Pension Protection Fund

Statement of Investment Principles

December 2016

Contents

This Statement of Investment Principles is produced to meet the requirements of the Pensions Act 2004 and to reflect the Government's voluntary code of conduct for Institutional Investment in the UK ("the Myners Principles"). The Board also complies with the requirements to maintain and take advice on the Statement and with the disclosure requirements.

1 Introduction

1.1 The Board ('the Board') of the Pension Protection Fund ("the Fund") has prepared this Statement of Investment Principles ("the Statement") in accordance with Section 114 of the Pensions Act 2004 ("the Act") and the Pension Protection Fund (Statement of Investment Principles) Regulations 2005 ("the Regulations")[1].

1.2 This written statement outlines the principles and policies governing determinations about investments made by or on behalf of the Board in the management of the Fund's assets. This Statement also reflects the Myners principles for institutional investment decision-making.

1.3 This Statement will be reviewed annually or when there is, or the Board anticipates that there might be, a significant change in relation to any matter contained in this Statement or to any of the matters which this Statement is required to cover by the Regulations.

1.4 This Statement is specifically concerned with the investment of the:-

- accumulated levy contributions paid into the Fund.
- assets transferred into the Fund from eligible pension schemes.

Although this Statement does not apply to the assets of schemes in an Assessment Period (as defined in Section 132 of the Act), the Board, where appropriate, will work with the trustees of such schemes to encourage co-ordination with the investment strategy of the Board and to minimise the costs of transitions.

This Statement covers the Fund as defined in Section 114 of the Act. It does not cover the Fraud Compensation Fund for which the Board is also responsible. A separate Statement of Investment Principles is in place for the Fraud Compensation Fund.

1.5 This Statement will be published and made available upon request.

1 Statutory Instrument 2005 No 675

2 Governance of the Pension Protection Fund

2.1 Investment powers and compliance with the Pensions Act 2004

2.1.1 Section 113 of the Act provides that the Board may invest for the purpose of the prudent management of its financial affairs. When exercising its power to invest the Board will consider the interests of current and potential beneficiaries of the Fund and the interests of stakeholders affected by the rate of the levies.

2.1.2 The Board is responsible for the governance and investment of the Fund's assets. The Board is satisfied that it has sufficient expertise, information and resources to carry out its role effectively. Several members of the Board have significant working experience in the investment industry. In addition, the Board has appointed an independent investment adviser to the Investment Committee and has access to in-house investment expertise. Attached in Annex 2 is a breakdown of the governance structure and the associated responsibilities.

2.1.3 In preparing this Statement, the Board considered written advice received from the Fund's investment adviser, Mercer Limited, who is a firm that the Board is satisfied has arrangements in place to secure that any individual who will provide advice to the Board on the preparation or, as the case may be, revision of the Statement will, at the time he provides that advice, have the appropriate knowledge and experience for providing that advice. The written advice considers the matters prescribed under section 114 of the Act and the Pension Protection Fund (Statement of Investment Principles) Regulations 2005. Actuarial advice relating to the assets and liabilities of the Fund is sought from the Board's Chief Actuary.

2.2 Investment Committee and Asset and Liability Committee

2.2.1 The Fund's funding objective and the appetite for investment risk are the responsibility of the Board.

2.2.2 The Board has established an Investment Committee to set an appropriate mix of assets consistent with the Board's funding objective and appetite for risk, and provide oversight of its implementation. The Investment Committee is accountable to the Board.

2.2.3 The Chief Executive has also established an executive committee, the Asset and Liability Committee (ALCO), to oversee the day to day investment activities of the Fund.

2.3 Day to day fund management

2.3.1 The day to day fund management of the assets is performed both by external professional fund managers, (each of which is authorised and regulated by the Financial Conduct Authority or a similar local regulatory authority as required), and the Chief Investment Officer, with authority to delegate to an in-house team of investment professionals, appointed in accordance with Section 113 of the Act. The Investment Committee is satisfied that the appointed external and in-house fund managers have the appropriate knowledge and experience to carry out their role in accordance with section 113(6) of the Act.

2.3.2 The Investment Committee oversees the appointment, monitoring, funding, termination and performance of professional fund managers. ALCO will be responsible for confirmation of the selection, funding and termination of managers and monitoring performance.

3 Funding Objective

3.1 The Board's primary objective is to have sufficient funds to pay compensation to the members of eligible defined benefit occupational pension schemes or defined benefit elements of hybrid occupational pension schemes, where these schemes have been transferred into the Fund.

3.2 In setting a funding objective, the Board envisages the Fund becoming, over a period of years, sufficiently mature such that the profile of liabilities is dominated by members who are receiving compensation.

3.3 The Board will target the Fund towards reaching an appropriate level of funding at that time, to be achieved by adopting a suitable low risk investment strategy, setting a levy on eligible schemes, and the prudent management of the Fund's assets.

3.4 This objective is to be met by the Fund achieving a balance between protecting and securing the compensation payments for current members of the Fund and of schemes undergoing an assessment period, whilst setting a fair and proportionate levy for eligible schemes that are not part of the Fund. Specifically, the investment strategy is designed to hedge current estimates of the Board's asset / liability mismatch risks and provide some outperformance over the estimated liabilities. Any outperformance should contribute to the long-term sustainability of the Fund and therefore reduce the burden on the levy payer. The Board regards a long term target investment return of 1.8% pa in excess of the liabilities to be consistent with these objectives.

3.5 The nature and timing of these actual and potential liabilities are uncertain and will vary as schemes transfer to the Fund. Assets will be set to match current estimates of the Board's liabilities and may be adjusted as the pattern of liabilities evolves over time.

4 Risk measurement and management

4.1 The Board targets a level of strategic investment risk equivalent to a tracking error net of illiquidity risk of 3% to 4.5% pa against the liabilities and an overall tracking error limit of 3.5% to 5% pa including illiquidity risk. The asset and liability modelling assumptions that underlie these measures are set by the Investment Committee of the Board.

4.2 The Board will assess and consider the following risks on an ongoing basis:

Asset/liability mis-match risks

- **"Basis risk"** - This risk arises where the Fund's liabilities cannot be perfectly matched. The Board manages this risk by defining a Replicating Portfolio, which is the portfolio of assets that most closely matches the expected liability cash flows. The Board then seeks to match assets as closely as possible against the Replicating Portfolio. The risk is further controlled by optimising the construction of the Replicating Portfolio, monitoring deviations and recalibrating where appropriate.
- **"Strategic investment risk"** - This is the risk arising from the failure of the selected long-term investment strategy to deliver the level of expected return or risk characteristics necessary to meet the Board's objectives. The Board manages this risk by setting appropriate long and short-term risk measures and limits. These are monitored regularly; if the level of observed or experienced risk is inconsistent with these limits the investment strategy will be reviewed.
- **"Illiquidity risk"** – This risk relates to the inability of assets to be sold quickly or sold at fair market values. The Board has set a prudent limit for this risk and monitors the Fund's exposure regularly using a measure that is consistent with that of insurance regulatory regimes.
- **"Tactical investment risk"** - This risk arises when the asset allocation is moved intentionally away from the allocation in the SIP based on decisions taken by the Fund's own internal team. This may occur where the team takes a view that in the short-term such an allocation can improve the risk-adjusted return of the Fund. However

it is possible that these positions may make losses, or may (because of their scale) distort the strategy of the Fund. The Board mitigates this risk by limiting the list of allowable instruments and asset classes (as set out in Section 6.2.3 and Annex 1 of this Statement), limiting the level of individual and aggregate risk of such positions and by monitoring the level of risk and performance throughout the period of deviation.

- **"Currency risk"** – This is the risk of market loss as a result of adverse movements in foreign exchange rates. The Board has determined a target currency hedge ratio for each asset class and will aim to limit deviations from these. Additionally, some fund managers may take currency positions with a view to improving the risk-adjusted return in the short-term. The Board limits this risk and monitors the aggregate of these positions.
- **"Longevity risk"** – This is the risk that members of the Fund live longer than expected and this leads to greater compensation payments being made from the Fund. The Board and its advisers will monitor the Fund's own mortality experience and monitor mortality trends and the likely outlook for future experience. Sensitivity testing on the mortality assumptions will be carried out to determine the impact of changes in the assumptions. The Board is prepared to hedge longevity risk if it feels that this risk has become significant and hedging costs are reasonable.

Other risks

- **"Credit risk"** – This is the risk of default by issuers of financial assets and the risk that the value of these assets may depreciate as a result of an increase in the overall level of perceived credit risk in the market. The Board controls credit risk exposure by imposing limits on the amount and type of credit assets that the Fund can hold.
- **"Concentration risk"** – This is the risk that the Fund has excessive exposure to a single institution or institutions that share a common risk factor, for example by operating in the same industry. The Board controls this risk by ensuring that the spread of assets, the fund managers' policies on investing in individual securities and the Board's investment guidelines to fund managers provide adequate diversification of investments.

- **"Counterparty risk"** - This risk arises when the Fund (or a fund manager appointed by the Board) enters a financial contract with a third party which then fails, probably through default, to fulfil its obligations. The Board controls this risk by setting an appropriately high minimum credit rating of counterparties it will transact with and limiting the exposure to any single counterparty. The Board requires collateral from counterparties to financial contracts to mitigate the loss in the event they fail to fulfil their obligations under the contracts. Investment Management Agreements with fund managers similarly contain provisions to limit counterparty risk to the Fund. The Board, in-house investment team and its advisors monitor and manage the aggregate exposure of the Fund to each counterparty.
- **"Financing Liquidity risk"** – This is the risk of exhausting liquid assets and therefore being unable to meet immediate liabilities. These liabilities include cash payments and margin calls relating to derivative transactions. Sufficient liquidity is maintained such that the probability of this risk occurring is very low. The Board and its in-house investment team carry out appropriate stress testing analysis, monitor the level of liquidity against strict limits, and will take pre-emptive actions to improve liquidity if necessary.
- **"Pipeline risks"** –These risks arise from Schemes in Assessment (SIA). They include the market (i.e. mis-matching) risk associated with investments of SIA, and the risk that incorrect data regarding the assets and liabilities of SIA leads to inaccurate hedging decisions made by the Fund. To control these risks, the Fund monitors the investments of SIA and liaises with the trustees of SIA regarding their investment policy. The Board may exercise its power of direction if necessary (see Section 5.3). The quality of the data of SIA will also be monitored.
- **"Investment operational risk"** – This is the risk of loss resulting from inadequate or failed internal processes, people or systems and external events in relation to internal or external operational risk. This includes risk arising from the custody or transfer of assets, either internally or from schemes entering the Fund. The Board manages these risks by ensuring processes and procedures are robust, documented and operated by trained individuals. Systems are appropriately tested and appropriate business continuity plans are in place. The custodian is subject to ongoing review.

- **"Fund manager risk"** – This is the risk that a fund manager makes excessive or persistent losses, or does not perform in a way consistent with its return target. This risk is mitigated through a robust manager selection and monitoring process, and through manager diversification. Upon appointment the Board will set a performance benchmark and tracking error expectations and limits. The Board will also assess and monitor its fund managers against a range of qualitative factors which it believes support successful fund management. These factors are monitored on a regular basis as part of the manager oversight process.
- **"Valuation risk"** – This is the risk that assets are mis-valued, in turn resulting in inappropriate investment decisions or inferences – for example, a mis-allocation of assets, or the mis-statement of the funding level of the Fund. This risk is mitigated through a valuation governance framework that defines the pricing principles, controls, sensitivities and stress tests appropriate to each asset class, together with monitoring processes for them.
- **"Market risk"** – The risk of experiencing excessive or persistent losses due to factors that affect the overall performance of the financial markets. This risk is mitigated through putting in place a diversified investment strategy across a range of asset classes, geographical regions and market sectors.

All of these risks are a potential threat to the achievement of the objective to target an appropriate funding level. These risks are monitored on a regular basis through the Asset and Liability Committee, with periodic review by the Investment Committee.

5 Investment strategy

5.1 The Board regards the selection of asset classes as the decision which has most influence on its ability to achieve its investment objectives.

5.2 Establishing the strategic asset allocation

5.2.1 The strategic asset allocation is set by taking into account the nature and timing of both actual and potential future liabilities, which are sensitive to interest rates, inflation, mortality and other financial and demographic factors. It is also set having regard to the Board's funding objectives. To meet these objectives the Board has set an investment return target, and risk appetite consistent with the Board's low risk investment philosophy. These are laid out below.

5.2.2 The Board targets a long term investment return of 1.8% pa in excess of the liabilities.

5.2.3 The Board targets a level of strategic investment risk equivalent to a tracking error net of illiquidity risk of 3% to 4.5% pa against the liabilities.

The asset allocation is split into:

1 Liability hedging assets – interest-bearing assets and derivatives that closely match the liability sensitivities to nominal and real interest rates. A well-matched position also contributes to reducing the level of correlation between the Fund's assets and liabilities relative to those of a standard UK defined benefit scheme, typically exposed to the risk of a decline in long term interest rates, or increase in inflation expectations.

2 Return-seeking assets – a diversified portfolio of assets which, over the long-term, is expected to generate additional return relative to the liabilities, avoiding unrewarded risks where possible.

3 Hybrid assets –assets which have a dual purpose. They have stable defined cash flows which can be incorporated into the liability hedge but also have excess return characteristics which contribute to the investment return target.

5.2.4 The asset classes which form the basis of the three asset allocation categories above are:

Liability hedging assets

UK interest-bearing assets, annuity contracts and derivatives that closely match the liability sensitivities to nominal and real interest rates. These are expected to reduce the Fund's exposure to interest rate and inflation and potentially longevity risks.

Return-seeking assets

- Global bonds of high credit quality, including global sovereign debt;
- Global credit instruments including investment grade and sub-investment grade corporate bonds, asset-backed securities and emerging market debt;
- Publicly quoted equities;
- Alternative credit;
- Private equity;
- Property;
- Farmland and timberland;
- Infrastructure equity; and
- Strategies aiming to provide an absolute investment return.

Hybrid assets

Return-seeking assets which are intended to be held to maturity and exhibit some interest rate and/or inflation hedging characteristics such as: sterling index-linked corporate bonds, long-dated corporate bonds and loans, private placements of bonds, social housing, structured notes, property debt, infrastructure debt, project finance debts.

The currency exposure of non-sterling denominated assets will be hedged back to sterling where appropriate.

5.2.5 The strategic allocation to Cash and Bonds (58%) and Hybrid assets (12.5%) reflects the Board's low risk appetite.

5.2.6 At any given time a minimum level of assets of sufficient liquidity and quality will be held to ensure the Fund is able to satisfy collateral or margin calls which may arise as a result of the derivatives positions it holds.

5.2.7 Alongside the strategic asset allocation, the Board also permits tactical investment views to be taken, either to enhance return, or to control risk. The combination of the strategic asset allocation and any tactical positions taken must operate within the range of investment risk targeted by the Board.

5.2.8 Asset protection, or hedging, strategies may also be employed, as appropriate, to mitigate the risk of a fall in assets against the liabilities.

5.2.9 The performance of the Fund is measured against the liability benchmark. This benchmark will change periodically as a result of the Board accepting the legal obligation to pay compensation to members of eligible pension schemes.

5.2.10 The Board will primarily use a combination of derivatives (interest rate swaps, inflation swaps and longevity swaps) and UK bonds (conventional and inflation-linked) to adjust assets to better match the liability profile. This is to control the interest rate, inflation and longevity aspects of asset/liability mis-match risks within the tolerance levels set by the Board. Additionally hybrid assets will also be used to help hedge the liabilities. The regular adjustment of assets to the sensitivities to real and nominal interest rates is undertaken by external and in-house specialist fund manager(s) using money market instruments, bonds and derivatives.

5.2.11 A period of implementation is scheduled for the transition to the strategic asset allocation. Subject to the availability of suitable assets it is expected that the transition will be complete by June 2017.

5.2.12 The strategic asset allocation will be reviewed annually by the Investment Committee. An earlier review may be conducted in the event of any significant change in capital markets, the liabilities of the Fund, or governing legislation.

5.3 Schemes in Assessment

5.3.1 The Board and the in-house investment team will also monitor the investment strategies and liabilities of pension schemes in assessment and consider whether and how the investment risks associated with these schemes might be mitigated within the investment strategy of the Fund.

5.3.2 Specifically, the Board will:

- Engage, where appropriate, with the trustees of schemes entering an assessment period to encourage co-ordination with the investment strategy of the Board and to minimise the costs of transitions.
- Monitor the asset allocation of schemes in assessment and, where necessary, adjust the asset allocation of the Fund to compensate for any imbalance caused by these schemes.
- Consider the use of its program of interest rate and inflation hedging to mitigate the residual risks not covered by the investment strategies of schemes in assessment. The Board will control these risks by monitoring their key characteristics, setting appropriate tolerances and taking corrective action when these tolerances are exceeded.

The Board also has power to make a direction, under Section 134 of the Act, to the trustees of a scheme in assessment with a view to ensuring that the scheme's protected liabilities do not exceed its assets or, if they do, to keep the excess to a minimum as this poses a risk to the Fund.

The Board is also able to make a loan to a scheme in assessment under Section 139 of the Act where the trustees of such a scheme are unable to pay benefits to the members as they fall due.

5.4 Rebalancing policy and cash flow

5.4.1 The Board is satisfied that, to the extent required by its Financing Liquidity risk policy, the mandates awarded to the fund managers mean that sufficient assets held will be readily realisable to provide cash to meet payments by the Fund.

5.4.2 To assist with cash flow management the Board also has the power to undertake borrowing, with a ceiling of £25m.

6 Day to day investment management of the assets

6.1 Fund management

6.1.1 For the management of the portfolios, the Board employs the services of investment experts as its external and internal fund managers and has specified investment guidelines and instructions concerning various types or categories of investment decisions. The fund managers make their trading decisions independently of the Board. The external fund managers are selected by a competitive tender process.

6.1.2 The fund managers are set a specific benchmark and performance objective by the Board. As a way of limiting the extent to which fund managers may deviate from their benchmark, the Board agrees tracking error ranges with the fund managers for their portfolios. Fund manager performance and risk is monitored each quarter by the Asset and Liability Committee. Material or unexpected deviations may result in a formal review by the Investment Committee.

6.2 Investment performance benchmarks

6.2.1 The overall Pension Protection Fund benchmark is a notional combination of zero coupon fixed interest instruments and zero coupon inflation-linked instruments that is designed to replicate the expected liability cash flows. It has been determined taking into account the liabilities of the transferred schemes and especially their sensitivity to real and nominal interest rates. This benchmark portfolio will change over time with future transfers of pension schemes into the Fund.

6.22 In order to judge the success of any tactical or hedging positions, and the performance of the fund managers, the investment performance of the Fund will also be judged against a composite benchmark calculated with reference to fixed asset allocations to defined Permitted Asset Classes, with performance assumed to follow a benchmark relevant to that asset class. More detail on what constitutes Permitted Asset Classes is included in Annex 1.

6.2.3 The Board will monitor the Fund's transition to the targeted strategic asset allocation over the period of implementation. The Fund will comprise a portfolio constructed from the Permitted Asset Classes, including interest-bearing assets and derivatives that closely match the liability sensitivities to nominal and real interest rates, and assets allocated as per the following table:-

Permitted Asset Class	Strategic Allocation	Asset Benchmark Index
Liability hedging instruments - Cash - UK conventional and index-linked Gilts - Interest rates and inflation swaps - UK Gilt repurchase agreements - Annuity Contracts	40%	Liability benchmark
Return-seeking assets - Global Government Bonds - Global Aggregate Bonds (including global government, government-related, corporate and securitized debt from developed and emerging market issuers of investment grade category) Developed and emerging markets debts of sub-investment grade category. - Public Equity Alternatives (including property, private equity, alternative credit, infrastructure equity, farmland and timberland, absolute return strategies)	47.5%	JP Morgan Government Bond Index Barclays Global Aggregate Bond Suitable indices will be specified for particular credit market sub-sectors Absolute return on total return All World Minimum Variance Index will vary according to the asset class
Hybrid assets (assets with return-seeking and liability hedging characteristics)	12.5%	Will vary according to the asset class

6.2.4 For the purpose of judging performance, particularly where an asset class is liquid and readily traded, the corresponding performance index will be used. Where no market index or generally accepted benchmark is available, the Investment Committee will define an appropriate performance benchmark.

6.2.5 Any tactical or hedging position taken must be expressed using Permitted Asset Classes or their derivative instruments, and within strictly defined limits set by the Investment Committee.

6.2.6 The Fund will be rebalanced regularly taking into account the need to minimise both transaction costs and risks associated with deviation from this target asset allocation. Tolerance ranges for deviation from the strategic asset allocation (set out in the table above) have been set by the Board to allow flexibility.

6.2.7 Mandates for each fund manager will be agreed prior to their appointment. Strategies relating to the control of transaction costs and soft commission will be specified in these mandates.

6.3 Fund manager fees

6.3.1 The Board will pay such fees and expenses as are negotiated with fund managers from the Fund in accordance with the Pension Protection Fund (Prescribed Payments) Regulations 2008, as amended[2].

6.3.2 The fund managers are currently remunerated by an ad valorem fee based on the level of assets under management and, in some cases, a performance-related fee based on out-performance over a specific benchmark or target.

6.3.3 The costs of management and transactions will be reviewed from time to time, and if appropriate, renegotiated.

2 Statutory Instrument 2011 No 671

7 Day to day custody of the assets

7.1.1 The Board has appointed a custodian with regard to the safekeeping of the assets in the Fund and other investment administrative requirements.

7.1.2 The Fund may participate in securities lending within limits set by the Board.

7.2 Performance

7.2.1 The Asset and Liability Committee will consider from time to time, and at least annually, the performance of the custodian according to specifically agreed key performance indicators.

7.3 Custody fees

7.3.1 The Board will pay such fees and expenses as are negotiated with the custodian from the Fund in accordance with the Pension Protection Fund (Prescribed Payments) Regulations 2008, as amended.

7.3.2 The costs of management and transactions will be reviewed annually and if necessary renegotiated.

8 Transition of assets to the Fund

8.1 The Board recognises that the asset allocation of eligible pension schemes may not reflect the Board's strategic asset allocation but would expect to manage the transition of those assets into the Fund periodically to be consistent with the investment objectives in 3.1. The Board will use a combination of transition managers or appointed passive managers to ensure that the costs and risks of transition are minimised.

8.2 The Board will consider the timing, liquidity and cost of transition of assets of transferring schemes that do not match the asset strategy of the Board. The Board will merge these assets into the Fund at the time it deems most appropriate and may hold up to 2.5% of total assets of the Fund in asset classes which do not form part of the Permitted Asset Classes. The Board may also retain without limit annuity contracts held by transferring schemes to meet specific liabilities.

9 Responsible Investment and corporate governance

9.1 The Board's primary concern, in setting its investment strategy, is to act in the best financial interests of the Fund and its beneficiaries, seeking the best return that is consistent with a prudent and appropriate level of risk.

9.2 The Board believes that in order to fulfil this commitment and to protect and enhance the value of the Fund's investments over the long-term, it must act as a responsible and vigilant asset owner and market participant.

9.3 The Board further believes that environmental, social and governance (ESG) factors can have an impact on the long-term performance of its investments, and that the management of ESG risks and exploitation of ESG opportunities, particularly for a portfolio-wide issue like climate change, can add value to its portfolio.

9.4 The Board is a signatory of the UN Principles of Responsible Investment (UN PRI), a set of best practice principles on Responsible Investment (RI). The Board intends to use these Principles as a benchmark with which to guide its own approach to RI, and in doing so will seek to apply RI principles across all the assets in which it invests.

9.5 The Board defines environmental, social and governance (ESG) factors as the interaction of its investments with:

- The physical environment (environmental);
- Communities, workforces, wider society and economies (social);
- The governance structures of the organisations and markets we invest in, as well as of our agents (governance, including corporate governance).

9.6 The Board will integrate the consideration of ESG issues across all asset classes and markets in which it invests. In particular the Board, or its agents on its behalf, will exercise its ownership rights, including voting rights, in order to safeguard sustainable returns in the long-term.

9.7 The Board expects its fund managers, where appropriate, to have integrated ESG factors as part of their investment analysis and decision-making process. Appropriate weight will be given to ESG factors in the appointment of fund managers. The Board will hold fund managers to account in this regard as part of its regular monitoring process.

9.8 In line with its commitment to transparency, the Board will report to its stakeholders on its responsible investment activities.

10 Compliance with this statement

10.1 The Investment Committee will monitor compliance with this Statement annually. The Investment team and Risk Department will obtain written confirmation from the fund managers that they have complied with this Statement as supplied to them and advise the fund managers promptly and in writing of any material change to this Statement.

10.2 The National Audit Office will audit and monitor compliance as part of its annual review of the Fund's accounts and statement of internal control.

Annex 1
Permitted Asset Classes

The assets of the Fund will be invested in a portfolio taken from the following list of Permitted Asset Classes which are as follows (all global unless specified):-

Liability-hedging assets

- Cash (including currencies)
- UK Gilts (fixed and inflation linked)
- Annuity contracts held by the PPF secured on the life of specific members
- Sterling denominated interest rate and inflation swaps
- UK Gilts repurchase agreements

Return-seeking assets

- Fixed income
    - Global sovereign bonds
    - Other bonds of investment grade or sub-investment grade credit quality
    - Emerging market debt
- Equities listed on recognized stock markets
- Alternative assets
    - Property
    - Private equity
    - Alternative credit (including illiquid credit assets such as senior loans, leveraged loans, distressed debt, long and short positions on credit default swaps, mezzanine debt)
    - Infrastructure
    - Farmland
    - Timberland
    - Absolute return strategies

Hybrid Assets

- Sterling index-linked corporate debt
- Structured notes
- Collateral upgrade trades
- Alternative assets with long-term stable cash flows (e.g. long-term lease property, infrastructure debt, infrastructure project loans, real estate debt)

Foreign Exchange contracts to control currency risk

Tactical and hedging positions may be taken using the Permitted Asset Classes above and their derivative instruments.

Annex 2
Governance structure

The Board is responsible for	• Setting structures and processes for carrying out its role • Setting the funding framework, including objectives and an acceptable investment risk appetite within that framework • Reviewing the content of this Statement of Investment Principles in conjunction with the investment adviser, the Fund's actuary and legal adviser and modifying it if deemed appropriate • Providing oversight of the Investment Committee • Consulting with relevant bodies when reviewing investment policy issues
The Investment Committee is responsible for	• Developing the Pension Protection Fund investment principles and strategic approach to investment • Approving revisions to the Statement of Investment Principles or recommending changes, where these are material, to the Board • Developing and maintaining the Fund's responsible investment principles • Determining the overall approach to risk management of investments and asset liability matching, including setting the asset allocation strategy, and the flexibility around which any risk budget may be expressed • Determining the principles for dealing with the investments of schemes in assessment and subsequent transfer to the Fund • Approval of the framework and oversight of the appointment, retirement and contractual review of the fund managers (as defined in section 113(5) of the Act) including the assessment of appropriate knowledge and experience under section 113(6) of the Act • General oversight of the investment performance • Approval of the framework for the appointment, retirement and contractual review of any investment advisers • Approval of the framework for the appointment, retirement and contractual review of the custodian to the Fund

The Asset and Liability Committee is responsible for	• Monitoring the implementation of the investment strategy and Statement of Investment Principles • Confirmation of the appointment, retirement and contractual review of the fund managers (as defined in section 113(5) of the Act) including the assessment of appropriate knowledge and experience under section 113(6) of the Act • Reviewing on a monthly basis the investment managers investment performance, compliance with investment mandates and short term strategies • Monitoring the performance of the custodian to the Fund • Monitoring the flows of cash and schemes transferred to the Fund making sure the asset allocation does not deviate significantly from the strategic asset allocation • Monitoring financial risks including, all investment risks relative to the liabilities, insurance risks and, where necessary, initiate remedial measures • Collaborating with the Chief Actuary in the annual valuation of the Fund, including choice of actuarial assumptions • Sponsoring the development of specific risk mitigation measures such as liability hedges • Recommending to the Investment Committee changes to asset allocation, fund mandates and fund managers
The investment advisers are responsible for	• Advising on all aspects of the investment of the Fund assets including implementation of strategy • Providing updates on the fund managers and their likelihood of achieving the performance objectives • Advising on this Statement of Investment Principles • Providing training in investment matters to the Board

The fund managers are responsible for	• Discretionary management of the portfolio, including implementation (within guidelines given by the Investment Committee) of changes in the asset mix and selecting securities within each asset class • Providing the Asset and Liability Committee with quarterly statements of the assets together with a quarterly report on actions and future intentions, and any changes to the processes applied to their portfolio • Informing the Asset and Liability Committee of any changes in the internal objectives and guidelines of any pooled funds used by the Fund as soon as practicable • The safekeeping of the assets within the pooled funds in which the Fund invests • Investing income paid to the Fund in a timely manner • Reconciling the manager's record of assets held with those of the Custodian
The custodian is responsible for	• The safekeeping of all the directly held assets of the Fund • Undertaking all appropriate administration relating to the held assets of the Fund • Processing all income with respect to the Fund in a timely manner • Processing all tax reclaims in a timely manner • Investing cash in a suitable low risk manner consistent with the provision set out in the investment management agreements as agreed by the Board • Reconciling records of assets held with those of the managers
The transition managers are responsible for	• Moving assets between fund managers and/or asset types in a cost efficient way whilst minimising risks • Managing the asset transition process when pension schemes in assessment fall into the Fund

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