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Investment Strategy Statement

Consultation Draft 2024

West Sussex County Council

lgps Local Government Pension Scheme

Introduction and Purpose

This is the Investment Strategy Statement for the West Sussex Local Government Pension Scheme as required under Clause 7 of The Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016.

The Local Government Pension Scheme (LGPS) is one of the largest public sector pension schemes in the UK. It is a nationwide pension scheme with five million members across over 10,000 employers. The LGPS in England and Wales is administered locally through 90 local pension funds. The scheme regulations are made under the Superannuation Act 1972 and the Public Service Pension Schemes Act 2013. Changes to scheme rules are discussed at national level by employee and employer representatives but can only be amended with the approval of Parliament.

West Sussex County Council is the Administering Authority responsible for maintaining and managing the West Sussex Pension Fund on behalf of its stakeholders: the scheme members and employers participating in the Fund. Flexibility is provided for each Administering Authority to determine their own governance arrangements and further information can be found in the Governance Policy and Governance Compliance Statement.

On 31 March 2023 the Pension Fund:

- was valued at £5.34bn,
- had 86,000 members, 23,000 of whom were receiving a pension
- had over 200 employers actively paying contributions into the Scheme
- was 125% funded

This Statement will be reviewed at least every three years and will be updated to reflect any substantive changes in the interim. The last formal review was at the Pensions Committee meeting in July 2023. This document has been prepared after taking appropriate advice.

Governance

The Pensions Committee have responsibility for managing the West Sussex Pension Fund. Specifically:

The Pensions Committee is responsible for the determination of the Pension Fund's investment strategy and oversight of the delivery of the strategy, appointment of professional and specialist investment advisers and managers on a consultancy basis and consideration of the recommendations of the advisers and managers.

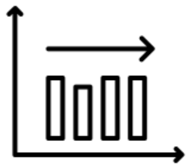
The Pensions Committee have an obligation to act as fiduciaries, safeguarding the interests of beneficiaries of the West Sussex Pension Fund. Decisions must be taken in accordance with public law obligations, including the obligations of reasonableness, rationality, and impartiality. The pursuit of appropriate risk adjusted return should therefore be the Committee's predominant concern, but it may also take non-financial considerations into account provided that doing so would not involve significant risk of financial detriment to the Scheme.

The Pensions Committee integrates environmental, social and governance principles throughout its investment decision-making process, from setting investment strategy to monitoring the Fund's investment managers – taking appropriate advice. It also oversees environmental, social and governance risks and opportunities, including those relating to climate.

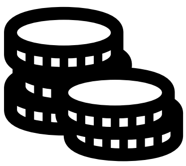
The Pensions Committee is responsible for the consideration of and response to the recommendations of the LGPS ACCESS Joint Committee. In 2015 the Government encouraged LGPS Administering Authorities to work together to "pool investments to significantly reduce costs, while maintaining investment performance". Whilst each Authority retains autonomy to make decisions about strategic asset allocations, the ACCESS Joint Committee is responsible for making collective decisions in relation to contract management and budgets.

The process for ensuring suitability of investments

There are several factors which are considered when the investment strategy is prepared including those set out below.



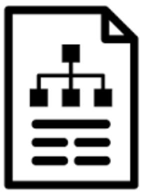
The Regulatory requirement that the Fund maintains as nearly constant employer contribution rates as possible and to contribute towards achieving and maintaining full funding.



The Pension Committee’s objective to maintain affordability of the Fund to employers as far as this is reasonable.

The need to meet pension liabilities as they fall due and, as a maturing Scheme, identify sources of income to generate cash as the Fund requires and to avoid being a forced seller of assets to pay benefits.

The objective to keep risk within acceptable limits.

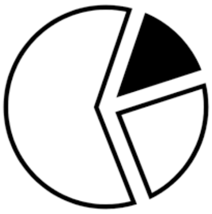


The need to consider credible, relevant, and distinctive scenarios for the potential impact of the future path of climate change on the Pension Fund’s assets, and in turn the investment strategy. This looks to capture longer-term potential impacts, as well as sudden events such as sudden climate related events, but it is acknowledged that there are high levels of uncertainty.

A successful investment strategy for the West Sussex Pension Fund is considered by the Pension Committee and advisers to be one which will maintain at least 2/3rds likelihood of being fully funded over 20 years and will maintain consistent employer contributions of around 18% of pay. This is consistent with the aims of the Fund’s Funding Strategy Statement and informs the assumptions made by the Actuary for funding purposes.

Investment Beliefs

The investment strategy is aligned to the Pension Committee's investment beliefs, as set out below. Clear investment beliefs have been evidenced as a common feature of well governed and strongly performing pension funds. These aid with decision making and provide a consistent framework for setting and implementing investment strategy:



Strategy

A long-term view should be taken when setting the investment strategy. This is important because the Pension Fund is open to new members and employer covenants are generally strong. By investing with a long-term view, the Committee can access opportunities which maximise the Pension Fund's investments, benefitting from the long-term risk premium earned from investing in equities, credit, property, and other illiquid assets, relative to government bonds. This will reduce transition costs that are associated with making short term tactical changes. In turn this provides the best possible net outcomes for stakeholders.

Specifically, illiquid investments should be considered by the Pensions Committee where an attractive premium return is expected to be available, though the total allocation within the Fund will be limited. This is important because, as a long-term investor, it allows the Fund to benefit from the illiquidity premium as part of a balanced approach to generating returns and managing risk.

Whilst the Committee take a long-term view, the investment strategy should be reviewed in conjunction with each actuarial valuation to recognise any changes. These include changes to the funding requirements, the appropriateness of risk within the investment strategy (and how this helps meet its objective of stable and affordable contribution rates for employers), government regulation and guidance, market conditions and changing environmental, social and governance risks and opportunities.

Avoiding a large number of separate manager relationships, and assessing the performance of active managers over suitably long periods, is preferable. This supports the Pensions Committee's approach to responsible investment and strong governance by appointing the best-in-class high conviction active investment managers and supporting a culture of long-term investment. This in turn should provide higher returns net of fees over the long term.

Fees and costs incurred within investment manager mandates are important, but the emphasis is on achieving the best returns net of fees. This is important because the Fund should be able to evidence value for money when investing Fund assets.

Local investments should be considered, though the risks and expected returns should be commensurate with comparable investment opportunities elsewhere. This is important because the Committee must maintain their fiduciary duties when considering potential investment opportunities and take a balanced approach to managing risk.

Governance

The Pensions Committee acknowledge that there can be conflicts of interest if the ability to represent the interests of the Pension Fund is hindered by other interests. These conflicts can arise within the Pensions Committee, with officers, or within external service providers. All members of the Committee and officers must declare any pecuniary or other registerable interests, including any that may affect the stewardship of the Fund’s investments. The Pensions Committee also expects effective policies to be in place to address any potential conflicts of interest.

Whilst the Pensions Committee can establish member groups to review aspects of investment strategy, all members of the Pensions Committee are responsible for determining the investment strategy, monitoring, and engaging with investment managers and considering environmental, social and governance matters.

Stewardship

Environmental, Social and Governance matters form a core part of any manager selection decision and the Fund should encourage its investment managers to engage with companies to drive positive change, reflective of a transition pathway to a low carbon future.

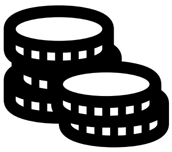
Active engagement with companies is preferred to exiting or not investing in companies. Well managed companies will produce superior returns for the Fund over the long term. Engagement will be with a company that supports research, monitoring, supports the management team and provides opportunity to influence. However, it is acknowledged that engagement requires an escalation strategy, and the Pensions Committee will discuss with its investment managers the actions taken if requests through engagement are ignored.

The Fund should exercise its voting rights as fully as possible and, whilst guidelines are maintained for some investments, ultimately providing investment managers with the ability to vote on the Pension Committee’s behalf strengthens their position when engaging with companies.

Strategic Asset Allocation

Strategic asset allocation refers to a long-term weighting to various types of investment (or asset classes) which are considered to meet the Pension Committee's objectives. Investments are then rebalanced periodically when the actual positions deviate from the strategic asset allocation weights due to market movements.

Different investments have different characteristics which help the Committee meet its overall objectives as described below.

	Nearly constant employer contribution rates and maintaining full funding.	➔	"Protection" assets such as bonds change value in line with liabilities and protect against movements in interest rates and inflation expectations.
	Maintain affordability to employers as far as reasonable.	➔	"Growth" assets such as equities and private equities generate higher returns and are therefore a key driver of long-term returns which help keep contributions affordable.
	The need to meet pension liabilities as they fall due generate cash as required.	➔	"Income" assets such as property, infrastructure and private debt generate a reliable income providing additional cash flows to pay for benefits. They also provide some additional yield versus protection assets.
	Keep risk within acceptable limits.	➔	The blend of the above provides diversification to reduce overall volatility of the portfolio.

Considering the above, the Pensions Committee have set a strategic asset allocation which invests Fund money in a wide variety of investments and is based on detailed advice from the Fund Actuary, Investment Consultant, and Investment Adviser through the completion of Asset Liability Modelling work. The current strategic asset allocation is illustrated below:

It should be noted:

- Whilst there is no strategic asset allocation to cash, cash is held as working balances in line with the Pension Committee's Treasury Management Strategy to pay benefits, cover invoices and fund investments.
- The strategic asset allocation reflects the long-term weighting to various asset classes. Whilst changes are not expected in the short term, if the funding level falls back to 90% the Pensions Committee will consider increasing the proportion of growth assets and/or raising the contribution rate target. No further de-risking is expected, such as increasing the proportion of protection assets.

Management of Asset Movements

Whilst the Pensions Committee have set a strategic asset allocation, market movements and investment activity can mean that the actual positions deviate from the strategic asset allocation weights from time to time.

The Committee believes that it should not take short term tactical asset allocation positions relative to the strategic asset allocation. Tactical asset allocation refers to shifts in asset allocations in a portfolio to take advantage of market trends or economic conditions.

In addition, buying and selling of investments can be expensive, particularly in relation to private equity, private debt, infrastructure, and property (the less illiquid assets within the portfolio).

To manage this, the Pension Committee have agreed a 'rebalancing' approach for investments in global equities and global corporate bonds to allow some incremental returns, reflecting shorter term market fluctuations but avoiding an overweight position to unintentionally develop.

On a quarterly basis, the Committee will review the actual positions of each of the investment portfolios against the strategic asset allocation and target ranges. The strategic asset allocation and target ranges are shown below:

Sub Fund Manager	Asset Class	Target %	Range
Baillie Gifford	Global Listed Equities and Global Corporate Bonds	40%	30-50%
Macquarie	Global Listed Equities	20%	15-25%
Fidelity	Global Corporate Bonds	15%	7.5%-22.5%

Where rebalancing is required because an investment portfolio is above or below the target range, cash holdings should be used where available to rebalance followed by other liquid portfolios (rebalancing to the midpoint of the tolerance range).

Management of Cashflow

It is important that the Pensions Committee manages its net cashflow position to ensure pension liabilities can be paid as they fall due, return on investments are maximised and the Pension Fund avoids becoming a forced seller. Whilst the Pensions Committee consider cashflow on a quarterly basis, benefit payments, contribution income, employers exits and drawdowns from investment managers can all be unpredictable.

The Pensions Committee have agreed the approach set out below for shorter term cash requirements (the liquidity ladder). The impact of trading costs is reflected in the priority order i.e., focusing on cash then equities before the more expensive bonds.

Step	Action
➊	Small cash buffer is maintained to reflect quarterly flows.
➋	If cash is unavailable, listed global equities will be sold to meet the cash requirements.
➌	If required, any further liquidity would be sourced from global corporate bonds.

To prevent listed equities and corporate bonds being depleted, they should then be replaced by the less liquid investments, over a reasonable time period.

Approach to Responsible Investment

The Pensions Committee believe that acting as a responsible investor by managing the Fund's assets in a manner consistent with long-term sustainable outcomes and making decisions within a long-term outlook is a core pillar of its fiduciary duty to beneficiaries of the Scheme. Investing in this way is considered by the Committee to provide an opportunity to generate better than expected returns and can lead to improved wider societal and environmental outcomes.

The Committee welcome investment opportunities which deliver a positive and measurable societal and/or environmental outcome, combined with an appropriate level of financial return. Where such opportunities exist, are investable and appropriate for the Fund, the Committee's view is favourable where investment without financial detriment is possible (i.e., without compromising on financial returns).

The Pensions Committee believes that investors with long-term time horizons may be more exposed to certain risks and should therefore take an approach to investing that aims to incorporate environmental, social and governance factors into investment decisions, to better manage risk and to generate sustainable returns. This includes climate related risks.

Action is required to transition economies to a low-carbon future and reduce global emissions, ultimately to net zero. There are a variety of possible transition scenarios and many uncertainties. The Pensions Committee therefore approaches manager appointments and fund investments with care and diligence, taking advice from suitably expert and reputable advisors. In some instances, where this aligns to its asset allocation and investment strategy, the Committee will consider investment in portfolios which exclude fossil fuel companies (i.e. those who gain the majority of their revenues from the extraction and production of coal, oil and gas) or which have other carbon reduction metrics or targets. In all instances, the Committee will pursue an engagement-led approach, encouraging the companies invested in to transform and adapt to meet the needs of a changing world.

The Committee will develop reporting on how assets (held directly and indirectly) will affect and be affected by climate change and work to assess the carbon intensity of all assets (using estimates if necessary).

To appropriately capture opportunities and mitigate risks within all investments made, it is important that the Committee and appointed investment managers embed consideration of Environmental, Social and Governance factors into their strategy and the management of investments on an ongoing basis. In practice this means that ESG factors are considered by the Pensions Committee as set out below

Setting the investment strategy	➔	Investment manager appointment	➔	Discharging the rights and responsibilities of asset ownership	➔	Investment manager monitoring

This in turn should encourage and promote high standards of governance and corporate responsibility - including consideration of climate change - with investment managers and in the underlying companies and assets in which the Fund (directly or indirectly) invests.

Whilst the Pensions Committee acknowledge that it is important to consider the appropriate nuances and differences which apply to differing asset types and taking appropriate expert advice, they do expect that all managers:

- Understand and integrate financially-material ESG risks into their analysis and investment processes
- Have clear policies on engagement and engage with companies on ESG-related issues
- Be able to provide a robust investment rationale for all companies held as part of a portfolio or strategy
- Seek to support – through their investment decisions and stewardship activities – the transition to a low carbon economy, provided the investments made fit within the risk and return parameters and are consistent with the trustees' fiduciary duties
- Continue to improve the quality, clarity, and consistency of climate-related data they provide and ensure that those they invest in also recognise this objective

This applies to all asset classes, but there are specific considerations for different asset types, as set out below.

Asset Class	**Consideration**
Global listed equities	The mandate with each investment manager reflects long-term performance expectations and require that appointed managers consider several factors – including financial – when making decisions about which companies to buy, sell and retain. Once an investment is made the Pensions Committee expects managers to be proactive in their engagement and asset stewardship activity. Corporate engagement can deepen the knowledge of and confidence in those companies invested in, build relationships and collaboration with company management. It allows investments managers to use their influence as a long-term investor to encourage positive behaviour and support improved practices. Voting powers are exercised by investment managers with the objective of preserving and enhancing long term shareholder value. The Fund expects the investment manager(s) to vote on all the shares they hold, and whilst Voting Guidelines may exist, these are on a comply or explain basis and the Pensions Committee supports investment managers retaining the ability to vote on the Pension Committee's behalf, to strengthen their position when engaging with companies. Investment managers are required to report on a quarterly basis to the Fund, including details of votes cast on corporate resolutions and company engagement for holdings in relevant portfolios. The Committee consider the information provided to discuss specific issues facing asset owners and activities undertaken by managers and to understand the effectiveness of engagement activity.

Asset Class	Consideration
Global corporate bonds	The mandate with each third-party investment manager reflects long term performance expectations and require that appointed managers consider several factors – including financial – when making decisions about which companies to buy, sell and retain. Understanding environmental, social and governance issues relating to a company can add value in both controlling risk and identifying opportunities for outperformance. The materiality of these factors will vary depending on the company's sector, region and the strength of its financial position. Whilst the ability to influence differs from that of a shareholder, given the contractual nature of the relationship with issuers, there is still opportunity to engage with corporate issuers of debt.
UK Direct property	Multiple ESG factors are relevant when managing assets (such as energy efficiency, use of certain materials, susceptibility to flood risk) and the Committee believe that understanding the characteristics of the property portfolio is fundamental in monitoring sustainability. The Fund's appointed property investment manager is expected to engage proactively with its assets in order to improve their characteristics over time and to safeguard and enhance the value of the Fund's portfolio. These enhancements (such as reduced energy consumption; water efficiency) are positively linked to the Fund's aim to support long-term sustainable outcomes. The portfolio is monitored against the Global Real Estate Sustainability Benchmark ('GRESB') and actions are discussed to continuously improve.
Private debt	As a provider of finance to private companies, ESG factors are an important factor when investing in private debt. The nature of the investment allows the manager to actively engage with companies and obtain information on their ESG approach to ensure companies are well governed and run given this will impact on their credit worthiness and the ability to meet ongoing loan obligations. The Fund's private debt managers' report regularly on how ESG factors have been considered as part of their loan origination and ongoing monitoring. Managers are also increasingly incorporating ESG and climate related metrics and goals in their loan terms with companies.

Asset Class	Consideration
Private equity	As a provider of capital to private companies, ESG factors are an important when investing in private equity. The nature of the investment allows the manager to actively engage with companies and obtain information on their ESG approach to ensure companies are well governed and run given this will impact on their growth potential and sustainability of the businesses. Stewardship can also have a greater impact than public equity investments and therefore is important for managers to ensure alignment of investment objectives. The Fund's private equity managers' report regularly on how ESG factors have been considered as part of their investments and ongoing monitoring of companies.
Infrastructure	Long-term infrastructure investors should consider a broad range of ESG issues that potential and existing investments might face over the course of the assets' life. The nature of infrastructure assets also means they can have a much more direct impact on communities, individuals and climate and therefore it is crucial that ESG considerations are considered and managed appropriately. The Fund's infrastructure manager reports regularly on their monitoring and management of ESG factors which includes the positive impact that investments can have on climate and communities.

Agreements with investment advisers and consultants also set out the requirement that each considers and integrates ESG issues when providing investment advice. This means that the Fund takes full consideration of ESG issues as they relate to its strategic asset allocation, including the impact of ESG matters on differing asset types and where ESG issues could have a material impact on the value of the Fund's assets and the funds in which the Fund invests.

The Fund recognises that collaboration with other investors is a powerful tool to keep informed of developments in this area and gives the potential for collective action to influence the behaviour of companies, policy makers and other industry stakeholders. This also applies to the appointed investment managers.

Scenario Analysis

The Pensions Committee recognises that climate change is one of the material Environmental, Social and Governance factors which pose a potential financial risk over the long term, and that it is important to consider the implications for the Fund of the challenges posed by climate change.

The Committee have therefore commissioned climate-related scenario analysis to help create and maintain its investment and funding strategies. It is considered that the results support the Pensions Committee's core belief on considering Environmental, Social and Governance issues when setting and implementing the investment strategy, engagement with policy makers and holding managers to account.

Whilst this is a developing area the Pensions Committee have received advice as part of determining the investment strategy.

The Committee will consider whether any new scenario analysis should be carried out to reflect any changes in the investment strategy, improvements in the availability of data, changes to the way the investment strategy is being implemented and investments invested, any consensus within the industry about modelling techniques or changes to government guidelines or Regulations.

In the future, the Pensions Committee may determine metrics to be reported against, and targets set relevant to the Pension Fund's investment strategy and the way climate-related risks and opportunities are managed.

Investment Risk

The Fund has an active risk management programme in place and the full risk register is reviewed regularly. The risk register includes those risks that may impact on the investment strategy and what appropriate measures are in place to mitigate those risks. The Pensions Committee considers risk including investment risk at each meeting.

Risk management is central to the Fund and measures are in place to manage the risk that the investment strategy will impact the ability to meet future pensions liabilities.

Risk is managed by setting investment beliefs, funding and investment objectives that are incorporated into the Fund's asset allocation.

The risks that are most likely to impact the investment strategy are –

- Investment risk: the risk of investments not performing (income) or increasing in value (growth) as forecast.
- Liquidity/maturity risk: the LGPS is going through a series of changes, each of which will impact upon the maturity profile of the Fund and have potential cash flow implications.
- Liability risk: inflation, life expectancy and other demographic changes, and interest rate and wage and salary inflation will all impact upon future liabilities.
- Regulatory and compliance risk: occupational pensions in the UK are heavily regulated, with thousands of pages of both general and LGPS-specific legislation that must be complied with.
- Climate related risk: the impact of the physical and transitional risks of climate change in the long term, and the responses of policy makers, on the finances of the Fund.

The above risks are included within the overarching risk management framework and strategy of the Fund

Investment Pooling

The LGPS ACCESS asset pool has a responsibility for implementation of the investment strategy where suitable pool investment solutions become available, except in respect of non-pooled assets which remain with the fund.

The Pensions Committee have agreed the following criteria for pooling:

- That the Pool enables access to an appropriate solution that meets the objectives and benchmark criteria set by the Fund
- That there is a financial benefit to the Fund in investing in the solution offered by the Pool, should a change of provider be necessary.

The Fund intends to keep its property allocation and legacy private equity and private debt investments outside of the formal pooling arrangement proposed based on ongoing value for money, large one-off transition costs and illiquidity of these assets.

Any asset that remains outside of the Pool will be reviewed at least every three years to determine whether the rationale remains appropriate and whether it continues to demonstrate value for money.

The ACCESS Pool Operator (Link Fund solutions) has a responsible investment framework and voting guidelines for investment managers, to promote good corporate governance and management in the companies invested in. The Operator requires investment managers to report on voting activity monthly including any cases where the investment managers considers that there have been good reasons not to follow the voting guidelines set out.

The Operator expects that investment managers will be signatories to and comply with the Financial Reporting Council’s Stewardship Code (the Code) and United Nations Principles of Responsible Investment (UNPRI).