. The regular commissioning of an asset/liability study to appraise alternative asset allocation strategies assists the Board to make strategic asset allocation decisions.

b Potential implications for local tax payers, strength of employer covenant and risk of default and longevity risk are all taken into account within either the actuarial valuation process (which includes setting appropriate employers' contribution rates) or the investment strategy.

4. Performance Assessment

a The Pension Fund Management Board/ISC receives expert advice at its quarterly meetings from the investment practice of Hymans Robertson. From January 2011 an assessment of the effectiveness of this advice will form part of the Board's annual strategy meeting.

b The effectiveness of the Board itself, and the decisions it takes, will also be assessed at the annual strategy meeting starting in January 2011.

c The performance of the Fund's investment managers is an on-going process, and the Board is assisted in this by Hymans Robertson, the Director of Corporate Resources and his staff.

5. Responsible Ownership

a The Board recognises that, within the overriding requirement to act in the best financial interests of the beneficiaries of the Fund, it also has a responsibility to act as a responsible owner of assets.

b The policies of the Fund’s investment managers in respect of responsible ownership (including Environmental, Socially Responsible and Governance issues) have been considered and the Board is comfortable that these policies are sufficiently robust to ensure that responsible ownership is taken seriously and acted on accordingly. As such, all actions in this area (including casting votes on behalf of the Fund) have been delegated to the investment managers. The managers are expected to report to the Board on any contentious or important issues on a quarterly basis.

6. Transparency and Reporting

a The Board/ISC will take all decisions in as transparent and open a manner as is possible, and relevant stakeholders will be consulted when it is appropriate to do so. There will be certain issues that are commercially or market sensitive and these issues, by their very nature, need to be dealt with in private. All agendas, reports (unless they are not for publication by virtue of paragraphs 3 and 10 of schedule 12(A) of the Local Government Act 1972) and minutes are public documents and will be published on the County Council’s website.

b An Annual Report will be produced and is available to members of the Fund and the general public, and an Annual General Meeting of the Fund will be held. All Fund members are entitled to attend the Annual General Meeting.

c Fund members will be informed of any changes which affect the benefits structure, but it is not cost effective to provide information to them on a regular basis unless it is considered important that they are aware of other changes.

APPENDIX 2

STRATEGIC ASSET ALLOCATION*

Asset class	Strategic allocation %	Benchmark index
UK equities	8.1	FTSE All-Share
Global equities (ex UK)	32.4	FTSE All-World Developed series/IFC Global (for emerging markets)
Global equities (incl UK)	8.0	FTSE World Index
Private equity	4.0	FTSE World Index
TOTAL EQUITIES	**52.5 (1)**	
Global inflation-linked government bonds	7.5	Barclays Global Inflation World 10+ year (£) index (total return)
Global Infrastructure	5.0 (2)	LA 7-day index + 4% p.a.
Global Timberland	2.0	LA 7-day index + 4% p.a.
TOTAL INFLATION-LINKED	**14.5**	
Global Credit	5.0	Merrill Lynch Sterling Broad Market Index
Emerging Market Debt	2.5	Fund specific benchmark
TOTAL BONDS	**7.5**	
PROPERTY	**10.0**	**IPD Monthly/Annual**
TARGETED RETURN	**11.5 (2)**	**LIBOR Sterling 3 month + 4% p.a.**
OTHER OPPORTUNITIES	**4.0 (1)**	**Various**
TOTAL ASSETS	100.0	

***** As agreed at Local Pension Committee Board on 22nd January 2016.

(1) Other opportunities can rise to up to 6% of total assets if sufficient attractive investments are found. Any increase above 4% will be funded by a reduction in the allocation to equities.

(2) Infrastructure weighting agreed to rise to 5% from 3%, funded by a reduction in targeted return. Not expected to happen until mid-2016.