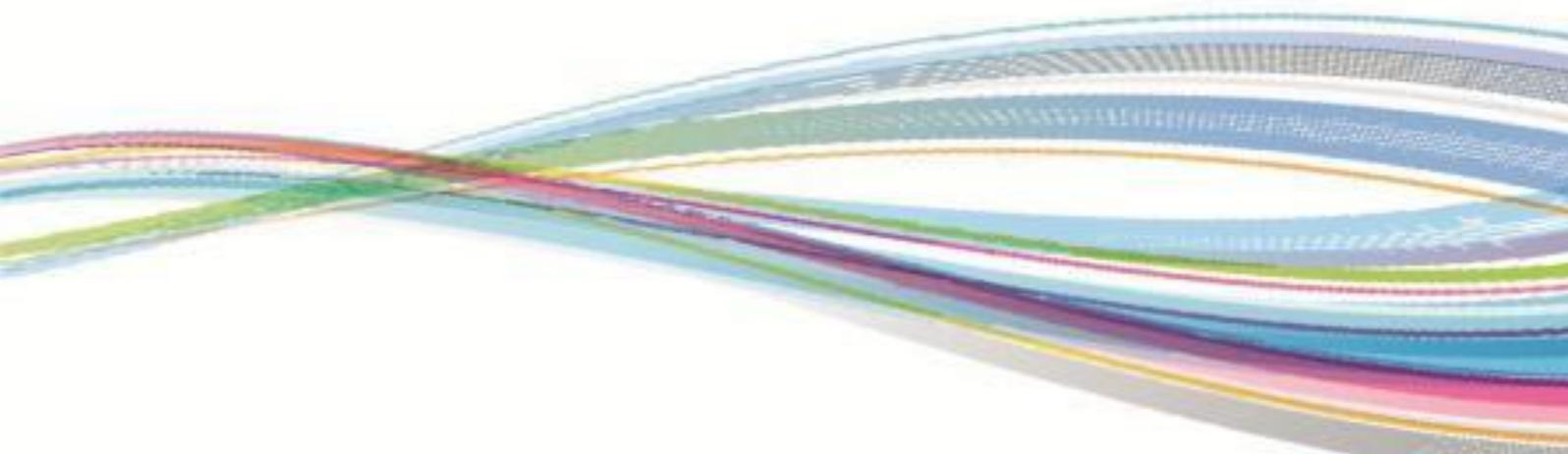


Investment Strategy Statement

October 2016



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1. INTRODUCTION

The Board (“the Board”) of the London Pensions Fund Authority (“the Fund”) has prepared this Investment Strategy Statement (“the Statement”) in accordance with the Guidance on Preparing and Maintaining an Investment Strategy Statement and after taking appropriate advice.

As set out in the Regulations, the Board will review this Statement from time to time, but at least every three years, and revise it as necessary. Also, in the event of a significant change in relation to any matter contained in this Statement, changes will be reflected within six months of the change occurring.

The Regulations require all Administering Authorities to take “proper advice” when formulating an investment strategy. In preparing this document and the overall investment strategy the Board has taken advice from Local Pension Partnership Investment Limited which is an FCA regulated investment manager with specific expertise and regulatory permissions to provide advice on investments.

2. INVESTMENT OBJECTIVES

The Fund’s primary investment objective is to ensure that over the long term the Fund will have sufficient assets to meet all pension liabilities as they fall due.

In order to meet this overriding objective the Board maintains an investment policy so as to:

- Maximise the returns from investments whilst keeping risk within acceptable levels and ensuring liquidity requirements are at all times met;
- Contribute towards achieving and maintaining a future funding level of 100%;
- Enable employer contribution rates to be kept as stable as possible.

The Fund will use its influence as a large institutional investor to encourage responsible long-term behaviour.

3. ASSET ALLOCATION FRAMEWORK

To pay benefits over time the Fund needs to generate a rate of return that is at least equal to the actuarial discount rate. The starting point for considering asset allocation is a simple portfolio of bonds and equities. However, this basic portfolio does not maximise diversification and therefore risk adjusted return.

In order to prudently diversify sources of risk and return, the Fund allocates capital across a wide variety of different asset classes. To be added to the portfolio, asset classes are first judged for **suitability**; they have to be well understood by the Board, consistent with the Fund’s risk and return objectives; and they have to make a significant contribution to the portfolio by improving overall return and risk characteristics. In addition, the new asset classes have to be less than perfectly correlated with equities and bonds, so that the portfolio benefits from increased **diversification**. The scheme has identified a total of eight asset classes that combined form the **policy portfolio**.

The eight asset classes shown below have different exposures to economic factors (GDP growth and inflation), and combine different geographies, and currencies. In assessing suitability the Board has considered the respective return drivers, exposure to economic growth and sensitivity to inflation – each an important consideration, relative to the sensitivities of the Fund’s liabilities and managing risk.

Asset Class	Long-Term Return Drivers	Economic Growth *	Inflation *	Geography	Currency
Global Equity	- Dividend Income - EPS Growth - Change in PE	+	+/- **	Diversified	Diversified
Private Equity	- Dividend Income - EPS Growth - Change in PE	+	+/- **	Diversified	Diversified
Fixed Income	- Yield (minus credit losses) - Roll down - Change in Yield	-	-		
Alternative Credit	- Yield (minus credit losses) - Roll down - Change in Yield - Liquidity Premium	+	-	Diversified	Diversified
Property	- Rental Yield minus Capex - Rental Growth - Capital Growth	+	+/- **	Predominantly UK	Predominantly GBP
Infrastructure	- Dividend Income - EPS Growth - Change in PE	+	+	Predominantly UK	Predominantly GBP
Total Return	- Diversified	Low correlation	Low correlation	Diversified	Diversified
Cash	- Yield	+	+	Predominantly UK	Predominantly GBP

* Sensitivities shown are to positive shocks, i.e., if growth and inflation surprise on the upside.

** Property, public and private equities expected to provide partial inflation protection.

These are the eight building blocks used to create the policy portfolio. The Board have determined benchmark weights to each asset class which it believe to be best suited to meeting the long term objectives of the Fund. It has also identified tolerance ranges within which shorter term variations would be tolerated and/or actively pursued due to a combination of relative returns and investment opportunity.

The benchmark weight and tolerances are shown in the table below. The weights are to be maintained within the ranges as long as the scheme can find attractive opportunities that meet its return, risk, and cash flow requirements. In the absence of opportunities investments will not be "forced" and under/over allocations may be made to any asset class.

Asset Class	Policy Portfolio	
	Benchmark Weight	Range
Global Equities	47.5%	40%-60%
Fixed Income	2.5%	0%-15%
Private Equity	7.5%	5%-15%
Infrastructure	7.5%	5%-15%
Alternative Credit	7.5%	0%-10%
Property	10.0%	5%-15%
Total Return	15.0%	0%-20%
Cash	2.5%	0%-10%
Total	100%	

Each asset class has its own specific investment objective and within each asset class there are further diversification controls. The mandates are managed by Local Pensions Partnership Investments Ltd (LPP I), to whom the Fund has delegated investment management and implementation duties in line with the principle of asset pooling within LGPS.

Global Equities

The objective is to outperform the MSCI All Country World, net dividends reinvested, in GBP Index over the full market cycle which is considered to be at least seven years (the "Benchmark"). All equity investments are made via LPP I, by investing in underlying funds which may be managed by LPP I ("Internal Mandates"), or by external third parties ("External Mandates").

Private Equity

The objective is to outperform the MSCI World, net dividends reinvested, in GBP Index and provide investors with access to attractive private equity opportunities. All new investments will include, but not be limited to the following sectors: Buyout, Venture Capital, Growth Equity, Special Situations/Distressed and Upstream Energy.

Fixed Income

The objective is to outperform the Barclays Global Aggregate Bond Index GBP Hedged. The LPP I Pool will pursue this aim by investing in underlying funds which may be managed by LPP I ("Internal Mandates"), or by external third parties ("External Mandates") which are consistent with the Fixed Income Pool's investment objectives and restrictions.

Total Return

The LPP I total return pool seeks to gain cost effective exposure to diversifying sources of return distinct from global equity beta and bond duration. The LPP I pool will pursue this aim primarily by allocating capital to investment strategies managed by external third parties ("External Mandates").

Infrastructure

The objective is to gain cost effective, diversified exposure to global infrastructure assets located predominantly in OECD nations. These investments seek to generate a satisfactory risk adjusted return; improve diversification; provide predictable cash flows; and indirectly hedge against inflation.

Alternative Credit

The objective is to gain cost effective exposure to diverse sources of return linked to global credit markets and credit instruments. The LPP I investment pool will pursue this aim primarily by allocating capital to investment vehicles, mandates or pooled funds managed by external third parties ("External Mandates").

Property

The objective is to gain cost effective, diversified exposure to UK and international property assets that meet its investment objectives: to generate a return in excess of the benchmark; earn predictable cash flows; and provide a partial hedge against inflation. The largest exposure of the portfolio will be to traditional sectors of the UK commercial real estate market. A smaller allocation will be made to value-added and opportunistic investments.

Cash/ Liquidity

The objective is to achieve cost effective management of cash balances by allocating capital to securities or funds in appropriate markets and in relevant currencies or hedged back to relevant currencies. The benchmark for the Liquidity pool is 1 month GBP LIBOR.

The policy portfolio has a number of illiquid assets that could prove difficult to sell in a period of market turmoil. Due to the fact most of these assets generate income that can be used to pay benefits throughout the business cycle (e.g. income from infrastructure and rent payments from properties), the scheme has determined that the illiquidity premiums that are generated from holding these assets are enough compensation for the level of risk.

4. INVESTMENT GOVERNANCE

The Board is responsible for setting the higher level objectives and risk tolerances of the scheme. The Board sets in conjunction with the scheme's actuary the required rate of return needed to achieve its objectives and the risks it is willing to take. Once these parameters are established, the Board will determine the strategic asset allocation or policy portfolio that it believes has the highest probability of succeeding. The implementation of the asset allocation is delegated to an expert investment manager – Local Pension Partnership Investment Ltd (LPP I). LPFA is a founding shareholder of LPP I and maintains ongoing corporate governance controls but plays no direct role in Investment Management activities. The Board will monitor the performance of LPP I and the portfolio.

5. INVESTMENT IMPLEMENTATION

The implementation of all investments is delegated to Local Pensions Partnership Investment Ltd, an FCA authorised company. The partnership was set up by the LPFA and Lancashire County Council for the purpose of achieving economies of scale, greater internal resource and superior investment opportunities. The partnership brings the benefit of scale and expert resources beyond that which would be available to the Fund alone. This facilitates lower costs and a broader opportunity set which together facilitate improved net returns. Pooled vehicles are used wherever appropriate. Where assets are not physically pooled the management is typically pooled.

The partnership has created eight investment pools to allow access to the asset classes listed in the Asset Allocation Framework section. The investment pools are a combination of internally managed and externally managed strategies that offer an effective and efficient way of achieving asset class exposures.

The Fund also expects to benefit from scale via pooling arrangements with other funds in order to better access direct investments in areas such as infrastructure.

Some of the pools are expected to use derivatives as part of their strategies. Derivatives can reduce implementation costs, or change economic exposures. They may be used for both active and passive management strategies. The broad use of derivatives is explicitly approved the Board for both investment purposes and efficient portfolio management. Both exchange traded and over the counter derivatives may be used.

6. POOLING OF ASSETS

The Board has delegated the management of its investments to LPP I who are responsible for managing 100% of the assets of the Fund. The large majority of the Fund's assets will be transitioned into investment pooling vehicles also managed by LPP I. A small minority of assets will remain on the balance sheet of the Fund as "legacy assets". Assets will be held as legacy assets if; the costs of transitioning outweigh any potential gains, the assets have reached "harvesting period", or transitioning would have a negative impact on the scheme's investment strategy. Proceeds from assets in "harvesting period" will be reinvested through LPP asset pools.

Asset Class	LPFA Assets			Legal Structure
	Transitioned*	Legacy*	Total*	
Public Equity	35.3%	13.8%	49.1%	Authorised Collective Scheme
Private Equity	7.5%	0.7%	8.2%	Limited Partnership
Infrastructure	4.9%	0.8%	5.7%	Limited Partnership **
Property	4.1%	0.0%	4.1%	Authorised Collective Scheme **
Total Return	15.3%	0.0%	15.3%	Authorised Collective Scheme **
Alternative Credit	7.6%	0.0%	7.6%	Limited Partnership **
Fixed Income	0.0%	0.0%	0.0%	Authorised Collective Scheme **
Cash	9.9%	0.0%	9.9%	Authorised Collective Scheme
Total	84.7%	15.3%	100.0%	

Information correct as at 30th June 2016.

* estimated figures ** subject to change

7. LGPS REFORM

The Fund has selected Local Pensions Partnership Limited (LPP) and its subsidiary LPP I to facilitate investment pooling. LPP has communicated its structure to DCLG via its response to the July 2016 consultation. This structure and associated business plan is consistent with the criteria contained within the November guidance.

8. RISK MANAGEMENT

The gradual reduction of the funding deficit is a core goal for the Board. Funding deficit is influenced by both assets and liabilities and for this reason the Board adopt an Asset and Liability Management approach which includes the use of liability hedging strategies. The Board review the hedging policy on an ongoing basis and may seek to hedge inflation and/or interest rate exposure using a combination of physical and derivative instruments.

Diversification is a very important risk management tool. As described in the section on Asset Allocation, the scheme will seek to maintain a diversified exposure to several different asset classes, geographies, and currencies. The Board expect this to provide (at least) two levels of protection: first, in periods of market turmoil some assets will preserve capital better than others, allowing the portfolio to better withstand a shock. Second, in periods of rising markets, some assets will do better than others, and since the Board do not know with certainty which ones will do best, it is better to diversify.

Another line of defence at the scheme level is to examine how the portfolio would perform under different scenarios including stress scenarios. The objective is to ensure that the losses that the portfolio endures will not cause future contributions to increase. When setting Asset Allocation the Board have considered different stress scenarios and possible outcomes.

The asset class pools described in the implementation section are also subject to a number of constraints to allow for intra-asset class diversification, including sector, country, manager, and maximum exposure to a single asset.

9. PERFORMANCE MEASUREMENT

Fund performance is measured at a number of different levels. The objective of the Fund is to outperform the actuarial discount rate. The policy portfolio is selected by the Board with advice from LPP I, the delegated investment manager, and is expected to generate returns above the discount rate.

The performance of the pooling arrangements is monitored via regular reporting and through periodic meetings. Performance for LPP I is measured against the policy portfolio. LPP I seeks to outperform the policy portfolio on a risk adjusted basis by tilting asset weights in an opportunistic manner, via active sub-asset class selection, selecting the best stocks/managers for each of the pools, and by implementing investments in a low cost manner. Performance for the investment pools is measured against widely used and transparent benchmarks.

Where performance falls short of expectations the Board will identify the cause of this underperformance and will respond appropriately either to alter its policy portfolio (where asset allocation is the underlying cause) or to require changes to the management of the pooling vehicles (where management skill within LPP I is the underlying cause). This latter intervention is enabled through the Board's ongoing governance rights within LPP I via its shareholding in Local Pension Partnership Limited, LPP I's parent company.

10. ESG POLICY

The Fund is committed to being a long term responsible investor. The Fund complies with and follows the principles of both the UK Stewardship Code and to the UN-backed Principles of Responsible Investment.

Responsible Investment is an investment approach which recognises the significance of the long-term health and stability of the market as a whole and encompasses

- the integration of material ESG factors within investment analysis and decision-making
- the active use of ownership rights in order to protect and enhance shareholder value over the long term – primarily through voting and engagement.

The objective of responsible investment is to decrease investor risk and improve risk-adjusted returns. Responsible investment principles are at the foundation of the Fund's approach to stewardship and underpin the Fund's fulfilment of its fiduciary duty to scheme beneficiaries.

ESG integration and the active use of ownership influence are integral to the investment management services provided by LPP I, which are delivered in accordance with an LPP I Responsible Investment Policy. It is an LPP I RI belief that ESG factors are relevant at every stage in the investment cycle - within investment strategy, investment selection and within



the stewardship of assets in ownership. As part of a prudent approach which applies care, skill and diligence LPP I procedures ensure that ESG issues are routinely considered as part investment analysis, are incorporated into the due diligence leading to investment selection and continue to be monitored and reviewed as part of the active ownership of assets under management.

The approach to incorporating ESG factors is to establish the type and materiality of relevant issues on a case by case basis, whilst taking account of global norms, rather than to apply artificial exclusions through negative screening. ESG factors are considered over the time horizon within which specific investments are likely to be held, in order to clarify the context that risks and returns operate within and assist the evaluation of investment risks and opportunities.

The Fund shall invest on the basis on financial risk and return having considered a full range of factors contributing to financial risk including both those detailed above and relevant social factors to the extent these indirectly or directly impact on financial risk and return.

11. EXERCISING THE RIGHTS OF OWNERSHIP

The Fund recognises that encouraging the highest standards of corporate governance and promoting corporate responsibility by investee companies protects the financial interests of pension fund members over the long term. The Fund's commitment to actively exercising the ownership rights attached to its investments, reflects the Fund's conviction that responsible asset owners should maintain oversight of the way in which the enterprises they invest in are managed and how their activities impact upon customers, clients, employees, stakeholders, and wider society.

The routes for exercising ownership influence vary across asset types and a range of activities are undertaken on the Fund's behalf by LPP I, including direct representation on company boards, presence on investor & advisory committees and participation in partnerships and collaborations with other investors. In the case of listed equities the most direct form of ownership influence comes through shareholder voting and engagement.

12. VOTING

Through the investments managed by LPP I, the Fund has ownership interests in listed companies across the globe. To ensure effective and consistent use of the voting rights attached to these assets LPP I, works with an external provider of governance and proxy voting services.

Voting is undertaken centrally rather than being delegated to individual managers and is in line with an agreed voting policy which promotes risk mitigation and long-term shareholder value creation by supporting responsible global corporate governance practices. The policy is reviewed and updated on an annual basis to reflect emerging issues and trends.

A quarterly report on voting activity is available from the LPP website which is signposted via a link from the LPFA website.



12. ENGAGEMENT

The Fund's approach to engagement recognises the importance of working in partnership to magnify the voice and maximise the influence of investors as owners. The Fund appreciates that to gain the attention of companies in addressing governance concerns, it needs to join with other investors sharing similar concerns. It does this primarily through:

- Membership of representative bodies including the Local Authority Pension Fund Forum (LAPFF) and the Pensions and Lifetime Savings Association (PLSA);
- Giving support to shareholder resolutions where these reflect concerns which are shared and represent the Fund interests;
- Joining wider lobbying activities when appropriate opportunities arise.

The Fund complies with the UK Stewardship Code and a statement of compliance which explains the arrangements which support its commitment to each of the seven principles is displayed on the Fund's website.