# Confederation of Health Service Employees 1974 Pension & Assurance Scheme

## Statement of Investment Principles – September 2020

### 1. Introduction

The Trustees of the Confederation of Health Service Employees 1974 Pension & Assurance Scheme (the "Scheme") have drawn up this Statement of Investment Principles (the "Statement") to comply with the requirements of the Pensions Act 1995 (the "Act") and subsequent legislation. The Statement is intended to affirm the investment principles that govern decisions about the Scheme's investments. A separate document detailing the specifics of the Scheme's investment arrangements is available upon request.

In preparing this Statement the Trustees have consulted the Sponsoring Employer ("UNISON") to ascertain whether there are any material issues which, in UNISON's view, the Trustees should take into account in agreeing the Scheme's investment arrangements.

### 2. Process for Choosing Investments

The process for choosing investments is as follows:

- identify appropriate investment objectives;
- agree the level of risk and expected return consistent with meeting the objectives set; and
- construct a portfolio of investments that is expected to meet the return objective (net of all costs) given the targeted level of risk.

In considering the appropriate investments for the Scheme, the Trustees have obtained and considered the written advice of their investment consultant, Mercer Limited (the "Investment Consultant"), whom the Trustees believe to be suitably qualified to provide such advice. The advice received and arrangements implemented are, in the Trustees' opinion, consistent with the requirements of Section 36 of the Pensions Act 1995 (as amended).

The Trustees' investment powers are set out in the Scheme's governing documentation and relevant legislation. If necessary, the Trustees will take appropriate legal advice regarding the interpretation of these. The ultimate power and responsibility for deciding investment policy, however, lies with the Trustees.

### 3. Investment Objectives

The Trustees' duty is to invest the Scheme's assets in the best interest of the members and beneficiaries, and in the case of a potential conflict of interest, in the sole interest of the members and beneficiaries. Within this framework the Trustees have agreed a number of objectives to help guide them in their strategic management of Scheme assets and control of the various risks to which the Scheme is exposed. The Trustees' primary objectives are as follows:

- To ensure that there are sufficient assets to cover the benefit promises accrued at any particular point in time (as defined by the Scheme's actuarial assumptions), without placing unnecessary financial burden on UNISON, and without resorting to a high risk profile.

- To pay due regard to UNISON's interests in the size and volatility of contribution payments.

## 4. Risk Management and Measurement

There are various risks to which the Scheme is exposed. In establishing the investment objectives, the Trustees have considered the following risks:

- The risk that there is a mismatch between the Scheme's assets and its liabilities. The Trustees recognise that whilst increasing risk relative to the Scheme's liabilities increases potential returns over a long period, it also increases the risk of a shortfall in returns relative to that required to cover the Scheme's accruing liabilities as well as producing more short-term volatility in the Scheme's funding position. The Trustees have taken advice on the matter and (in light of the objectives noted previously) considered carefully the implications of adopting different levels of risk.

- The risks that may arise from a lack of diversification of investments. Subject to managing the risk from a mismatch of assets and liabilities, the Trustees aim to ensure the asset allocation policy in place results in an adequately diversified portfolio.

- The documents governing the manager appointments include a number of guidelines which, among other things, are designed to ensure that only suitable investments are held by the Scheme. The managers are prevented from investing in asset classes outside of their mandate without the Trustees' prior consent.

- Arrangements are in place to monitor the Scheme's investments to help the Trustees check that nothing has occurred that would bring into question the continuing suitability of the current investments. Further information is set out in Section 10.

- The safe custody of the Scheme's assets is delegated to professional custodians via the use of pooled vehicles.

- Investment managers may not borrow monies without prior consent. Whilst the Trustees recognise that borrowing on a temporary basis is permitted, this option will only be utilised when it is deemed absolutely necessary or where the Trustees have received advice that the Scheme's overall exposure to risk can be reduced through temporary borrowing, e.g. during an asset transfer.

- Environmental, Social and Governance risks (including but not limited to climate change) are recognised and these risks are considered to be financially material. Further information is set out in Section 11.

The risk and other factors set out above are those that the Trustees determine to be financially material over the Scheme's anticipated lifetime.

Should there be a material change in the Scheme's circumstances, the Trustees will review whether and to what extent the investment arrangements should be altered, in particular whether the current risk profile remains appropriate.

## 5. Portfolio Construction

The Trustees have adopted the following control framework in structuring the Scheme's investments subject to the overriding constraint that at the total Scheme level the expected level of risk and return is consistent with the investment objectives detailed in Section 3:

- There is a role for both passive and active management. Passive management will be used for one of a number of reasons, namely:

  - To reduce costs, as ongoing monitoring requirements and management fees are significantly lower for passive management than for active management.

  - To invest in markets deemed efficient where the scope for active management to add value is limited.

- Illiquid investments, such as property or private equity, may be held as long as the Trustees judge that the lack of liquidity will not prevent the Scheme from achieving the investment objectives set out in Section 3.

- Investment in derivatives is permitted either directly or within pooled funds as long as they contribute to a reduction in risk or facilitate efficient portfolio management.

- Investment may be made in securities that are not traded on regulated markets. In recognition of the risks (in particular liquidity and counterparty exposure), such investments will normally only be made with the purpose of reducing the Scheme's mismatch risk relative to its liabilities or to facilitate efficient portfolio management. In any event the Trustees will ensure that the assets of the Scheme are predominantly invested in regulated markets.

- At the total Scheme level and within individual manager appointments, investments should be broadly diversified to ensure there is not a concentration of investment with any one issuer. This restriction does not apply to investment in UK Government debt.

## 6. Investment Strategy

Given the investment objectives the Trustees have implemented the investment strategy detailed in the table below. The Trustees believe that the investment risk arising from the investment strategy combined with the risks arising from active management are consistent with the overall level of risk being targeted:

| Asset Class | Target Benchmark Exposure (%) |
|---|---|
| **Index Linked Gilts** | **77.5** |
| Over 5 Year Index Linked Gilts | 10.0 |
| Under 15 Year Index Linked Gilts | 25.0 |
| Single Stock Index Linked Gilts (various) | 42.5 |
| **Corporate Bonds** | **22.5** |
| UK Corporate Bonds | 22.5 |
| **Total** | **100.0** |

The current investment strategy, as outlined above, is intended to help reduce funding level volatility whilst the Trustees consider the viability of a buy-in of some or all of the Scheme's liabilities. If it is discovered that a buy-in is not feasible at the present time the Trustees will review the suitability of the above strategy, in particular whether there is deemed to be sufficient excess return potential to progress towards buy-in in the future.

## 7. Day–to-Day Management of the Assets

The Trustees delegate the day-to-day management of assets to investment managers and have currently appointed two with whom day-to-day responsibility for the investment of the Scheme's assets rests. The Trustees have taken steps to satisfy themselves that the managers have the appropriate knowledge and experience for managing the Scheme's investments and that they are carrying out their work competently.

The Trustees have determined, based on expert advice, a benchmark mix of asset types and ranges within which each appointed investment manager may operate.

The Trustees regularly review the continuing suitability of the Scheme's investments, including the appointed managers. Any adjustments would be done with the aim of ensuring the overall level of expected return and risk is consistent with that being targeted as set out in Section 3.

Details of the currently appointed managers can be found in the Investment Policy Implementation Document ("IPID").

## 8. Expected Return

The Trustees expect the initial strategic asset allocation set out in Section 6 to generate a return, over the long term, of circa 0.2% per annum (before expenses) in excess of that implied by a portfolio of appropriate long-dated Government debt. It is recognised that over the short-term performance may deviate from the long-term target.

## 9. Realisation of Investments

The investment managers have discretion in relation to the timing of the realisation of investments and in considerations relating to the liquidity of those investments, within parameters stipulated in the relevant appointment documentation and pooled fund prospectuses.

The investment managers rebalance the portfolio as set out in the IPID.

## 10. Investment Manager Appointment, Engagement and Monitoring

**Aligning manager appointments with investment strategy**

The investment managers are appointed by the Trustees based on their capabilities and, therefore, their perceived likelihood of achieving the expected return and desired risk characteristics. The Trustees utilise the Investment Consultant's manager research ratings in decisions around the selection, retention and realisation of manager appointments. These ratings are based on the Investment Consultant's assessment of the manager's idea generation, portfolio construction, implementation and business management.

If the investment objective for a particular manager's fund changes, the Trustees will review the fund appointment to ensure that it remains appropriate and consistent with the Trustees' wider investment objectives.

The UK Corporate Bond mandate is actively managed and the manager is incentivised through a performance target (and this appointment would be reviewed following periods of sustained underperformance). The Trustees will review the appropriateness of using actively managed funds as part of the wider monitoring of the Scheme's managers.

As the Trustees invest in pooled investment vehicles they accept that they have no ability to specify the risk profile and return targets of the manager, but appropriate mandates can be selected to align with the overall investment strategy.

With respect to the index linked gilt portfolio, the manager has been appointed to manage the assets across a range of durations with the splits designed to broadly reflect the profile of the underlying liabilities of the Scheme.

The investment managers are aware that their continued appointment is based on their success in delivering the mandate for which they have been appointed. If the Trustees are dissatisfied, then they will look to replace the manager.

**Evaluating investment manager performance**

Trustees receive investment manager performance reports on a quarterly basis, which present performance information over a range of time periods. The Trustees review absolute performance, relative performance against a suitable index used as a benchmark, where relevant, and against the manager’s stated performance target (over various time periods), on a gross of fees basis. The Trustees’ focus is primarily on long term performance but short term performance is also reviewed.

If a manager is not meeting performance objectives, or their investment objectives for the mandate have changed, the Trustees may ask the manager to review their fees instead of terminating the appointment.

**Responsible Investing engagement with investment managers**

The Trustee will also consider the Investment Consultant’s assessment of how each investment manager embeds ESG into its investment process and how the manager’s responsible investment philosophy aligns with the Trustees’ responsible investment policy. This includes the investment managers’ policy on voting and engagement (where relevant). The Trustees will use this assessment in decisions around selection, retention and realisation of manager appointments. Further information is set out in Section 11.

**Portfolio turnover costs**

The Trustees do not currently monitor portfolio turnover costs but are looking to do this going forward and plan to include such analysis periodically as part of their ongoing monitoring on the investment managers.

In particular, the Trustees plan to ask investment managers to include portfolio turnover and turnover costs in their presentations and reports to the Trustees going forward.

The Trustees will engage with a manager if portfolio turnover is higher than expected. This may be assessed by comparing portfolio turnover across the same asset class on a year-on-year basis, or relative to the manager’s specified portfolio turnover range in the investment guidelines or prospectus.

**Manager turnover**

The Scheme is a long-term investor and the Trustees are not looking to change the investment arrangements on a frequent basis.

The Trustees will retain an investment manager unless:

- There is a strategic change to the overall strategy that no longer requires exposure to that asset class or manager; [and/or]

- The manager appointment has been reviewed and the Trustees are no longer comfortable that the manager can deliver the mandate.

## 11. Socially Responsible Investment and Corporate Governance

Financially material considerations, including (but not limited to) environmental, social and governance ("ESG") considerations (including climate change) are considered by the Trustees.

The Trustees believe that good stewardship and ESG issues 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. The Trustees also recognise that long-term sustainability issues, particularly climate change, present risks and opportunities that increasingly may require explicit consideration. The Trustees have taken into account the expected time horizon of the Scheme when considering how to integrate these issues into the investment decision making process.

The Trustees have given the appointed investment managers full discretion in evaluating ESG factors, including climate change considerations, and exercising voting rights and stewardship obligations attached to the investments, in accordance with their own corporate governance policies and current best practice, including the UK Corporate Governance Code and UK Stewardship Code. Given the evolution of the investment strategy in recent years there are no longer holdings in equities and hence there are no longer assets held which have voting rights.

As the Trustees invest in pooled fund arrangements they have not set any investment restrictions on the appointed investment managers in relation to particular products or activities. However, with the assistance of the Investment Consultant, the Trustees monitor the activities of the investment managers in relation to ESG factors and risks, including engagement with investee firms and the exercise of voting rights (where relevant).

The Trustees consider how ESG, climate change, and stewardship is integrated within investment processes in appointing new investment managers and monitoring existing investment managers. Monitoring is undertaken on a regular basis and is documented at least annually.

The Trustees do not explicitly take into account any non-financial matters (for example the views of members of the Scheme on ethical issues) in the selection, retention and realisation of assets.

## 12. Compliance with this Statement

The Trustees monitor compliance with this Statement annually and may seek written confirmation from the investment managers that it has given effect to the investment principles in this Statement so far as reasonably practicable.

## 13. Review of this Statement

The Trustees will review this Statement at least once every three years and without delay after any significant change in investment policy. Any change to this Statement will only be made after having obtained and considered the written advice of someone who the Trustees reasonably believe to be qualified by their ability in and practical experience of financial matters and to have the appropriate knowledge and experience of the management of pension scheme investments.