

# Statement of Investment Principles

## Bhs Pension Scheme

September 2020

### Introduction

- 1 On 3 March 2016 the Bhs Pension Scheme (the Scheme) entered a PPF Assessment Period. During this Assessment Period the Trustees of the Scheme intend to continue to apply the investment principles set out in this document.
- 2 During 2017, the members of the Bhs Pension Scheme were given the option to transfer to a new scheme, BHS2 Pension Scheme. In February 2018, the majority of assets held by Bhs Pension Scheme were transferred to the new Scheme.
- 3 Whilst the Scheme remains in an Assessment Period, the Trustees are concurrently operating the investment principles set out in this document with a view to the proposed benefits that will need to be paid under the PPF. This may mean deviations from this document occur in some instances, however the Trustees do not see these as significant changes in investment policy and consider that the SIP remains consistent with the Trustees' overall investment policy.

### Pensions Act

- 4 Under the Pensions Act 1995, subsequently amended by the Pensions Act 2004, Trustees are required to prepare a statement of the principles governing investment decisions. This document contains that statement for the Scheme.
- 5 The power and responsibility for deciding investment policy lies solely with the Trustees.
- 6 In preparing this document, the Trustees have sought written advice from the Scheme's Investment Consultant (Willis Towers Watson). The written advice considers the requirements of the Occupational Pension Schemes (Investment) Regulations 2005 and the principles contained in this statement.
- 7 The Trustees will review this document, in consultation with the Investment Consultant and Scheme Actuary, at least every three years or without delay following a change in investment strategy, or where the Trustees think a review is needed for other reasons.
- 8 In preparing this document the Trustees have had regard to the requirements of the Pensions Act 1995 and any subsequent amendments and will consider those requirements on any review of this document or any change in their investment policy. The Trustees will refer to this document where necessary to ensure that they exercise their powers of investment so as to give effect to the principles set out in it.
- 9 When choosing investments, the Trustees and the Investment Managers (to the extent delegated) are required to have regard to the criteria for investment set out in the Occupational Pension Schemes (Investment) Regulations 2005 and the principles contained in this document.

### **Scheme details**

- 10 The Scheme operates for the exclusive purpose of providing retirement benefits and death benefits to eligible participants and beneficiaries.
- 11 The Scheme is registered under the terms of the Finance Act 2004.
- 12 In accordance with the Financial Services and Markets Act 2000, the Trustees set general investment policy and determine asset allocation but delegate responsibility for the selection of specific investments to an appointed Investment Manager or Managers, which may include an insurance company or companies. The Investment Managers shall provide the skill and expertise necessary to manage the investments of the Scheme competently.
- 13 Section 36(1) of the Pensions Act 1995 requires that the Trustees must exercise their powers of investment in accordance with the Investment Regulations. Regulation 4 of the Investment Regulations requires that the assets must be invested in the best interests of the members and beneficiaries and, in the case of a potential conflict of interests, in the sole interest of the members and beneficiaries.

### **Division of responsibilities**

- 14 The Trustees have ultimate responsibility for decision making on investment matters. In order to ensure that such decisions are taken effectively, the Trustees use other bodies either through direct delegation or in an advisory capacity. The roles of each group are shown below.

### **Trustees**

- 15 The Trustees of the Scheme are responsible for:
  - a. Reviewing this Statement of Investment Principles (SIP) on a regular basis and for modifying it if deemed appropriate, in consultation with the Investment Consultant and Scheme Actuary
  - b. Reviewing the suitability of the investment policy following the results of each actuarial review, and/or asset liability modelling exercise, in consultation with the Investment Consultant and Scheme Actuary
  - c. Assessing the quality of the performance and processes of the Investment Managers by means of regular reviews of the investment results and other information
  - d. Allocating assets between the Investment Managers
  - e. Appointing (and dismissing) Investment Managers.

### **Investment Managers**

- 16 The Investment Managers will be responsible for:
- a. At their discretion, but within any guidelines given by the Trustees, implementing changes in the asset mix and selecting securities within each asset class
  - b. Providing the Trustees with quarterly statements of the assets along with a quarterly report on actions and future intentions, and any changes to the processes applied to their portfolios.
  - c. Having regard to the need for diversification of investments so far as appropriate and to the suitability of investments and the criteria for investment set out in the Occupational Pension Schemes (Investment) Regulations 2005 as well as the principles contained in this document as far as is reasonably practicable.

### **Investment Consultant**

- 17 The Investment Consultant will be responsible for:
- a. Participating with the Trustees in regular reviews of this SIP, at least once every three years or without delay following a change in investment policy
  - b. Advising the Trustees in the following areas:
    - through consultation with the Scheme Actuary, how any changes within the Scheme's benefits, membership, and funding position may affect the manner in which the assets should be invested
    - of any changes in the Scheme's Investment Managers' organisations that could affect the interests of the Scheme
    - of any changes in the investment environment that could either present opportunities or problems for the Scheme
  - c. Undertaking project work as required including:
    - reviews of asset allocation policy
    - research reviews of Investment Managers
  - d. Advising on the competency and skill of the current Investment Managers and on the selection of new Investment Managers at the request of the Trustees.

### **Scheme Actuary**

- 18 The Scheme Actuary will be responsible for broad-ranging advice on the financial position of the Scheme, including:

- a. Liaising with the Investment Consultant on the suitability of the Scheme's investment strategy
- b. Advising the Trustees in relation to funding matters, including in relation to the Statutory Funding Objective under the Pensions Act 2004 and related matters taking into account the Scheme's current position of being in a Pension Protection Fund assessment period.

## Objectives

- 19 The investment objectives of the Scheme are:
- a. To limit the risk of the assets failing to meet the Scheme's liabilities and benefit promises over the long term; and
  - b. To minimise the long-term costs of the Scheme, having regard to objective **19a** above.
- 20 The Trustees' policy is to seek to achieve the objectives through investing in a suitable mixture of real, monetary and absolute return assets. They recognise that the returns on real assets, while expected to be greater over the long term than those on monetary assets, are likely to be more volatile. Moreover they expect that the returns from absolute return assets will be largely uncorrelated with those from either real or monetary assets.
- 21 In establishing the Scheme's asset allocation and manager structure, the Trustees receive advice from the Investment Consultant and will consider the risk and return assumptions of particular asset classes / investment opportunities and how this will affect the risk and return characteristics of the Scheme's assets as a whole.

## Expected return on investments

- 22 The Trustees' policy with regard to the expected return on investments is to set, from time to time, an overall objective, that represents their best judgement of what relative return is necessary to meet the relevant liabilities, given their understanding of the contributions likely to be received. The investment return objective is set from time to time by the Trustees.
- 23 The following table sets out the Investment Consultant's expectations for the rates of return to be earned in future on the various asset classes in which the Scheme invests and the expected volatility of those returns. They are based on market conditions as at 30 June 2020. All figures are for real returns in excess of price inflation, as measured by the Consumer Prices Index (CPI).

### Summary assumptions for Towers Watson Asset Model as at 30 June 2020 relative to CPI

	Arithmetic average 1 year real return	1 year standard deviation	10 year median real return

	% pa	% pa	% pa
UK long fixed interest gilts	-1.8	10.5	-1.4
UK long index-linked gilts	-2.6	8.6	-2.2
Cash	-1.9	1.3	-1.4
<b>Inflation (UK CPI)</b>	<b>1.3</b>	<b>1.5</b>	<b>1.6</b>

### **Manager structure**

- 24 The Scheme will invest in either segregated portfolios or pooled vehicles. When reviewing the Investment Managers, if applicable, the Trustees' policy is to obtain advice on whether the actual pooled vehicles invested in are satisfactory, as required by the Pensions Act.
- 25 The Scheme's assets will consist predominantly of investments admitted to trading on regulated markets. Investments in assets which are not admitted to trading on such markets will be kept to a prudent level.

### **Performance objectives and investment restrictions**

- 26 Each Investment Manager retained by the Trustees is set a performance target and a range of guidelines and restrictions have been agreed with each Investment Manager consistent with achieving those targets.
- 27 Whilst the Trustees are not involved in the Investment Managers' day to day method of operation and therefore cannot directly influence attainment of the performance target, they will assess performance and review each Investment Manager's appointment on a regular basis, usually annually. A measurable objective has been developed for each Investment Manager consistent with the achievement of the Scheme's longer-term objectives, and an acceptable level of risk.
- 28 The Investment Managers' restrictions are considered in such a way that the Scheme's assets are properly diversified so as to avoid excessive reliance on any particular asset, issuer or group of undertakings and so as to avoid accumulations of risk in the portfolio as a whole. Through these restrictions the Trustees attempt, as far as is practicable, to avoid investments in assets issued by the same issuer or by issuers belonging to the same group so as not to expose the Scheme to excessive risk concentration.
- 29 Investment in futures, options, currency forwards, or derivatives of any kind shall only be entered into for the purposes of hedging or efficient portfolio management (which shall include transactions for the purposes of asset allocation and transactions to reduce risk and/or costs). Such investments are subject to the restrictions detailed in the investment management agreement.

- 30 The Trustees' policy is not to leverage the portfolio. Some short-term borrowing for settlement is allowed, but is strictly limited and for the purpose of trade settlement only (which is standard practice in investment management). This, however, does not restrain Investment Managers from using leverage in their products where appropriate.

### **Manager monitoring**

- 31 The appointment of the Investment Managers will be reviewed by the Trustees based on the results of their monitoring of performance and investment process and of the Investment Managers' compliance with the requirements of the Pensions Act 1995 as amended by the Pensions Act 2004 and the criteria for investment set out in the Occupational Pension Schemes (Investment) Regulations 2005.
- 32 Before investing and periodically thereafter, the Trustees will ensure that the investment objectives and guidelines of any particular pooled vehicle are consistent with its policies, where relevant to the mandate in question.
- 33 Should the Trustees' monitoring process reveal that a manager's portfolio is not aligned with the Trustees' policies, the Trustees will engage with the manager further to encourage alignment. Where relevant, this monitoring process may include specific consideration of the sustainable investment/ESG characteristics of the portfolio and managers' engagement activities. If, following engagement, it is the view of the Trustees that the degree of alignment remains unsatisfactory, the manager will be terminated and replaced.
- 34 For most of the Scheme's investments, the Trustees expect the investment managers to invest with a medium to long time horizon, and to use their engagement activity to drive improved performance over these periods.
- 35 The Trustees appoint its investment managers with an expectation of a long-term partnership, which encourages active ownership of the Scheme's assets. Given this, the Trustee's arrangements with its investment managers have no set duration, but have appropriate termination rights included in their terms.

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### **Fee basis**

- 37 Investment manager fees for the Scheme are generally on an ad valorem basis, in line with normal market practice, for a given scope of services which includes consideration of long-term factors and engagement. The Trustees believe that it is not in the commercial interests of the Scheme to disclose a detailed schedule of investment manager fees.
- 38 Given the current position of the Scheme and the high quality of assets held, there is not expected to be any material turnover in the portfolio. As a result, the Trustee has no target turnover or turnover ranges against which turnover is monitored.

### **Social, environmental and ethical issues**

- 39 The Trustees have delegated responsibility for the selection, retention and realisation of investments to the Investment Managers.
- 40 In view of the low risk and largely passive investment strategy of the Scheme, the Trustees have formed the view that environmental, social and governance factors, including climate change, and other relevant matters including capital structure of investee companies, actual and potential conflicts, other stakeholders and the ESG impact of underlying holdings are not financially material to the Scheme and therefore have chosen not to take them into account in the development of the Scheme's investment strategy.
- 41 The Trustee has decided not to take into account non-financial considerations in designing and implementing the investment strategy, including (but not limited to) the views of members and beneficiaries of the Scheme.
- 42 The Trustees support the aims of the Stewardship Code and their Investment Managers are invited to operate in accordance with the guidelines laid out in the Stewardship Code which covers matters of both voting and engagement. The Investment Managers are required to report their adherence to the Stewardship Code using the "comply or explain" principle, where appropriate.

### **Rights attaching to investments**

- 43 The Trustees' policy is to delegate responsibility for the exercising of rights (including voting rights) attaching to investments to the Investment Managers.
- 44 The Trustees do not hold any equity securities either directly or within the investment strategy of any of its investment managers. As a result, the Trustees and its investment managers do not have any voting rights in relation to their investments.
- 45 The Trustees believe it is appropriate for its investment managers to engage in stewardship activity with key stakeholders. Such stakeholders may include corporate management of debt or equity issuers, other holders of the debt or equity, others with an interest in the issuer or debt or equity, or regulators and governance bodies (as appropriate to the Trustees' investments). As part of this, the Trustees expect investment managers to discuss with these stakeholders matters concerning the relevant issuer of debt or equity, including corporate governance, management of potential conflicts of interest, capital structure, performance, strategy, risks and ESG factors.

- 46 The Trustees expect that investment managers will provide details of their stewardship policy and activities on a periodic basis, where relevant to their investment strategy and restrictions.

### **AVCs**

- 47 Prior to its closure to future accruals on 15 August 2009, the Scheme provided a facility for members to pay AVCs into the Scheme to enhance their benefits at retirement. Members were offered a range of funds in which to invest their AVC payments. The Trustees' objective was to provide a range of funds which will provide a suitable long term return for members, consistent with members' reasonable expectations. As a result of entry into a PPF assessment period all AVCs have been discharged into members names.

### **The IGG Principles (formerly known as the Myners Principles)**

- 48 The Trustees have reviewed the IGG (Investment Governance Group) principles and confirm their broad compliance with the Principles.

### **Risk management**

- 49 The Trustees recognise a number of risks involved in the investment of the Scheme's assets. These risks are measured through the assessments described below. These risks are managed by taking them into consideration as described below:
- Solvency risk and mismatching risk:
    - are assessed through a qualitative and quantitative review of the expected development of the liabilities relative to the current and alternative investment policies
    - are considered by the Trustees during the reviews of the asset allocation strategy
    - Manager risk (underperformance risk):
      - is assessed by the expected deviation of the prospective return, as set out in the Investment Managers' objectives, relative to the investment policy
      - is considered by the Trustees who monitor the actual deviation of returns relative to the objective and factors supporting the Investment Managers' appointment
  - Liquidity risk:
    - is assessed by the level of cash flow required by the Scheme over a specified period
    - is considered by the Scheme administrators, who estimate the monthly benefit outgo and ensure that sufficient cash balances are available in order to limit the impact of the cash flow requirements on the investment policy.
  - Political risk and inappropriate investments:



- is assessed by the level of concentration in any one asset class leading to the risk of an adverse influence on investment values arising from political intervention
- is considered by the Investment Managers when carrying out regular assessment of the levels of diversification within portfolios managed on behalf of the Scheme and through specific asset limits and other restrictions within the investment guidelines.
- Counterparty and default risk:
  - is managed by the Investment Managers through the guidelines and restrictions set out in the Investment Manager agreements.

50 The Trustees will keep these risks under regular review.

**Accepted and Signed on behalf of the Trustees of the BHS Pension Scheme on 21<sup>st</sup> September 2020**