



USS Default Lifestyle Option Statement of Investment Principles

1. Introduction

- 1.1 This is the Statement of Investment Principles of the Universities Superannuation Scheme (“**USS**” or “**scheme**”) Default Lifestyle Option (the “**Default SIP**”). The USS Default Lifestyle Option is the default arrangement in relation to the Investment Builder part of the scheme (“**DC part**”). Although the USS Default Lifestyle Option can be actively chosen by members as their investment strategy, as the default arrangement it is the investment strategy into which the contributions of members in the DC part who do not make any investment decisions are paid.
- 1.2 Universities Superannuation Scheme Limited (the “**trustee**”) has selected a lifestyle strategy as its default arrangement. The lifestyle strategy is designed to meet the divergent objectives of maximising the value of a member’s assets at retirement and protecting the value of accumulated assets particularly in the years approaching retirement.
- 1.3 This Default SIP sometimes refers to the main Statement of Investment Principles (the “**Main SIP**”), which applies to the whole scheme. Copies of the Main SIP can be found in the “*How we invest*” area of the scheme’s website uss.co.uk.

2. The trustee’s Investment Beliefs

- 2.1 The trustee maintains a set of Investment Beliefs which are available in the “*How we invest*” area of the scheme’s website uss.co.uk. These beliefs form the basis of the trustee’s investment principles as set out in Section 1.2 of the Main SIP and Section 2 of this Default SIP.
- 2.2 In relation to the Default Lifestyle Option, the trustee’s key beliefs are that:
 - 2.2.1 The investment design of the Default Lifestyle Option will take into account the hybrid benefit design and the benefit flexibility that members have up to and into retirement;
 - 2.2.2 The asset allocation will adjust around a glide-path consistent with assumed member risk tolerance throughout the member’s savings life-cycle. The default strategy cannot capture all differences across individual members. However, a higher risk tolerance is assumed when members are far from retirement, with the aim of increasing expected real (after inflation) returns and retirement savings. In later stages of the savings life-cycle, the accumulated investment pots will

typically be greater and the ability to subsequently make good any material losses is reduced;

- 2.2.3 Asset allocation and the timing of material changes to it are important drivers of a fund's financial outcomes. The asset allocation process for the Default Lifestyle Option balances diversified risks against the expected additional returns for exposure to these risks. The main sources of return for bearing risk ('risk premia') are expected to be equity, credit, illiquidity and complexity. Other exposures such as duration, inflation and foreign exchange offer less reliable risk premia but are expected to provide valuable sources of portfolio diversification. The asset mix should be reviewed periodically for suitability relative to evolving investment objectives and to take into account material changes to relative valuations across asset classes, which strongly influence long-run return prospects and risk of loss;
- 2.2.4 Private Markets provide investment opportunities and structures not available in Public Markets in areas such as private equity, infrastructure, property and private debt. Private Markets may be accessed via a mix of direct investments, co-investments and fund investments. They may provide opportunities for additional returns (including illiquidity premia), diversification or other desired characteristics relative to Public Market assets; and
- 2.2.5 Diversification through effective portfolio construction allows risk to be mitigated and spread across a range of factors. This reduces the adverse impact of any one risk on a member's pension investments. There are limits, however, on overall risk-reduction from diversification and there are scenarios in which the correlation between asset classes increases and diversification may be less effective.

3. Investment governance structure

- 3.1 The trustee applies the same governance structure it uses for the scheme as a whole to the Default Lifestyle Option. This is described in detail in Section 1.3 of the Main SIP.
- 3.2 Broadly, the trustee's governance structure focuses on embedding compliance with legislative and regulatory requirements into agreements with investment and related service providers. The trustee monitors compliance by having clear terms of reference for the board and sub-committees to which it delegates a number of tasks, supplementing this with appropriate formal investment advice where required.

4. Aims and objective of the USS Default Lifestyle Option

- 4.1 The main investment objectives in relation to the DC part are described in detail in Section 3.1 of the Main SIP. The Default Lifestyle Option aims to take a suitably controlled amount of risk to generate investment returns in order to provide a reasonable level of retirement benefits for members, taking into account the expected performance of asset markets and the level of contributions paid over a member's lifetime into the DC part and recognising the hybrid nature of the scheme.
- 4.2 As well as the objectives set out in the Main SIP, the specific objectives of the Default Lifestyle Option are detailed below:

- 4.2.1 To focus particularly on generating returns in excess of inflation during the growth phase of the strategy (up to ten years before target retirement age) with a degree of downside risk mitigation;
- 4.2.2 To provide a strategy that reduces investment risk in the consolidation phase for members between ten and five years before target retirement age;
- 4.2.3 To provide exposure, at retirement, to a portfolio of assets that aligns as much as possible with how a typical member is likely to use their savings at and into retirement; and
- 4.2.4 To ensure sufficient liquidity to be able to pay benefits or transfers when required.

5. Investment Strategy

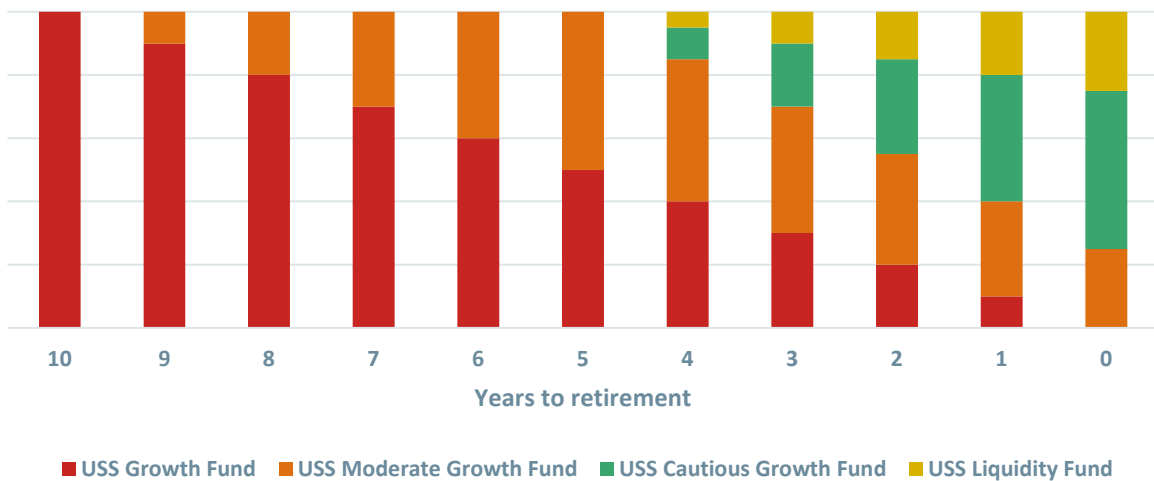
5.1 Kinds of investments to be held

- 5.1.1 The main policies covering the kinds of investments to be held, the expected returns and the balance between different kinds of investments can be found in Section 3.2 of the Main SIP.
- 5.1.2 The following are indicative descriptions of the type of investments that may be held by the different underlying funds comprising the USS Default Lifestyle Option:
 - **USS Growth Fund** – will invest predominantly in growth assets, with an objective to provide long-term growth in excess of inflation to members. Investments will be made in both Public and Private Markets across a range of asset classes in order to take advantage of the opportunity to earn enhanced returns including a premium for illiquidity and the benefit of diversification.
 - **USS Moderate Growth Fund** – will typically invest a majority in growth assets, with more diversification than the growth fund, and with an objective to provide long-term growth in excess of inflation from a balanced, more diversified portfolio of assets. Investments will be made in both Public and Private Markets across a range of asset classes to increase diversification and enhance returns. This additional diversification aims to mitigate portfolio risk to a greater extent than is the case for the USS Growth Fund.
 - **USS Cautious Growth Fund** – with an objective to provide stable growth in excess of inflation to members from a portfolio of predominantly lower risk, income focussed assets, with some diversification, and minority exposure to growth assets. Investment will be made in both Public and Private Markets across a range of asset classes to increase diversification and enhance returns.
 - **USS Liquidity Fund** – typically aims to produce a return in-line with its benchmark which represents short-term interest rates, principally from a

portfolio of Sterling denominated cash, deposits and money market instruments.

5.1.3 Moving from the USS Growth Fund to the USS Moderate Growth Fund to the USS Cautious Growth Fund would be associated with decreasing proportions in growth assets, such as equities and property; and increasing proportions in non-government and government bonds.

5.1.4 The chart below provides an illustration of the Default Lifestyle Option structure, in particular detailing the balance between the different funds held in the years prior to a member’s target retirement age:



5.2 Managing risk

5.2.1 The Default Lifestyle Option manages strategic asset allocation risks through use of diversification. The allocation typically consists of a mix of mainstream Public Market assets as well as allocations to Private Market assets throughout the savings life-cycle. The asset allocation is calibrated to different stages in the Default Lifestyle Option (as indicated in Section 5.1.3 of this Default SIP). Risk is not considered in isolation, but in conjunction with expected investment returns and outcomes for members. In designing the Default Lifestyle Option, the trustee considers the trade-off between risk and expected returns and opportunities for diversification and continues to monitor these risks through ongoing reporting. The actual holdings within the constituent parts of the Default Lifestyle Option will include Private Market assets where appropriate in order to take advantage of the opportunity to earn enhanced returns including a premium for illiquidity and to gain additional diversification.

5.2.2 The USS Growth Fund invests in equities and other growth-seeking and diversifying assets. These investments are structured to generate higher real returns over the long term with some downside protection. During the growth phase, the downside risk from an equity market downturn is partially mitigated through diversification away from equities into other growth-seeking asset classes.

- 5.2.3 In the consolidation phase, which commences 10 years before target retirement age, the trustee is seeking, through greater diversification of assets, to reduce the likelihood of extreme investment shocks adversely affecting retirement outcomes.
- 5.2.4 In the final five years before target retirement age, the trustee has constructed a glide-path that seeks to continue to grow the member's DC retirement savings while reducing volatility. In the final five years, assets are therefore switched to more cautious assets (such as government and corporate bonds), including an allocation to money market instruments. This has been designed to reflect the uncertainty inherent in the timing of retirements, and the post-retirement investment choices that might be made by members.
- 5.2.5 Section 3.3 of the Main SIP details key risks that the trustee considers in relation to the DC part in particular.

5.3 Realisation of investments, cashflow and liquidity management

- 5.3.1 The DC part offers members a range of daily dealing notional funds. While a portion of the USS Default Lifestyle Option will be in illiquid assets throughout the savings life-cycle, the trustee's policy is to maintain sufficient investments in liquid assets so that the realisation of assets will not be unduly costly nor disrupt the Default Lifestyle Option or the scheme's overall investment strategies in foreseeable circumstances. The trustee has thresholds on the proportion of illiquid assets being held in the Default Lifestyle Option and, while it currently has no plans to increase these in the near future, it reviews the thresholds on a periodic basis. More detail can be found in Section 3.2.9 of the Main SIP.

6. The trustee's policies on responsible investment and engagement activities

- 6.1 The USS Default Lifestyle Option is managed in line with the trustee's policies as set out in the Main SIP, in particular, Section 1.4 of the Main SIP. The trustee's policies on responsible investment and engagement activities cover:
 - 6.1.1 how financially material considerations are taken into account in the selection, retention and realisation of investments. This includes how the trustee considers the financial impact of Responsible Investment (RI) factors where financially material to the scheme;
 - 6.1.2 the extent to which non-financial matters are taken into account in the selection, retention and realisation of investments;
 - 6.1.3 the exercise of the rights (including voting rights) attaching to the investments; and
 - 6.1.4 engagement activities in respect of the investments.
- 6.2 In addition to the Default Lifestyle Option, the trustee makes available the Ethical Lifestyle Option reflecting the fact that a number of members have specific preferences. The specific objectives of the Ethical Lifestyle Option are defined in the USS Investment Builder Ethical Guidelines. This Ethical Lifestyle Option is built along similar principles to the Default

Lifestyle Option but has been specifically designed to reflect certain preferences. As well as this, an ethical equity fund and a Sharia consistent fund are included in the range of self-select funds offered to members.

- 6.3 The scheme's Responsible Investment Policy sets out detailed information on how the trustee considers RI factors where financially material to the scheme and the extent to which it takes non-financial RI and other factors into account. The trustee expects its internal and external managers to act consistently with this statement in the selection, retention and realisation of the scheme's investments. The trustee's position on RI can be found in the "How we invest" area of the scheme's website uss.co.uk. This area of the website includes the RI Beliefs and Ambition statement which further articulates the trustee's investment beliefs.
- 6.4 The trustee's policies in relation to its arrangements with asset managers are as set out in Section 1.5 of the Main SIP, including in relation to the trustee's wholly owned investment manager and advisor, USS Investment Management Limited ("USSIM") which is primarily responsible for the management of the Default Lifestyle Option and manager selection.

7. Investment in the best interests of beneficiaries

- 7.1 In designing the Default Lifestyle Option, the trustee aims to invest in the beneficiaries' best financial interests, taking into account the different risk profile of representative members (e.g., according to their expected time frame until retirement). In doing so, the trustee explicitly considers the trade-off between risk and expected returns and continues to monitor these risks through ongoing reporting. The trustee considers high level profiling analysis of the scheme's membership in order to inform decisions regarding the Default Lifestyle Option. In accordance with the trustee's mandate, USSIM also manages and monitors the default arrangement and the performance of investment managers involved in that arrangement and makes changes where necessary to ensure the trustee's aims and objectives are met.

8. Compliance and review

- 8.1 This Default SIP has been prepared in accordance with the requirements of the Pensions Act 1995 and relevant regulations, including the Occupational Pension Scheme (Investment) Regulations 2005, and taking into account guidance from the Pensions Regulator.
- 8.2 The trustee will undertake a review at least triennially, or sooner and without delay if there are significant changes to the scheme's investment policy, demographic profile or other circumstances which the trustee determines warrant a reconsideration of the Default Lifestyle Option.
- 8.3 The trustee will revise the Default SIP after every review unless it decides that no action is needed as a result of the review.