Nestlé UK Pension Fund (DB Section)

# Statement of Investment Principles

August 2019

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# Introduction

The law requires Nestlé UK Pension Trust Limited ('the Trustee') to produce a formal 'Statement of Investment Principles' or 'SIP' for Nestlé UK Pension Fund ('the Fund'). This SIP sets out the principles governing investment decisions for the Fund.

This SIP covers a number of technical points to comply with legislation, as well as meet the expectations of the Pensions Regulator and needs of the Fund's Auditors. The Fund compromises of both a defined benefit section and defined contribution section. This document covers the defined benefit section (DB Section) only of the Fund.

**For the record**

This SIP has been prepared in accordance with the requirements of sections 35, 36 and 56 of the Pensions Acts 1995 and 2004. The Trustee have taken proper written advice from their Investment Consultant and consulted the Principal Employer to the Fund in the preparation of this Statement of Investment Principles.

The Trustee will review this Statement at least every three years or more frequently as required by the Regulations, and without delay after a significant change in investment policy or demographic profile of the Fund's membership.

This Statement of Investment Principles was completed in August 2019. It will be next reviewed no later than August 2022.

**Signed on behalf of the Trustee Directors of Nestlé UK Pension Trustee Limited as Trustee of the Nestlé UK Pension Fund:**

| Name | Signature | Date |
|---|---|---|
| JD Chillman | | Aug 2019 |

| Name | Signature | Date |
|---|---|---|
| SJ Robinson | | Aug 2019 |

# Section 1: Investment Beliefs

The Trustee, having consulted with the Fund's Investment Consultant(s), has adopted the following investment beliefs:

- An effective investment strategy must have clearly defined objectives for both return and risk and clear measures of success that allows progress to be monitored.
- To meet our objectives, we need a clear understanding of the risks that we are taking and to only take risks that we believe are adequately rewarded. To the extent it is possible, we try and mitigate any unrewarded risks through strategies such as hedging.
- The most significant contribution to meeting our investment objectives will come from our asset allocation and risk management choices.
- Good governance and decision-making will positively impact our ability to meet our objectives.
- Our approach to investment should avoid unnecessary complexity.
- Over the long-term, higher-risk assets such as equities are expected to outperform lower-risk assets (such as bonds), but their returns are also expected to show higher variability.
- Diversification within and across asset classes reduces the risk created by particular investments failing and should lower the volatility of overall returns.
- We believe that investments should be assessed in a value-based context, i.e. the impact of investments on both expected and actual risk-adjusted returns should be viewed net of costs. Additionally, the impact of costs needs to be understood before we invest and they should be kept as low as possible without compromising our objectives.

# Section 2: Trustee's Objectives

The Trustee's objectives are:

- Primarily to invest the assets of the Fund to meet its liabilities when they are due. The Trustee wishes to protect members' accrued benefits, whilst maintaining a reasonable prospect of improving the funding level up to 100% on their target basis;
- To manage the investment risk, including that arising due to mismatch between assets and liabilities, and limit the total risk of the Fund. This includes (but is not limited to) deficit risk, investment manager risk, volatility/market risk, liquidity risk, currency risk, interest rate and inflation risk, political risk, sponsor risk and counterparty risk. The Trustee monitors and manages these risks through measures specific to each risk; and
- Maintain suitable liquidity of assets such that the Fund is not forced sell investments at particular times to pay member benefits or meet potential collateral calls.

In order to help the Trustee achieve its investment objectives, the Trustee has established a Defined Benefit Financing Committee ('DBFC'), which is responsible for certain investment matters delegated to it under terms of reference agreed by the Trustee from time to time ('the DBFC Terms of Reference').

# Section 3: Summary of the Fund's Investment Strategy

Three key portfolios make up the Fund's Strategic Asset Allocation ('SAA'):

- The Growth portfolio: The intention of this portfolio is to invest in assets such as Equities, Private Equity, Hedge Funds, that look to generate positive long-term returns to help the Fund meet its investment objectives.
- The Matching Plus portfolio: The intention of this portfolio is not to perfectly match the Fund's liabilities. Instead, it aims to achieve a modest excess returns by investing in assets that have the characteristics of generating a set of cashflows, which may have some element of interest rate and inflation sensitivity. These assets will, therefore, provide risk reduction and help the Fund meet its liabilities when they fall due.
- The Matching Portfolio: This portfolio is invested in assets that look to match the interest rate and inflation sensitivities of the liabilities (up to a hedge ratio specified by the Trustee). These assets have the sole purpose of reducing interest rate and inflation risk that the Fund is exposed to through the valuation of the liabilities.

The Trustee has a long-term objective to manage the SAA in a manner that reflects the Fund's maturity and funding level. Therefore, as the Fund's liabilities mature and/or its funding level improves, a portfolio of predominantly Growth assets will transition towards Matching Plus and Matching assets. The exact nature of the long term SAA is under discussion pending the conclusion of the 31 December 2018 valuation, however the Trustee and sponsor have agreed that a short-term de-risking action is appropriate given the Fund's progress against its investment objectives as stated in this section.

The assets within each portfolio are determined after taking into consideration the Trustee's overall objectives stated in this section and the objectives of the underlying portfolios stated in section 4. Their expected returns are as estimated and advised by the Fund's Investment Consultant(s).

The Fund holds investments as permitted by its Trust Deed and Rules.

# Section 4: Investment Managers

The Trustee delegates the day-to-day management of the assets to a number of Investment Managers.

Investment Managers are carefully selected to manage each of the underlying mandates following guidance and written advice from the Investment Consultant(s).

The Fund pays an annual fee to each manager, which along with the mandate's performance targets, benchmarks and restrictions are set out in the respective Investment Management Agreements.

The Trustee assesses the managers' performance regularly against a benchmark appropriate to each manager, taking into account the level of risk taken by each manager. To assist the Trustee in assessing performance, the Investment Consultant(s) will provide relevant reporting on a quarterly basis. As part of this process, the Trustee has delegated the detailed monitoring of the Fund's Investment Managers to its Investment Consultant(s).

From time to time managers and/or mandates are changed. This is done after due consideration and the receipt of appropriate advice from the Fund's Investment Consultant(s).

# Section 5: Responsible Investment Principles

The Trustee has an objective to stay up to date with new developments and emerging risks in Environmental, Social and Governance ('ESG') factors. The Trustee's policy on ESG is summarised by these points:

- ESG factors (including climate change) are likely to be financially material.
- In the long term, better financial returns are likely to be achieved by investing in companies and assets that demonstrate they contribute to the long-term sustainable success of the global economy.
- ESG factors will become increasingly financially material and an important factor in strategic decision making.
- All else being equal, the strategy should allocate to asset classes where ESG can be integrated into decision making. However, this does not mean that the Trustee will allocate to asset classes for ESG reasons alone or preclude the use of asset classes where this is not possible; ESG will be assessed along with other factors such as investment risk and return.
- For each new asset class considered, the relevance of ESG will be assessed and weighted accordingly when carrying out manager selection exercises and while determining the investment approach (e.g. active or passive). Whilst, for existing asset managers we regularly review their processes to ensure the extent to which they integrate ESG into their investment process is sufficient for that asset class.
- For each asset class, the relevance of good stewardship should be assessed to ensure that Investment Managers engage with companies where appropriate. Where voting rights are held (e.g. through direct equity ownership), these rights should be exercised.
- Investment Managers are required to provide quantitative reporting on ESG where possible and monitor quantitative ESG reporting, using this to inform future manager selection and asset allocation decisions.

For passively managed funds, the Trustee recognises that the role of the manager is to track an index, and the choice of index will dictate the assets held. The Trustee keeps this under review.

For actively managed funds (where the Investment Manager decides where to invest) Investment Managers are expected to take financially material considerations into account when deciding on the selection, retention and realisation of investments where permissible within the applicable guidelines and instructions.

The Trustee does not take non-financial factors into account in the selection, retention and realisation of investments in the DB Section.

# Section 6: Stewardship, Voting and Engagement

The Trustee believes that engagement with the companies in which the DB Section invests, including the proactive use of shareholder voting rights, can improve the longer-term returns of the DB Section's investments.

The Trustee has adopted a policy of delegating voting decisions on stocks to the underlying Investment Managers on the basis that voting power will be exercised by them with the objective of preserving and enhancing long term shareholder value. The Investment Managers are expected to exercise the voting rights attached to individual investments in accordance with their own house policy.

Where relevant, the Trustee is planning to review the voting and engagement policies of the Investment Managers over the coming year and determine if these policies are appropriate. Going forward, on an annual basis, the Trustee will request that Investment Managers provide details of any change in their house policy.

Where appropriate, the Trustee will engage with and may seek further information from Investment Managers on how portfolios may be affected by a particular issue.

The Trustee does not engage directly but believes it is sometimes appropriate for the Investment Managers to engage with key stakeholders, which may include corporate management, regulators and governance bodies, regarding their investments in order to improve corporate behaviours, improve performance and mitigate financial risks. The Trustee aims to review engagement activity undertaken by the Investment Managers as part of its broader monitoring activity.

# Section 7: Other Matters

## 7.1 Custodians

The Trustee makes use of a global custodian to safeguard the Fund's non-pooled fund assets.

## 7.2 Investment Consultant(s)

The Trustee of the Fund has selected an appropriate investment consultancy firm(s) as adviser(s) to the Trustee and the DBFC.

## 7.3 What is the Trustee policy on self-investment?

As a general principle, the Fund should not actively invest in Nestlé-related assets, whether commercial paper, notes, bonds, loans, shares or buildings occupied by the Company, unless agreed by the Trustee.

The Trustee has agreed that it is acceptable to hold Nestlé related shares in passive funds or quantitative portfolios, where the manager is not assessing Nestlé on its fundamental principles. Additionally, in actively managed portfolios, it can be acceptable to hold a passive position in Nestlé shares in line with the weighting in the underlying benchmark.

The total of such investments (in any Nestlé fixed-income instruments + Nestlé shares + land rent/building occupied by the Company) should not exceed 5% of total assets of the Fund, unless specifically agreed by the Trustee.

## 7.4 Review of the SIP

The Trustee will, from time to time, review the appropriateness of the SIP with the help of its advisers, and will amend the SIP as appropriate. These reviews will take place as soon as practicable after any significant change in investment policy, and at least once every three years. Some changes to the SIP can be made by the DBFC in accordance with the DBFC Terms of Reference.