National Library of Wales Staff Superannuation Scheme
Statement of Investment Principles
August 2020

1. INTRODUCTION

1.1. The Pensions Act 1995, as subsequently amended by the Pensions Act 2004, requires trustees to prepare a statement of the principles governing investment decisions. Whilst the Trustees of the National Library of Wales Staff Superannuation Scheme ("the Scheme") are exempt from this requirement as a result of the Scheme having a Crown Guarantee, the Trustees nevertheless consider it best practice to maintain a Statement.

1.2. The Trustees have prepared this Statement of Investment Principles ("the SIP") to govern the investment decisions of the Scheme in order to meet its investment objective.

1.3. In preparing the SIP and prior to any future changes to the SIP the Trustees will obtain and consider appropriate investment advice from the Fiduciary Manager.

1.4. The Trustees will review the SIP whenever there is a change in the investment strategy. As a minimum the Trustees will review the SIP every three years. The Trustees will notify the Fiduciary Manager when the parameters of the investment strategy change. Furthermore, any material changes to the employee covenant or Scheme will trigger a strategy review, at which point the Trustees will notify the Fiduciary Manager.

1.5. The SIP has been prepared in accordance with local regulatory requirements and industry best practice. The SIP should be considered in tandem with the Scheme's Investment Management Agreement ("the IMA") and Pensions Act 1995 Advisory Agreement, both signed in agreement with the Fiduciary Manager.

1.6. The SIP will be made available upon request.

1.7. **This version of the SIP was agreed on 6 August 2020**.

2. SCHEME DETAILS

2.1. The Scheme operates for the sole purpose of providing retirement benefits and death benefits to eligible participants and beneficiaries

2.2. The Scheme is open to future accrual and a summary of the main provisions of the Scheme can be found in the report entitled **Actuarial valuation as at 31 March 2019**.

2.3. The Scheme provides the facility for members to enhance their retirement benefits by purchasing additional years of service with Additional Voluntary Contributions. As a result, these contributions are invested in line with the Scheme's investment strategy.

3. GOVERNANCE

3.1. The Trustees are responsible for ensuring the investment strategy is consistent with the Scheme's funding objectives and their assessment of the employer covenant.

3.2. Professional advisers have been appointed by the Trustees to support the running of the Scheme. Roles and responsibilities are as follows:

- Fiduciary Manager – advises on the long term investment strategy and manages the Scheme's assets in line with the investment strategy. The Fiduciary Manager will comply with legislation and investment management agreement/contract.

- Investment Managers – should consider the suitability and diversification of each investment. The Investment Managers will comply with legislation and their investment management agreements/contracts. The underlying Investment Managers are expected to exercise best practices.

3.3. The Trustees delegate the day-to-day investment decisions to the Fiduciary Manager. As governed by the investment strategy agreed with Trustees and the guidelines outlined in the IMA, the Fiduciary Manager will appoint investment managers to invest the Scheme's assets.

3.4. Some of the Trustees are remunerated indirectly by virtue of their employment by the Library. Trustees not employed by the Library are reimbursed expenses incurred in undertaking their roles as Trustees but are not paid explicitly.

4. INVESTMENT STRATEGY

4.1. The broad investment objectives of the Scheme are:

- To achieve long term growth of portfolio relative to its liabilities with an acceptable amount of risk, and
- To outperform the relevant benchmarks taking into account investment restrictions

4.2. Following professional advice, the Trustees have determined an appropriate asset allocation to be implemented by the Fiduciary Manager, as governed by the IMA. The IMA details the level of delegation afforded to the Fiduciary Manager and outlines the parameters the Fiduciary Manager must operate within. The IMA is subject to change over time as the strategy evolves.

4.3. The investment strategy defines the journey plan to achieve the investment objective. As part of this process the Fiduciary Manager will rely on assumptions to determine the liability profile and expected return across the portfolio of assets. The Trustees recognise that this is not an exact science and will constantly evolve, hence assumptions will be reviewed on a regular basis and updates will be factored in where appropriate.

4.4. The investment strategy for the Scheme is to:

- Invest in a portfolio of assets to immunise a proportion of the interest rate and inflation risk inherent within the Scheme's liabilities
- Invest in a diversified portfolio of assets to achieve an efficient risk / reward trade off with the objective of generating sufficient returns to close the Scheme's funding deficit

4.5. The de-risking plan for the Scheme:

- When the funding level is sufficiently ahead of the Journey Plan (beyond a predetermined level) assets will be switched out of the growth portfolio into matching assets,
- Should the funding level fall sufficiently behind the Journey Plan (beyond a predetermined level) this will act as a review trigger to consider re-risking, i.e. switch assets from matching to growth, and
- As the funding level improves and the Scheme approaches its time horizon the inflation and interest hedge ratios will be increased.

5. RISK MANAGEMENT

5.1. The Trustees recognise that the key risk to the Scheme is that it has insufficient assets to make provisions for 100% of its liabilities ("**funding risk**"). The Trustees have identified a number of risks which have the potential to cause a deterioration in the Scheme's funding level and therefore contribute to funding risk. These are as follows:

- The risk of a significant difference in the sensitivity of asset and liability values to changes in financial and demographic factors ("**mismatching risk**"). The Trustees and their advisers considered this mismatching risk when setting the investment strategy.
- The risk of a shortfall of liquid assets relative to the Scheme's immediate liabilities ("**cash flow risk**"). The asset allocation has taken into account the Scheme's liability cashflow profile from the most recent Actuarial Valuation. This should offer sufficient liquidity to meet liquidity needs. Should liquidity requirements change then the Trustees will notify the Manager and update the IMA accordingly.
- The failure by the Manager to achieve the rate of return required to meet the investment objective ("**manager risk**"). This risk is considered by the Trustees upon the initial appointment of the Manager and on an ongoing basis thereafter (for example by regular monitoring).
- The failure to spread investment risk ("**risk of lack of diversification**"). The Scheme's assets are invested across a range of pooled fund investments representing different assets classes in order to target the Scheme's objective, as set out in the IMA.
- The possibility of failure of the Scheme's sponsoring employer ("**covenant risk**"). The Trustees considered this risk by taking external advice when setting investment strategy and consulted with the sponsoring employer as to the suitability of the proposed strategy.

- The risk that exposure to overseas currencies has an adverse influence on investment values ("**currency risk**"). The Trustees considered this risk when setting the Scheme's investment strategy and this is managed risk by hedging a proportion of the overseas currency exposure.

- The risk that environmental, social and governance factors have an adverse effect on the long-term performance of the Scheme assets (**"ESG Risks"**). The Trustees will ensure that the Fiduciary Manager explicitly incorporates ESG information into investment decisions when considering the appointment and de-selection of investment managers.

- The risk that a custodian defaults ("**custodian risk**"). Assets are managed primarily within pooled funds and custody-related risks in relation to underlying pooled fund investments are managed by management companies or operators of such pooled funds. Outside of the pooled fund investments, the Trustees have appointed a Scheme custodian (BNY Mellon) to manage cashflows and settle trades on time.

- The risk that events outside the control of the Scheme have an adverse influence on investment values ("**event risk**"). The Trustees periodically reviews stress tests on the portfolio to understand the effect that extreme events could have on the Scheme's funding level so that they are able to plan accordingly. In addition, the Scheme invests in a diversified portfolio of assets to help manage volatility.

- The risk that a counterparty fails to fulfil its side of the agreement it makes in connection with derivative transactions ("**counterparty risk**"). The Trustees have appointed the Manager to mitigate this risk by assessing the credit quality of the counterparties it transacts with, ensures appropriate counterparty diversification and that collateral payments are made where required.

- The risk of fraud, poor advice or acts of negligence ("**operational risk**"). The Trustees have sought to minimise such risk by ensuring that all advisers and third-party service providers are suitably qualified and experienced and that suitable liability and compensation clauses are included in all contracts for professional services received.

5.2. The Trustees consider risk holistically across the portfolio and hence the Scheme's assets are invested across a diverse range of investments. Asset classes used as part of the investment strategy include, but not limited to, are:

- Equities – both active and passive strategies invested across different regions,

- Credit – both active and passive across the spectrum of risk including Investment Grade, High Yield, Emerging Market,

- Alternatives – these are often less liquid than other risky assets where an illiquidity premium is rewarded. These are designed to offer a diverse return stream to traditional risky assets such as equity.

- Liability Driven Investment – both derivatives and physicals.

5.3. The Trustees, with the aid of their Fiduciary Manager, monitor risk on both a qualitative and quantitative basis.

5.4. Implementing portfolio changes has been be delegated to the Fiduciary Manager who will assess the appropriateness of each transaction on a risk/return basis ensuring cost effectiveness.

6. RESPONSIBLE INVESTING

6.1. The Trustees recognise that ESG risks could impact the ability of the Scheme to meet its investment objectives and therefore the Trustees have considered how to evaluate and manage these risks when setting their investment strategy as set out in the following paragraphs (along with other matters).

6.2. The Trustees also recognise the importance of the Well-being of Future Generations (Wales) Act 2015, which focusses on improving the social, economic, environmental and cultural well-being of Wales. The Trustees believe that the Responsible Investing considerations outlined in this document broadly reflect the seven well-being outcomes of this Act.

6.3. The Trustees will ensure that the Scheme's Fiduciary Manager shall, alongside other investment risks, integrate consideration of ESG risks throughout its investment decision making processes,

6.4. The Trustees will request that:

- the Fiduciary Manager, as part of its due diligence, assesses the approach of all the Scheme's investment managers in integrating ESG risks considerations into the selection, retention and realisation of investments, before appointing them;

- the Fiduciary Manager, as part of its ongoing monitoring, will review the adherence of the Scheme's investment managers to their ESG principles and, on at least a quarterly basis, will report on key ESG metrics for the Scheme's investment managers and aggregate these to portfolio level where appropriate;

- the Fiduciary Manager, as part of its ongoing monitoring, reviews the execution of voting and engagement responsibilities and periodically reports back its findings to the Trustees (for example where the Scheme invests in pooled funds, the Scheme's investment managers are responsible for exercising voting rights and reporting on how they have exercised those rights); and

- where UK-domiciled investment managers are not signatories to the FRC's UK Stewardship Code, the Fiduciary Manager shall consider the investment manager's rationale for this position and, where appropriate, report back its findings to the Trustees.

6.5. The Trustees do not take into account non-financial matters when selecting, retaining and realising investments. Non-financial matters are defined as the views of members and beneficiaries, including (but not limited to) their ethical views, and their views relating to social and environmental impact and quality of life.

7. STEWARDSHIP

7.1. The Trustees understand that stewardship can enhance value over the long term and recognises that it has a responsibility to act as a good steward and protect and grow the long-term value of the Scheme for the benefit of the Scheme's members.

7.2. In order to be a good steward, the Trustees have set a policy to ensure that the Scheme's respective stakeholders undertake activities in relation to issues that have a material impact on the long-term value of the Scheme's investments.

7.3. The Trustees expect the Fiduciary Manager to ensure that the stewardship policy is appropriately implemented as far as is reasonably practicable. The policy includes ensuring to the extent possible that the underlying or external managers exercise on the Trustees' behalf rights and duties as an investor. This should include, where appropriate, voting and engaging with underlying investee companies, as part of an effective stewardship approach that meets the Trustees' expectations. The Trustees expect that voting and engagement activities are carried out in the best financial interests of the assets being managed.

7.4. The Trustees have delegated monitoring of underlying or external managers to the Fiduciary Manager. As part of this responsibility, the Fiduciary Manager is expected to:

- Request voting and/or stewardship policies of the underlying or external managers.

- Enquire about underlying manager's voting activity with respect to their stated policies, where appropriate.

- Request that underlying investment managers report on an annual basis a summary of the voting actions which have been taken and any votes cast which differ from the stated voting policy of that manager.

- Provide a summary to the Trustees of the overall level of voting activity on an annual basis.

7.5. The Trustees will engage with the Fiduciary Manager to understand any reports which have been provided and challenge any outcomes which they feel are not in keeping with policy. the Fiduciary Manager is expected to engage with the underlying or external managers as and when required to facilitate this. Where an underlying or external manager is not adhering to this policy in line with the Trustees' expectations, the Trustees would expect the Fiduciary Manager to consider appropriate actions having regard to the long-term financial wellness of the Scheme.

8. ARRANGEMENTS WITH MANAGERS

8.1. The Trustees recognise that the arrangements with all of the managers of the Scheme are important to ensure that its interests are aligned as far as is reasonably practicable. This includes arrangements with the Fiduciary Manager and the underlying or external managers. In particular, the Trustees seek to ensure that the Fiduciary Manager is incentivised to act in a way which generates the best long-term results for the Scheme.

8.2. The Trustees agree to share the SIP with the Fiduciary Manager and request that the Fiduciary Manager reviews the SIP and confirms that the investment strategy is aligned with the Trustees' policies.

8.3. The Trustees' policy on arrangements with asset managers will take into account the following five considerations:

- How the arrangement with the Fiduciary Manager incentivises the Fiduciary Manager to align its investment strategy and investment decisions with the Trustees' investment policies.

- How that arrangement incentivises the Fiduciary Manager to make decisions based on assessments about the medium to long-term financial and non-financial performance of issuers of debt or equity.

- How the method and time horizon of the evaluation of the Fiduciary Manager's performance and the remuneration for services are in line with the Trustees' investment policies.
- How the Trustees monitor "portfolio turnover costs" incurred by the Fiduciary Manager, and how they define and monitor targeted portfolio turnover or turnover range.
- The duration of the arrangement with the Fiduciary manager.

8.4. The Trustees recognise that there are different ways to engage with their managers including legal documentation as well as more informal arrangements such as ad hoc communication and reporting and monitoring deliverables provided by each manager.

8.5. The Trustees recognise that the predominant manager it has arrangements with is their Fiduciary manager. The arrangement is governed by the IMA between the Trustees and the Fiduciary Manager. The Trustees ensure that appropriate restrictions are outlined in the IMA in order to seek to ensure that the decisions which the Fiduciary Manager makes are in line with the long-term interests of the Scheme. This includes, but is not limited to, setting a clear investment objective, eligible instruments, asset allocation ranges and which asset classes are in scope for active and/or passive strategies.

8.6. The Trustees have also ensured that the IMA (and the supplemental disclosures provided by the Fiduciary Manager) include conflicts of interest policies in order to seek to ensure that incentives are aligned between the Trustees and the Fiduciary Manager as far as is reasonably practicable.

8.7. The Fiduciary Manager provides the Trustees with an annual cost transparency report. The report provides information in line with latest regulatory requirements for fiduciary managers. On a quarterly basis the Fiduciary Manager reports total performance net of fees so that the Trustees are able to take into account the impact of fees and costs when evaluating performance. The Trustees believe that in order to appropriately assess the performance of their managers, the net of costs performance returns should be monitored over various time periods to ensure that managers are evaluated in line with the Trustees' policies.

8.8. The Trustees will review the arrangements with the Fiduciary Manager on a regular basis, however there is no restriction on the duration of any arrangement.

8.9. The Trustees expect the Fiduciary Manager to review arrangements with the underlying or external managers which also have no restriction on duration of any arrangement. the Fiduciary Manager is expected to review these arrangements on an ongoing basis and take action to seek to revise any arrangements where it is understood to be in the best long-term interests of the Scheme.

8.10. The Fiduciary Manager is expected to take into consideration the Trustees' investment objective as well as Responsible Investing and Stewardship policies when selecting and/or appointing new underlying or external managers. The Fiduciary Manager is also expected to monitor the underlying managers or external managers and take into consideration the investments that they are permitted to make in order to seek that they are aligned with the long-term interests of the Scheme.

8.11. The Trustees believe that they have a governance framework in place in order to seek to ensure that the Fiduciary Manager's actions are aligned with the five arrangements policies listed above. If the Trustees have reason to believe that the Fiduciary Manager is acting outside of the Trustees' policies, the Trustees will bring this to the attention of the Fiduciary Manager as soon as is reasonably practicable and engage with the Fiduciary Manager so that the parties can understand such actions and seek to resolve any concerns.

9. REALISATION OF ASSETS

9.1. Assets can be held in segregated portfolios and pooled funds across a range of liquid and illiquid strategies. The allocation of Scheme assets to illiquid strategies has been considered with the Scheme's overall cashflow position in mind. Should the cashflow profile of the Scheme change (whereby benefit payments become proportionally significant) then the allocation to liquid assets can be increased. The liquid portfolio and LDI portfolio can be liquidated fairly easily.

10. MONITORING

10.1. The Trustees monitor the performance and risk exposures of the portfolio on a regular basis. The Trustees receive periodic reports showing:

- Commentary over the period covering performance, macroeconomic factors and portfolio positioning,
- Risk decomposition across the portfolio, including scenario stress tests,

- Return attribution across the portfolio, including underlying manager monitoring,
- Estimated funding ratio change, including a summary of contributors/detractors,
- Review of the funding level versus both the planned and expected journey plan, including any de-risking triggers,
- Asset allocation summary showing tactical asset allocation (where applicable) versus the strategic asset allocation and permitted ranges, and
- Interest rate and inflation hedge ratios versus target.

10.2. Monitoring of the underlying investment managers' suitability is delegated to the Fiduciary Manager. The Fiduciary Manager has been delegated the responsibility for ensuring the underlying strategies are satisfactory and appropriate for the investment strategy