# Alwen Hough Johnson
# Pension and Assurance Scheme

# Statement of Investment Principles

## June 2020

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# 1. INTRODUCTION

## 1.1 PURPOSE OF THE STATEMENT

This statement sets out the principles and policies that govern investments made by the Trustees of the Alwen Hough Johnson Pension and Assurance Scheme.

## 1.2 STATUTORY REQUIREMENTS

This statement is made in accordance with the requirements of the Pensions Act 1995 and the Occupational Pensions (Investment) Regulations 2005 made under the Pensions Act 2004.

The Trustees are aware of the Pension Regulator's Investment Guidance for defined benefit pension schemes dated March 2017 and of the Myners Principles which were updated in 2008. The Trustees consider their investment policy to be consistent with this guidance.

## 1.3 INVESTMENT ADVICE

As required by legislation, in the preparation and maintenance of this statement and when considering the suitability of any investments, the Trustees have obtained and considered written advice from their investment adviser.

The Trustees are advised on investment matters by First Actuarial LLP. First Actuarial LLP is regulated by the Institute and Faculty of Actuaries and is qualified to provide the required advice through knowledge and practical experience of financial matters relating to pension schemes.

## 1.4 EMPLOYER CONSULTATION

Under legislation, the ultimate responsibility for determining the investment strategy rests with the Trustees. However, the Trustees must consult with the sponsoring employer and consultation must comprise a sharing of views, not simply notification of intent.

The Trustees have consulted with the sponsoring employer as part of the work preparing this statement.

## 1.5 REVIEWING THIS STATEMENT

This statement will be reviewed at least every three years and without delay after any significant change in circumstances or investment policy.

A copy of this statement and any amendments made to it are available to the Scheme Actuary and to the managers of the pooled investment vehicles used by the Trustees.

# 2. OBJECTIVES AND STRATEGIC ALLOCATION

## 2.1 INVESTMENT OBJECTIVES

The Trustees have set an investment strategy that reflects the following objectives:

| **Primary Objectives:** | |
|---|---|
| Cash Flow Objective | To try and ensure assets are available to meet benefits as they fall due. |
| Valuation Objective | To achieve and maintain a stable funding level of at least 100% on the Statutory Funding Objective (“SFO”) basis. |
| Stability Objective | To pay due regard to the sponsoring employer’s interests in the size and incidence of Employer’s contribution payments. |
| **Secondary Objective:** | |
| Valuation Objective 2 | To achieve and maintain a stable funding level of at least 100% on the low dependency basis. |

It is recognised that targeting higher levels of investment return introduces investment risk which increases the volatility of the financial position.

## 2.2 INVESTMENT BELIEFS

The investment beliefs stated below have been developed by the Trustees and are reflected in the Scheme’s investment strategy.

*Risk versus Reward*

- Targeting higher levels of investment return requires increased levels of investment risk which increases the volatility of the funding position.

*Asset Allocation*

- Long-term performance of the Scheme’s assets is attributable primarily to the strategic asset allocation rather than the choice of investment managers.

*Diversification*

- Asset diversification helps to reduce risk.

*Use of Pooled Funds*

- Taking into account the size of the Scheme’s assets, it is expected that pooled funds will typically be a more practical way of implementing the Scheme’s investment strategy than establishing segregated mandates with investment managers.

*Use of Active Management*

- For some asset classes, active management has the potential to add value either through offering the prospect of enhanced returns or through the control of volatility. In addition, it is recognised that active management may help to mitigate the financial impact of ESG risks.

- For each asset class, the Trustees will consider whether the higher fees associated with active management are justified.

## 2.3 SETTING THE STRATEGIC ASSET ALLOCATION

The Trustees' strategic asset allocation is determined after considering written advice from the investment adviser and is designed to strike a balance between the above objectives. The strategic asset allocation takes into account:

- the nature and timing of liability payments;
- expected levels of investment return on the different asset classes;
- expected levels of investment return variability and, specifically, the expected level of short-term volatility of the Scheme's financial position;
- the sponsoring employer's ability to withstand the additional contribution requirements that may arise from such volatility in the financial position; and
- the full range of available investments (within the bounds of practicality).

In determining the strategic asset allocation, the Trustees view the investments as falling into two broad categories:

1. **Growth Assets** – Assets that are expected to deliver long-term returns in excess of liability growth. The use of Growth Assets is expected to deliver the level of investment returns deemed appropriate by the Trustees.
2. **Liability Matching Assets** – Assets that are expected to react to changes in market conditions in a similar way to the liabilities. The use of Liability Matching Assets is expected to protect the funding position of the Scheme.

The Trustees' strategic asset allocation is detailed in a separate document entitled 'Investment Implementation Policy' and dated June 2020, although this may be amended from time to time.

As part of the Secondary Objective listed above, the Trustees have agreed a separate "De-risking Protocol" to reduce risk when the Scheme reaches a certain funding level on this basis. A summary of the agreed investment strategies for each trigger is set out in the separate document entitled 'Investment Implementation Policy' as referenced above. This also includes details of the target interest rate and inflation hedge ratios at each trigger point.

# 3. IMPLEMENTATION

## 3.1 IMPLEMENTATION OF THE INVESTMENT STRATEGY

Day-to-day management of the assets is delegated to one or more investment managers. The mandates set for the investment managers are intended to implement the Trustees' investment objectives within an acceptable level of risk.

Details of the mandates set for the investment managers are provided in the separate document entitled 'Investment Implementation Policy' as referenced above.

The Trustees are satisfied that the investment managers have the appropriate knowledge and experience required to competently manage the investments.

The Trustees consider each investment manager's mandate carefully to ensure it is appropriate. Where pooled investment vehicles are used, it is recognised that the mandate cannot be tailored to the Trustees' particular requirements. However, the Trustees ensure that any pooled investment vehicles used are appropriate to the circumstances of the Scheme.

The Trustees, in conjunction with their investment adviser, regularly review each of the investment managers to ensure that the manager remains competent and that the assets continue to be managed in accordance with the manager's mandate.

## 3.2 SAFEKEEPING OF ASSETS

To ensure safekeeping of the assets, ownership and day to day control of the assets is undertaken by custodian organisations which are independent of the sponsoring employer and the investment managers. Where pooled investment vehicles are used, the custodians will typically be appointed by the investment managers.

## 3.3 REGULATED MARKETS AND DERIVATIVES

Assets are invested predominantly on regulated markets, as so defined in legislation. Any investments that do not trade on regulated markets are kept to a prudent level.

The investment managers are permitted to use derivative instruments to reduce risk (for example to mitigate the impact of a potential fall in markets) or for efficient portfolio management. Efficient portfolio management would include using derivatives as a cost-effective way of gaining access to a market or as a method for generating capital and/or income with an acceptable level of risk.

The derivatives used by the investment manager of the Liability Matching Assets may result in the Liability Matching Assets being leveraged. Since these assets are closely aligned to the liabilities, the allocation to Liability Managed Assets (and any associated derivatives) reduces the volatility of the Scheme's funding position and therefore reduces risk.

## 4. RISKS AND OTHER MATTERS

### 4.1 INVESTMENT RISKS

Identification, measurement and management of risk form an integral part of the process adopted by the Trustees to determine an appropriate investment strategy. The principal investment risks are listed in the accompanying Investment Risk Policy document along with an explanation of how those risks are managed.

### 4.2 EMPLOYER-RELATED INVESTMENT

The proportion of the Scheme's investments which can be related to the sponsoring employer (as defined within legislation) is limited to 5% of the value of total assets.

The Trustees do not hold any direct employer-related assets and any indirect exposure is expected to be less than 5% of total assets.

### 4.3 TRUSTEES' APPROACH TO SOCIAL, ENVIRONMENTAL AND GOVERNANCE ("ESG") FACTORS

In setting the Scheme's investment strategy, the Trustees' primary concern is to act in the best financial interests of the Scheme and its beneficiaries, seeking return that is consistent with a prudent and appropriate level of risk. This includes the risk that environmental, social and governance factors (including climate change) negatively impact the value of investments held if not understood and evaluated properly. The Trustees consider this risk by taking advice from their investment adviser when setting the Scheme's asset allocation, when selecting managers and when monitoring their performance.

The Trustees invest primarily through pooled investment vehicles. It is therefore accepted that the extent to which corporate governance, socially responsible practices and ethical behaviour are used in the selection of suitable investments will be determined by the investment managers' own policies on these matters.

**Stewardship (voting and engagement) –** As part of their delegated responsibilities, the Trustees expect the Scheme's investment managers to take into account environmental, social and governance considerations in the selection, retention and realisation of investments (where actively managed); and to exercise the Trustees' voting rights in relation to Scheme assets (for both passively and actively managed funds).

The Trustees regularly review the suitability of the appointed managers, including reputational matters. This includes consideration of broader stewardship matters and the exercise of voting rights by the appointed managers.

**Members' views and non-financial factors –** In setting and implementing the Scheme's investment strategy the Trustees do not explicitly take into account the views of Scheme members and beneficiaries in relation to ethical considerations, social and environmental impact, or present and future quality of life matters (defined as "non-financial factors").

## 5. INVESTMENT MANAGER ARRANGEMENTS

### 5.1 COMPATIBILITY OF POOLED FUNDS WITH THE TRUSTEES' INVESTMENT STRATEGY

When selecting a pooled fund, the Trustees consider various factors, including:

- the assets that will be held within that fund and whether the asset allocation of the fund is expected to change over time;
- the risks associated with the fund along with the return that is expected;
- the fund's objective (as stated by the fund's investment manager) and whether the objective is consistent with the performance that the Trustees expect from that fund;
- the fund's fee structure to ensure that this is reasonable and that it does not provide an incentive for the investment manager to manage the fund in a way that differs from the expectations of the Trustees.
- how frequently underlying investments within the fund are expected to be traded by the investment manager;
- how financially material considerations[1] (including ESG factors) over the appropriate time horizon[2] are taken into account by the investment manager;
- the investment manager's policy in relation to the exercise of the rights (including voting rights) attaching to the investments held within the pooled fund; and
- the investment manager's policy in relation to undertaking engagement activities in respect of the investments held within the pooled fund[3].

- [1] *"financially material considerations" includes (but is not limited to) environmental, social and governance considerations (including but not limited to climate change), which the trustees of the Scheme consider financially material.*
- [2] *"appropriate time horizon" means the length of time that the trustees of the Scheme consider is needed for the funding of future benefits by the investments of the scheme.*
- [3] *This includes engaging with an issuer of debt or equity regarding matters including (but not limited to) performance, strategy, capital structure, management of actual or potential conflicts of interest, risks, and ESG matters. It also includes engaging on these matters with other investment managers, other holders of debt or equity and persons or groups of persons who have an interest in the issuer of debt or equity.*

After analysing the above characteristics for a fund, the Trustees identify how that fund would fit within their overall investment strategy for the Scheme and how the fund is expected to help the Trustees meet their investment objectives.

## 5.2 DURATION OF INVESTMENT MANAGER ARRANGEMENTS

The Trustees normally expect that pooled funds will be held for several years.

However, as part of the periodic strategic asset allocation reviews (which take place at least every three years), the Trustees will review whether the ongoing use of each fund remains consistent with their investment strategy.

The Trustees regularly monitor the financial and non-financial performance of the pooled funds held and details of this monitoring process is set out below. If the Trustees become concerned about the ongoing suitability of a pooled fund, they may reduce exposure to it or disinvest entirely. Such action is expected to be infrequent.

## 5.3 MONITORING POOLED FUNDS

The Trustees regularly assess the performance of each fund held and this monitoring includes an assessment of whether the investment manager continues to operate the fund in a manner consistent with the factors used by the Trustees to select the fund (listed above).

When assessing the performance of a fund, the Trustees do not usually place too much emphasis on short-term performance although they will seek to ensure that reasons for short-term performance (whether favourable or unfavourable) are understood.

The Trustees expect the investment managers of pooled funds to invest for the medium to long term and they expect investment managers to engage with issuers of debt or equity with a view to improving performance over this time frame.

If it is identified that a fund is not being operated in a manner consistent with the factors used by the Trustees to select the fund, or that the investment manager is not engaging with issuers of debt or equity, the Trustees may look to replace that fund. However, in the first instance, the Trustees would normally expect their investment adviser to raise the Trustees' concerns with the investment manager. Thereafter, the Trustees, in conjunction with their investment adviser, would monitor the performance of the fund to assess whether the situation improves.

## 5.4 PORTFOLIO TURNOVER

The Trustees are aware of the requirement to monitor portfolio turnover costs (the costs incurred as a result of the buying, selling, lending or borrowing of investments). When selecting a pooled fund, the Trustees will consider how the investment manager defines and measures:

- the targeted portfolio turnover (the frequency within which the assets of the fund are expected to be bought or sold); and
- turnover range (the minimum and maximum frequency within which the assets of the fund are expected to be bought or sold).

At least annually, the Trustees, in conjunction with their investment adviser, will consider the transaction costs incurred on each pooled fund. As part of this analysis, the Trustees will consider whether the incurred turnover costs have been in line with expectations.

The Trustees will take the above information on portfolio turnover into account when assessing the ongoing suitability of each pooled fund.

## 6. FUTURE AMENDMENTS

From time to time, and following receipt of advice from its investment adviser, the Trustees may agree to make changes to the investment strategy set out in this statement. Any such changes will be summarised in an addendum to this statement.

Before any changes are made to the investment strategy, the Trustees will consult with the sponsoring employer.

The principles set out in this statement have been agreed by the Trustees:

Philip Whittome

Date: 13th August 2020

For and on behalf of the Trustees of the Alwen Hough Johnson
Pension and Assurance Scheme

The principles set out in this statement have been agreed by the sponsoring employer:

Angela Treen

$13^{th}$ August 2020

For and on behalf of the sponsoring employer