Chivas Brothers Pension Scheme

Statement of Investment Principles

1. Introduction

Chivas Brothers Pension Scheme (Trustee) Limited (the “Trustee”) is the sole Trustee of the Chivas Brothers Pension Scheme (“the Scheme”) and has drawn up this Statement of Investment Principles (“the Statement”) in compliance with the requirements of the Pensions Act 1995 (“the Act”) and subsequent legislation. The Statement is intended to affirm the investment principles that govern decisions about the Scheme’s investments.

In this Statement reference to the Trustee shall include those persons occupying the office of director of the Trustee.

In preparing this Statement the Trustee has consulted the Sponsoring Company to ascertain whether there are any material issues of which the Trustee should be aware in agreeing the Scheme’s investment arrangements.

2. Process for choosing investments

The process for choosing investments is as follows:

- Identify appropriate investment objectives;
- Agree the level of risk consistent with meeting the objectives set; and
- Construct a portfolio of investments that is expected to maximise the return (net of all costs) given the targeted level of risk.

In considering the appropriate investments for the Scheme the Trustee has obtained and considered the written advice from advisors whom the Trustee believes to be suitably qualified to provide such advice. The advice received and arrangements implemented are, in the Trustee’s opinion, consistent with the requirements of Section 36 of the Pensions Act 1995 (as amended).

3. Investment objectives

The Trustee’s overriding objective is to invest the Scheme’s assets in the best interest of the members and beneficiaries. Within this framework the Trustee has agreed a number of objectives to help guide them in their strategic management of the assets and control of the various risks to which the Scheme is exposed.

The Trustee’s primary objectives are as follows:

- To ensure that we can meet our obligation to the beneficiaries of the Scheme;
- To achieve a return on the total Scheme which is compatible with the level of risk considered appropriate, and supports the Scheme’s ongoing funding assumptions; and

- To pay due regard to the Sponsoring Company's interest in the size and incidence of contribution payments.

4. Risk management and measurement

4.1 There are a number of risks to which any investment is exposed. The Trustee recognises that whilst increasing risk increases potential returns over a long period, it also increases the risk of a shortfall in returns relative to that required to cover the Scheme's liabilities, as well as producing more short-term volatility in the Scheme's funding position.

4.2 In addition to targeting an appropriate overall level of investment risk, the Trustee seeks to spread risks across a range of different sources, believing that diversification limits the impact of any single risk. The Trustee aims to take on those risks, for which a reward, in the form of excess returns, is expected over time.

4.3 A "Liability Driven Investment" ("LDI") portfolio is also employed to more closely match the change in the liabilities due to changes in fixed interest and inflation rates.

4.4 The Trustee is aware of and pays close attention to a range of risks inherent in investing the assets of the Scheme, and which the Trustee believes may be financially material to the Scheme.

4.5 The following risks are recognised and considered by the Trustee:

- **Mismatch risk** - The primary risk upon which the Trustee focuses is that arising through a mismatch between the Scheme's assets and its liabilities. The key risks that can cause mismatching are:
  - Equity and credit market risk (the risk that equity and credit valuations fluctuate in an uncorrelated way with the value of the liabilities)
  - Interest rate risk (the risk that the assets do not move in line with the value placed on the Scheme's liabilities in response to changes in interest rates)
  - Inflation risk (similar to interest rate risk but concerning inflation)

- **Sponsor Covenant risk** - the financial capacity and willingness of the Sponsoring Company to support the Scheme is a key consideration of the Trustee and is reviewed on a regular basis.

- **Diversification risk** - The Trustee recognises the risks that may arise from the lack of diversification of investments. Subject to managing the risk from a mismatch of assets and liabilities, the Trustee aims to ensure that the asset allocation policy results in an adequately diversified portfolio.

- **Concentration risk** - The Trustee is also aware of concentration risk which arises for example when a high proportion of the Scheme's assets are invested in securities, whether debt or equity, of the same or related issuers or in the same or similar industry sectors. The overall investment arrangements are intended to provide an appropriate spread of assets by type and spread of individual securities within each asset class.

- **Liquidity risk** - The Trustee recognises that there is liquidity risk in holding assets that are not readily marketable and realisable. Given the long-term investment horizon, the Trustee believes that a degree of liquidity risk is acceptable, given the potential return and diversification benefits. The majority of the Scheme's assets are realisable at short notice.

- **Manager risk** - The Scheme's assets are invested with a number of managers. Allocations to different managers increase the level of diversification at the manager level.

- **Regulatory and political risk** - Across all of the Scheme's investments, there is the potential for adverse regulatory or political change. Regulatory risk arises from investing in a market environment where the regulatory regime may change. This may be compounded by political risk in those environments subject to unstable regimes. The Trustee will attempt to invest in a manner which seeks to minimise the impact of any such regulatory or political change should such a change occur.

- **Exchange rate risk** - This risk arises from unhedged overseas investments. The Trustee seeks to manage these risks as set out below:

Asset Class	Manager	Currency Hedging Arrangement
Developed Market Equity	Schroders	50% hedged back to GBP
	Baillie Gifford	
Emerging Market Equity	Schroders	Unhedged
Credit Opportunities	Mercer	Unhedged[1]
Multi-Asset Credit		Unhedged[1]
Long Lease Property	Aberdeen Standard Investments	Not applicable, manager only invests in the UK property market
Secured Finance	Ares	Unhedged[2]
	HSBC	Hedged

[1]In practice the underlying managers may, at their discretion, hedge currency risk exposures from time to time.
[2]The base currency of the Fund is USD and Ares hedge all non-USD exposure (including GBP) back to USD. Therefore, the Scheme is exposed to USD/GBP risk only.

4.6 The documents governing the appointment of each investment manager include a number of guidelines which, among other things, are designed to ensure that only suitable investments are held by the Scheme.

4.7 Arrangements are in place to monitor the Scheme's investments to help the Trustee check that nothing has occurred that would bring into question the continuing suitability of the current investments. To facilitate this, the Trustee meets with the investment managers from time to time, and receives regular reviews from the Investment Managers and the Investment Consultant.

4.8 The safe custody of the Scheme's assets is delegated to professional custodians (either directly or via the use of pooled vehicles).

4.9 Should there be a material change in the Scheme's circumstances, the Trustee will review whether (and to what extent) the investment arrangements should be altered; in particular, whether the current risk exposure remains appropriate.

5. Portfolio construction

5.1 The Trustee has adopted the following control framework in structuring the Scheme’s investments subject to the overriding constraint that at the total Scheme level the expected level of risk is consistent with the investment objectives:

- There is a role for both active and passive management. Passive management will be used for one of a number of reasons, namely:
  - To diversify risk;
  - When investing in markets deemed efficient where the scope for active management to add value is limited; and
  - As a temporary home pending investment with an active manager.
- All other things being equal there is a preference to invest via pooled funds, however segregated investments will be considered as circumstances require.
- To help diversify manager specific risk, multiple manager appointments within a single asset class are preferred where practical.
- At the total Scheme level and within individual manager appointments, investments should be broadly diversified to ensure there is not an over concentration of investment with any one issuer, if this is not considered to be in the best interests of the Scheme. For example, the Trustee may be willing to accept a degree of concentration risk if it is considered that there is a high probability of a particular investment enhancing the Scheme’s financial status and security. This restriction does not apply to investment in UK Government debt.
- Investment in alternative growth assets will be considered as a means of diversifying the Scheme’s return seeking assets and reducing the reliance on equities. The Trustee recognises the potential illiquidity risk involved in such investments, but considers this risk reasonable given the Scheme’s cashflow position, investment time horizon and the diversification that can be gained. Investment may be made in securities that are not traded on regulated markets. Recognising the risks (in particular liquidity and counterparty exposure) such investments will normally only be made with the purpose of reducing the Scheme’s mismatch risk relative to its liabilities, improving the Scheme’s funding level, to generate asset cashflows, or to facilitate efficient portfolio management (including improving collateral adequacy and liquidity).
- No direct investment in securities issued by the Scheme’s Sponsoring Company or affiliated companies is permitted (other than any such securities held within a pooled

fund in which the Trustee invests).

- No investment by an appointed investment manager in the securities issued by the relevant manager’s company or any affiliated companies is permitted (other than any such securities held within a pooled fund in which the Trustee invests).

- The LDI portfolio will be invested in physical gilts and index-linked gilts, as well as derivatives such as gilt and index-linked gilt repurchase agreements (“repo”), gilt and index-linked gilt total return swaps and interest and inflation rate swaps.

- The LDI portfolio is a bespoke arrangement which targets 70% of the interest rate and inflation exposure of the liabilities on a gilts flat basis (this assumes a zero contribution from the Central Asset Reserve to the overall level of hedging).

- The Trustee believes that the use of structured equity strategies, from time to time, are an effective way control equity market risks.

6. Asset Allocation

The Scheme's target investment strategy is detailed in the table below:

Asset Class	Target Allocation (%)	Control Ranges (%)
Liability Hedging and Synthetic Equity Capital	**51.0**	
Schroders - Collateral Pool[1]	51.0	No set control ranges, but monitored regularly
Credit Opportunities[2]	5.0	No set control ranges, but monitored regularly
Long Lease Property	1.0	8.0 – 12.0
Multi-Asset Credit	20.0	18.0 – 22.0
Secured Finance	10.0	8.0 – 12.0
Global Small Cap Equity	4.0	2.0 – 6.0
Total	**100.0**	
Liability Hedge Ratio (gilts flat basis)	**70% Interest Rates, 70% inflation**	

[1]The collateral pool includes an allocation to the Schroders Securitised Credit fund.
[2]The capital committed to Credit Opportunities is held in a Diversified Growth Fund on an interim basis, as part of the capital draw-down arrangements in place.

In addition to the liability hedging programme, the collateral pool supports a synthetic equity portfolio and equity downside protection strategy. The synthetic equity and equity downside protection strategy is designed to provide the equivalent of c. 26% (as a % of total assets) exposure to global equity markets, with partial protection against extreme downside scenarios.

In addition to this, the Scheme has an allocation of c. 4% (as a % of total assets) to Global Small Cap equities, which brings the total equity allocation (including the synthetic equities) to 30%.

Manager	Asset Class	Target Allocation (%)
Schroders (Synthetic)	Global Developed Equities	8.5
	Global Developed Equities (GBP Hedged)	12.5
	Global Emerging Market Equities	5.0
Baillie Gifford (Physical)	Global Small Cap Equities	4.0
Total		**30.0**

An equity downside protection strategy has been designed to provide partial, but not complete, protection against extreme downside scenarios. To control the cost of the strategy, exposure to extreme events remains, although in such scenarios the protection strategy reduces the losses experienced, even if it does not offset them entirely.

7. Central Asset Reserve (CAR)

In addition to the above investment strategy, the Scheme also has holdings in two asset backed funding arrangements, referred to as CAR I and II. These assets are not considered to form part of the Scheme's formal investment strategy due to their unique structure and illiquid nature. The value of CAR I and II is, however, included in the overall value of the Scheme's assets when assessing the Scheme's funding level. As such, the CAR I and II provide additional security to the Scheme's financial status and this factor is considered by the Trustee when assessing the overall level of investment risk that it deems acceptable.

The Trustee has received legal advice to confirm that the holding in the CAR does not constitute an Employer Related Investment. The Trustee has received and considered investment advice regarding the suitability of the arrangement from an investment perspective.

8. Day to day management of the 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 themselves that the managers have the appropriate knowledge and experience for managing the Scheme's investments and that they are able to carry out their work competently.

The Trustee regularly reviews the continuing 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. However, any such adjustments would be done with the aim of ensuring the overall level of risk is consistent with the investment objectives.

9. Direction of Cash-flows & Rebalancing Policy

The Trustee monitors the allocation between the appointed managers and between asset classes on a regular basis to determine if any rebalancing is required.

The Trustee looks to invest any excess cash-flows (or make disinvestments – if required) in such a way to help maintain the Scheme's actual assets in relation to the target asset allocation to the extent possible, allowing for the timeliness of the cashflow requirements.

10. Expected return

The investment returns that the Trustee expects to achieve are those which are broadly in line with or above the returns of the respective market indices and performance targets against which the investment managers are benchmarked. Over the longer term, the Trustee expects to achieve an investment return in excess of the Scheme's Liability Benchmark Portfolio (an investible portfolio of fixed and index-linked gilts that seeks to hedge as far as is practical the interest rate and inflation sensitivities of the Scheme's liabilities).

11. Additional assets

The Scheme provides a facility for members to pay additional voluntary contributions (“AVCs”) to enhance their benefits at retirement. Members are offered some choice of arrangements in which to invest their AVC payments, in order to allow them to make investments which are consistent with their needs and reasonable expectations. The Trustee reviews the suitability and performance of the AVC arrangements on a regular basis.

12. Realisation of investments

The investment managers have discretion in the timing of realisation of investments and in considerations relating to the liquidity of those investments within parameters stipulated in the relevant appointment documentation and pooled fund prospectuses.

13. Investment manager fees

The investment managers are remunerated based on an agreed percentage of assets (or market exposure) basis, which are reviewed regularly.

14. Socially Responsible Investment & Corporate Governance

The Trustee believes that environmental, social, and corporate governance (ESG) factors may have a material impact on investment risk and return outcomes, and that good stewardship can create and preserve value for companies and markets as a whole. The Trustee also recognises that long-term sustainability issues, particularly climate change, present risks and opportunities that increasingly may require explicit consideration.

The Trustee expects the Scheme’s investment managers to evaluate ESG factors, including climate change considerations, when making investment decisions. The Trustee also expects the relevant investment managers to exercise voting rights and stewardship obligations attached to the investments, in accordance with their own corporate governance policies and current best practice, including the UK Corporate Governance Code and UK Stewardship Code.

The Trustee considers how ESG, climate change and stewardship is integrated within investment processes in appointing new investment managers and monitoring existing investment managers. Monitoring is undertaken on a regular basis and is documented periodically.

The Trustee has not set any investment restrictions on the appointed investment managers in relation to particular products or activities, but may consider this in future.

The Trustee does not explicitly consult members when making investment decisions.

15. Investment Manager Appointment, Engagement and Monitoring

Aligning manager appointments with investment strategy

The investment managers are appointed based on their capabilities and, therefore, their perceived likelihood of achieving the expected return and risk characteristics required for the asset class being selected for.

The Trustee looks to its investment consultant for their forward looking assessment of a manager's ability to outperform over a full market cycle. This view will be based on the Consultant's assessment of the manager's idea generation, portfolio construction, implementation and business management, in relation to the particular investment fund that the Scheme invests in. The Consultant's manager research ratings assist with due diligence and questioning managers during presentations to the Trustee and are used in decisions around selection, retention and realisation of manager appointments.

If the investment objective for a particular manager's fund changes, the Trustee will review the fund appointment, with the Consultant's assistance, to ensure it remains appropriate and consistent with the Trustee's wider investment objectives.

Some appointments are actively managed and the managers are incentivised through performance targets (an appointment will be reviewed following periods of sustained underperformance). The Trustee will review appropriateness of using actively managed funds (on an asset class basis) periodically, and receives updates on performance from the managers and Consultant on a quarterly basis.

Some appointments are segregated: the Trustee has specified criteria in the investment manager agreements for the respective manager to be in line with the Trustee's specific investment requirements. For example, the Trustee has appointed Schroders to manage the LDI mandate and equity downside protection mandates, which are tailored to the specific requirements of the Trustee.

As the Trustee invests in pooled vehicles they accept that they have no ability to specify the risk profile and return targets of the manager, but appropriate mandates can be selected to align with the overall investment strategy.

Evaluating investment manager performance

The Trustee considers the Consultant's assessment of how each investment manager embeds ESG into its investment process and how the manager's responsible investment philosophy aligns with the Trustee's responsible investment policy. This includes the investment managers' policy on voting and engagement. The Trustee will use this assessment in decisions around selection, retention and realisation of manager appointments.

The Trustee meets with each investment manager, on a regular basis, as deemed appropriate The Trustee can review the decisions made by the managers, including voting history (in respect of equities) and engagement activity, and can challenge such decisions to try to ensure the best long term performance over the medium to long term.

The Trustee reviews an annual stewardship monitoring report, which includes details of voting and engagement activities associated with each of the funds invested in.

The Trustee reviews the investment managers' compliance against the UK Stewardship Code on an annual basis.

Investment managers are aware that their continued appointment is based on their success in delivering the mandate for which they have been appointed to manage. If the Trustee is dissatisfied, then they will look to replace the manager.

Time horizon

The Trustee receives investment manager performance reports on a quarterly basis, which present performance information over 3 months, 1 year, 3 years and since inception. The Trustee reviews the performance of the investments on an absolute basis and relative to pre-defined benchmarks (over the relevant period) on a net of fees basis. The Trustee's focus is long-term performance but will put a manager 'on watch' if there are short-term performance concerns.

If a manager is not meeting its performance objectives, over sustained period of time, and after consideration of all relevant factors, the Trustee may take the decision to terminate the manager.

Portfolio turnover costs

The Trustee reviews portfolio turnover and associated transaction costs on an annual basis.

The Trustee will engage with a manager if portfolio turnover is higher than expected. This is assessed by comparing portfolio turnover across the same asset class, on a year-for-year basis for the same manager fund, or relative to the manager's specified portfolio turnover range in the investment guidelines or prospectus.

Duration of investment arrangements

The Trustee is a long-term investor and does not look to change the investment arrangements on a frequent basis.

There is no set duration for the manager appointments. The Trustee will retain an investment manager unless:

- There is a strategic change to the overall strategy that no longer requires exposure to that asset class or manager; or

- The manager appointment has been reviewed and the Trustee has decided to terminate the manager.

16. Review of this Statement

The Trustee will review this Statement at least once every three years or after a significant change in the investment policy has been determined. Any change to this Statement will only be made after having obtained and considered the written advice of someone who the Trustee reasonably believes to be qualified by their ability in and practical experience of financial matters and to have the appropriate knowledge and experience of the management of pension scheme investments.

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