

SUPERANNUATION ARRANGEMENTS OF THE  
UNIVERSITY OF LONDON

# Statement of Investment Principles

*The Trustee's Policy  
on Investment Matters*

April 2010

# STATEMENT OF INVESTMENT PRINCIPLES

## 1. Introduction

SAUL is an independently managed and invested pension Scheme for the non-academic staff of some 50 colleges and institutions which have links to higher education in the south-east of England. These include most of the colleges of the University of London, Imperial College and the University of Kent.

Twelve Directors make up the Board of the SAUL Trustee Company which is the Trustee of SAUL and runs the Scheme. The Trustee is responsible for the investment of SAUL's assets and its investment powers are set out within the Scheme's governing documentation and relevant legislation. The Trustee appoints the members of the SAUL Investment Committee which reports to the Trustee and manages all matters relating to the investment of the assets of the Scheme with the exception of the overall strategic asset allocation. The Investment Committee has formal Terms of Reference and Delegated Authority agreed by the Board.

The Trustee has drawn up a set of investment aims, which help the Trustee to plan the strategy for managing the Scheme's assets. The Trustee is responsible for the policy covering investment aims and strategy, and this is set out in detail in Section Three of this Statement. The Trustee will refer to this Statement when making investment decisions to ensure that they are consistent with these principles as far as reasonably practicable.

The Trustee delegates day-to-day management of the assets to professional investment managers. The policies that affect day-to-day management are set out in Section Four of this Statement.

The Trustee has adopted and will review regularly a policy on Corporate Governance and voting issues. The Trustee expects the managers to follow the voting policy unless to do so would restrict the investment managers' ability to invest in the best financial interests of the Scheme.

In preparing this Statement of Investment Principles the Trustee has taken written advice from its Investment Consultant and has consulted the sponsoring employers.

## 2. Statement of Funding Principles

A major influence on investment approach is the Statement of Funding Principles introduced by the Pensions Act 2004. The Statement of Funding Principles sets out the basis on which SAUL is funded and because the investment return on the assets is a key element of the assumptions in the Statement of Funding Principles it is closely linked to this Statement.

A copy of the Statement of Funding Principles is available on request.

## 3. Investment Objectives

The Scheme builds up a fund by investing the contributions paid by members and employers. The cash and other investments are known as the "assets" of the Scheme. The Scheme needs the assets to cover payments which may be

made under the Scheme Rules to members and their families in the future. These payments are the “liabilities” of the Scheme. As more members build up service in the Scheme and their salaries rise, the liabilities of the Scheme grow.

The Actuary can calculate an estimate of the present day value for the liabilities and compare it with a current value of the assets. The comparison between assets and liabilities is called the funding level. An explanation of the Actuary’s methods and conclusions are set out in the Actuarial Valuation Report. No one can predict the exact future values of the assets or of the liabilities which means that a sensible investment management strategy will allow for various “risks”.

The Trustee’s primary investment objectives are:

### **3.1. Long-Term**

- i Keeping contribution rates for employers and members stable;
- ii Investing to produce an investment return on the portfolio that, after all investment related fees and expenses, is above the actuarial assumptions;
- iii Ensuring that the assets are sufficient to cover the ongoing liabilities of the Scheme; and
- iv Not forcing the Scheme to buy and sell investments at particular times.

As a supplement to these objectives the Trustee aims to maximise the money earned by the investments over the long-term, while at the same time limiting the level of risk.

### **3.2. Short-Term**

Over the short-term, the goal is that the growth of the investments should be equal to or better than a target level called a “return benchmark”.<sup>1</sup> The return benchmark adopted by the Trustee was developed by the Investment Consultant and is a combination of market indices and is not influenced by other UK pension funds. Section 3.5 has further details.

The SAUL benchmark was chosen because it reflects changing economic conditions which affect the value of the liabilities and therefore the level of risk which the Trustee is taking.

The Trustee believes that the strategy used will achieve the long-term and short-term goals.

### **3.3. Risk**

Because no-one can predict the future, all pension schemes are exposed to various risks. The Trustee has considered the following risks:

- i The risk that the funding level calculated on a specific basis for SAUL, which has been agreed by the Trustee, could decline;

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<sup>1</sup> Benchmarks are calculated using a formula which is based on one or more indices. Each index measures the performance of a particular asset.

- ii The risk that assets could be insufficient to cover the ongoing liabilities of the Scheme;
- iii The risk that the investment growth may not live up to the Trustee's expectations. The Trustee is aware that this risk is greater where the investment management is active, so part of SAUL's assets are managed passively. (Although the risk may be higher for active management, potential returns from active management are also higher than for passive management.);
- iv The risk that values of asset classes, and the individual investments in each asset class, may fluctuate;
- v The risk that an investment manager may not deliver the expected performance.
- vi The risk that, due to volatility in investment markets, the assets could be lower than the liabilities at the point of a formal (normally triennial) actuarial valuation.

These risks are managed (but not eliminated) through a variety of methods, including:

- i) Diversifying investments across asset classes, geographical boundaries and investment managers;
- ii) Taking a long-term view of investment markets and not being swayed by fashions and short-term events;
- iii) Holding a proportion of assets in bonds, the asset class most closely (although not perfectly) related to pension liabilities;
- iv) Regular monitoring of investment performance through in-depth discussions with the investment managers, and also through discussion and analysis from the Investment Consultant;
- v) Monthly review of the actual asset allocation against the strategic benchmark;
- vi) Provision of education and training for members of the Investment Committee and Board;
- vii) Use of an independent, qualified and experienced Investment Consultant.

### **3.4. Risk Measurement**

The Trustee measures these identified risks through a variety of means. Some are measured using information from the Scheme Actuary. Others are measured using information from the investment managers as verified independently by the Trustee's performance measurement service. The aim of the risk measurement is to ensure that appropriate risk is being taken to provide the best possible chance of achieving a long-term rate of return that, after fees, matches or exceeds the rate of increase in the value of the liabilities.

### **3.5. Long-Term Investment Strategy**

Having considered the current economic environment the Trustee takes the view that the medium to longer term future will see a lower investment return environment than that experienced in the 20 years

between 1980 and 2000. This view has been formed from advice and commentary from the Investment Consultant, supplemented by commentary provided from economists at some of the Trustee's investment managers. In addition, the Trustee takes the view that over the medium term investment returns could be more volatile than was the case between 1980 and 2000.

The Trustee also has reviewed the maturity of the Scheme. SAUL is no longer cash-flow positive, but benefits outflow will be exceeded by the expected rise in asset value in the next 20 to 30 years and retirements will not peak for approximately another 15 years. Accordingly SAUL can be considered relatively immature.

Taking this into account, together with regular analysis of the liability profile from the actuary and advice from the Investment Consultant, the Trustee has determined a strategic asset allocation.

The Trustee considers that asset classes fit into a continuum from risk-reducing to return-seeking and the appropriate mix of assets will come from this continuum. This view is reflected in the strategic asset allocation agreed by the Trustee which is to allocate 65% of the assets to return-seeking asset classes and 35% to risk-reducing asset classes.

The strategic mix of assets drives the benchmarks against which the investment managers and the whole portfolio are measured over the short-term (less than five years). These benchmarks are the relevant market indices for the asset classes that each manager is appointed to manage. Over the longer-term it is expected that the portfolio will exceed the growth in the liabilities, thus protecting the contribution rate and the funding position. The Trustee uses longer-dated Index-linked Gilts as a proxy for the liabilities when measuring the performance of the assets.

### **3.6 *Expected return on Investments***

The strategic benchmark is expected to produce a return over the long term in excess of the investment return assumed in the actuarial valuation since the actively managed assets are expected to outperform their benchmarks over the long term.

## **4. Day-to-Day Management of the Assets**

### **4.1. *Introduction***

Having established the long-term asset allocation the Trustee has identified separate investment mandates. Following advice from the Investment Consultant, Investment Managers have been carefully selected to manage these separate mandates.

### **4.2. *Main Assets***

The Trustee delegates the day-to-day management of the assets to a number of investment managers. The Trustee has taken steps to satisfy itself that the managers have the appropriate knowledge and experience to manage the Scheme's investments. The managers are

regularly monitored to ensure they are carrying out their work competently.

From time to time managers and/or mandates are changed and this is done after due consideration and the receipt of appropriate advice from the Investment Consultant.

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

The Trustee regularly reviews the suitability of the Scheme's investments including the appointed managers and the balance between active and passive management which may be adjusted from time to time. The Trustee uses a combination of active and passive management in the investment allocation, using passive management where the Trustee does not believe that it is possible, net of fees, for active managers to add value.

A list of the managers and their mandates is included in the Trustee's Annual Report & Accounts.

#### **4.3 *Tactical and Opportunistic Investments***

The Trustee recognises that on occasion there are tactical themes or opportunistic investments that, whilst of potential value to overall performance and delivery against the Trustee's investment objectives, require a different, but no less rigorous, governance model than that used for the strategic allocation. To that end, the Trustee has established, as a sub-group of the Investment Committee, a Tactical Investment Group. This Group, operating with strict risk controls and reporting on a regular basis to the Investment Committee, is empowered to identify and make recommendations to the Investment Committee for smaller, more tactical and opportunistic investments, which, by their nature, will always be between £10m and £20m in size. The size of this portfolio is limited to a maximum initial investment of £60m in total across all the investments in the Tactical Portfolio.

#### **4.4. *Rebalancing Policy***

Over time, the actual balance of assets in the Scheme will tend to move away from the strategic allocation. This will be because the performances of the various investment markets and of the investment managers will differ. The Trustee recognises this and has a policy on when and how to rebalance assets back to the strategic benchmark. Around each element of the benchmark allocation ranges have been set following the advice of the Investment Consultant.

The manager appointed to manage the passive part of the fund rebalances to the ranges appropriate to the passive element of the fund on a monthly basis. Each month the Trustee looks at the actual asset allocation against the permitted ranges and checks to see if there were movement outside the range. If there were such a movement this would be reported to the Investment Committee (or a properly authorised sub-Committee) who, with the advice of the Investment Consultant, would

decide whether or not to rebalance the assets back to the strategic allocation. If the decision were not to do so, this would be for short term tactical reasons.

#### **4.5. *Appointment of Investment Managers***

The Trustee has appointed investment managers to manage the assets. The appointment of each manager is a careful process and advice and guidance are received both verbally and in writing from the Investment Consultant at every stage.

The Investment Consultant will, following extensive research, recommend a long-list of possible managers for a particular part of the Fund, all of whom will be properly authorised to invest money by the appropriate regulatory bodies. All the proposed managers will, in the view of the Investment Consultant, have the requisite skill and experience to deliver the Trustee's expectations.

Normally, the Investment Committee will then issue a "Request for Information" to the long-listed managers. This Request for Information will be drafted by the Investment Consultant taking into account the views of the Trustee and will be a fact-finding exercise. This exercise may be supplemented by meetings between the long-listed managers and representatives of the Trustee. The Investment Committee, or a properly authorised sub-Committee together with the Investment Consultant, will review the responses and draw up a short-list of candidates who then will be interviewed by the full Investment Committee.

As part of the "Request for Information" process, all long-listed managers will be asked if they will provide an AAF01/06 Report. This report provides external assessment of the qualities of the internal controls at the Investment Manager. If the manager does not provide an AAF01/06 Report the Trustee ensures that an equivalent (such as an SAS 70 Report) is available. If the manager cannot provide assurance that it has a robust, independently verified system of internal controls then the Trustee will not appoint the manager.

At the conclusion of the selection process the Investment Committee will make a recommendation to the Trustee as to the appointment of the appropriate manager.

Appointments of managers for investments in the Tactical Portfolio may follow a different process, but one which is no less rigorous.

The appointment of the manager is a process which is completely separate from the asset allocation decision.

All managers are monitored regularly, regard being paid not only to their investment performance to date, but also to their expected future performance. In cases where the Trustee is of the view that a manager is unlikely to meet the requirements of the mandate in the future the Trustee may decide to replace that manager.

#### **4.6. Realisation of Investments**

The active investment managers are free to use their professional judgement in the timing of the purchase and sale of investments and the ease with which they can convert these to cash.

The Scheme's investment managers have responsibility for generating cash as and when it is needed to pay out benefits. The Trustee's current policy is that, when cash is needed from the investment managers for the payment of benefits, such cash is taken from investment income.

#### **4.7. Monitoring the Investment Managers**

The Investment Committee represents the Trustee in regular meetings with the investment managers to review the managers' actions. These meetings can be held either at the SAUL Trustee Company offices, or at the offices of one of the managers. The Committee considers the background against which the managers have made decisions and the reasons for the investment performance. The investment managers provide quarterly reports which are reviewed by the Investment Committee on behalf of the Trustee.

The Trustee has responsibility for monitoring the investment managers and employs the Investment Consultant as investment consultants to help with this. In addition, an independent performance measurement service provides quarterly and annual reports that measure the performance of the investment managers against individual benchmarks together with the performance of the total Fund, also on a quarterly and annual basis.

#### **4.8. Transaction Costs**

In line with the recommendations in the Myners' Review of Institutional Investment Decision Making (See 8. below), the Trustee has entered into a dialogue with the investment managers on the costs incurred in transacting the purchase and sale of investments on SAUL's behalf. All the managers have provided information on transaction costs and the Trustee is content that all the managers keep these costs (including market impact) to a minimum.

The Trustee will keep transaction costs under review, accepting that higher costs result in lowered performance which, of itself, is an incentive for managers to keep their costs to a minimum.

In addition the Trustee uses Mercer Sentinel, an analysis service provided by the Investment Consultant. This compares the costs of custodian services, foreign exchange and trading in order to ensure that the Trustee receives best value for money.

#### **4.9. Additional Assets**

The Trustee holds, on behalf of the Scheme, all the issued shares of STC Pension Management Ltd, a small company established for the purpose of offering third party administration services to pension funds other than those that participate in SAUL. The Trustee believes that the

maximum investment is unlikely to represent more than 0.1% of the total assets of SAUL.

#### **4.10. Cash Balances**

Working cash balances are held separately and are managed by the SAUL Trustee Company office. The cash is invested both in the overnight money markets and in pooled money market funds in order to ensure that the best wholesale money market interest rates available are obtained.

## **5. Performance Measurement**

The Trustee, in line with the recommendations in the Myners' Review, measures the performance of itself, the Investment Committee, the Investment Consultant and the individual managers. As stated in Section 4. above, the Trustee employs an independent performance measurement service to help in the process of measuring the performances of the managers who are measured against benchmarks over rolling three-year or five-year periods.

Results of the measurement of the Trustee are reported in the Trustee's Annual Report & Accounts, copies of which are available on request. The Trustee measures SAUL's performance against the long-term objectives, and against the benchmark which is a composite of market indices and is not related to other pension schemes.

## **6. Social, Environmental & Ethical Considerations**

In common with most pension funds, the Trustee has a legal obligation to treat the financial interests of the members and beneficiaries as paramount. The Trustee also has a legal obligation to ensure proper diversification of investments and to act prudently. Therefore, unlike retail funds or pension funds linked to organisations with specific social objectives, the Trustee cannot screen out individual companies, much less entire sectors, for non-financial reasons.

The Trustee's investment objectives are set out in Section 3. The aim of these objectives is, in summary, to ensure that the fund has sufficient assets to meet the cost of the promised benefits. It is the objectives which drive the asset allocation policy and other strategic decisions. In implementing the objectives the Trustee uses the investment powers for the purpose of maximising the money earned having due regard to social, environmental and ethical considerations. Reference to these considerations is made also in the Trustee's Corporate Governance Policy. This Policy is given to all Investment Managers. A copy is available on request.

## **7. Exercise of Shareholder Rights**

The Trustee has instructed the investment managers to exercise voting and other shareholder rights in a manner consistent with the investment objectives. The investment managers are instructed to vote all shares held on behalf of SAUL. This applies to overseas investments, unless to do so would seriously

restrict the investment managers' freedom to invest in the best financial interests of the Scheme.

## **8. Code of Practice for Institutional Investment Decision-Making**

SAUL complies with the 6 points of the Code of Practice for Institutional Investment Decision-Making. A report on performance against the Code is included in the Trustee's Annual Report & Accounts.

## **9. Compliance with this Statement**

The Trustee will supply the investment managers with a copy of this Statement and will advise them promptly of any material change to it. The Trustee will check each year that the managers have acted in accordance with the Statement. Each investment manager has a duty under the Pensions Act 1995 to operate in line with the Statement as far as is reasonably practicable.

## **10. Review of this Statement**

The Trustee will review the Statement of Investment Principles in response to any material changes to any aspects of the Scheme. These could include changes to liabilities or finances. Any change in the attitude to risk of the Trustee or of the Scheme's sponsoring employers also could trigger a review, since it could have a bearing on the stated policy.

At the very least, the Trustee will review the Statement every year. In accordance with its statutory obligations the Trustee takes written investment advice and will consult the employers who sponsor the Scheme as part of that review process should changes to this Statement be proposed.

If you would like more information about the pension scheme, please write to:

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