

# Statement of Investment Principles – Edrington UK Distribution Limited Pension Scheme (September 2021)

## Introduction

- 1 This document is the Statement of Investment Principles (the ‘SIP’) made by the Trustees of the Edrington UK Distribution Limited Pension Scheme (the ‘Scheme’) in accordance with the requirements of Section 35 of the Pensions Act 1995 (as amended by the Pensions Act 2004 and regulations made under it).
- 2 The Trustees will review this SIP at least every three years and without delay after any significant change in investment policy. Before finalising this SIP, the Trustees took advice from a suitably qualified firm and consulted Edrington UK Distribution Limited (the ‘Company’). The ultimate power and responsibility for deciding investment policy, however, lies solely with the Trustees.

## Investment objectives

- 3 The Trustees have the following investment objectives:
  - The acquisition of suitable assets of appropriate liquidity which will generate income and capital growth to meet, together with new contributions from the Company, the cost of current and future benefits which the Scheme provides.
  - To limit the risk of the assets failing to meet the liabilities, both over the long-term and on a shorter-term basis.
  - To minimise the long term costs of the Scheme by maximising the return on the assets whilst having regard to the objective shown under the point above.

## Investment strategy

- 4 The Trustees have received advice to determine an appropriate investment strategy for the Scheme. The Trustees have a desire to diversify risk exposures and to manage its investments effectively.
- 5 The investment strategy makes use of three key types of investments:
  - a range of instruments that provide a broad match to changes in liability values;
  - a portfolio of secure income assets; and
  - a diversified portfolio of return-seeking assets.
- 6 The Trustees appointed an investment manager to manage the Scheme’s assets on a discretionary basis and to provide investment advisory services to the Trustees (the “Fiduciary Manager”). The balance within and between these investments will be determined from time-

to-time at the discretion of the Fiduciary Manager, with the objective of maximising the probability of achieving the Scheme's investment objective set by the Trustees. The Fiduciary Manager's discretion is subject to guidelines set by the Trustees within its Fiduciary Management Agreement (the "FMA"). In exercising its discretion, the Fiduciary Manager is required to act in accordance with the FMA and in doing so is expected to take into account the principles contained in this SIP (as far as reasonably practicable). This ensures appropriate incentivisation and alignment of decision-making with the Trustees' overall objectives, strategy and policies.

- 7 The Scheme will hold assets in cash and other money market instruments from time to time as may be deemed appropriate.
- 8 The Trustees will monitor the liability profile of the Scheme and will regularly review, in conjunction with the Fiduciary Manager and the Scheme actuary, the appropriateness of its investment strategy.
- 9 The expected return of all the Scheme's investments will be monitored regularly and will be directly related to the Scheme's investment objective.
- 10 The Trustees' policy is that there will be sufficient investments in liquid or readily realisable assets to meet cash flow requirements in foreseeable circumstances so that the realisation of assets will not disrupt the Scheme's overall investments, where possible.

## Investment managers

- 11 The Trustees have delegated investment manager selection, de-selection and the ongoing management of relationships with asset managers to the Fiduciary Manager subject to the guidelines set by the Trustees.
- 12 The Trustees consider the Fiduciary Manager's performance in carrying out these responsibilities as part of its ongoing oversight of the Fiduciary Manager. The Trustees expect the Fiduciary Manager to ensure that the investment portfolio, in aggregate, is consistent with the policies set out in this SIP, in particular those required under regulation 2(3)(b) of the Occupational Pension Schemes (Investment) Regulations (2005). The Trustees expect the Fiduciary Manager to check that the investment objectives and guidelines of pooled vehicles managed by investment managers are consistent with the Trustees' policies contained in this SIP.
- 13 In accordance with the Financial Services and Markets Act 2000, the selection of specific investments will be delegated to investment managers. The investment managers will provide the skill and expertise necessary to manage the investments of the Scheme competently.
- 14 The Trustees and Fiduciary Manager are not involved in the investment managers day-to-day method of operation and do not directly seek to influence attainment of their performance targets. However, the Fiduciary Manager may provide investment recommendations to the investment managers of certain pooled funds where it considers it appropriate. The Fiduciary Manager will maintain processes to ensure that performance and risk are assessed on a regular basis against measurable objectives for each investment manager, consistent with the achievement of the Scheme's long term objectives.
- 15 The Trustees expect the Fiduciary Manager to appoint investment managers with an expectation of a long-term partnership with the Trustees, which encourages active ownership of the Scheme's assets. When assessing an investment manager's performance, the Trustees

expect the Fiduciary Manager to focus on longer-term outcomes, commensurate with the Trustees' position as a long-term investor. Consistent with this view, the Trustees do not expect that the Fiduciary Manager would terminate an investment manager's appointment based purely on short term performance but recognise that an investment manager may be terminated within a short timeframe due to other factors such as a significant change in business structure or investment team. The Trustees adopt the same long-term focus as part of their ongoing oversight of the Fiduciary Manager.

- 16 For most of the Scheme's investments, the Trustees expect the Fiduciary Manager to appoint investment managers with a medium to long time horizon, consistent with that of the Scheme. In particular areas such as equity and credit, the Trustees expect the Fiduciary Manager to work with investment managers who will use their engagement activity to drive improved performance over medium to long term periods within the wider context of long-term sustainable investment. The Trustees note that the Fiduciary Manager may invest in certain strategies where such engagement is not deemed appropriate or possible, due to the nature of the strategy and/or the investment time horizon underlying decision making. The Trustees expect that the appropriateness of the Scheme's allocation to such mandates is determined in the context of the Scheme's overall objectives.
- 17 The Trustees have delegated responsibility for the selection, retention and realisation of investments to the Fiduciary Manager and in turn to the Scheme's investment managers. However, the Trustees and Fiduciary Manager recognise that an investment's long-term financial success is influenced by a range of financially material factors including environmental, social and governance (ESG) issues.
- 18 Consequently the Trustees (through the selection of the Fiduciary Manager with its approach to ESG issues, as set out below) seeks to be an active long-term investor. The Trustees' focus is explicitly on financially material factors. The Trustees' policy at this time is not to take into account non-financial matters.
- 19 The Fiduciary Manager has a dedicated Sustainable Investment resource and a network of subject matter experts. The consideration of ESG issues is fully embedded in the investment manager selection and portfolio management process, with oversight undertaken on an ongoing basis.
- 20 The Trustees expect the Fiduciary Manager to assess the alignment of each investment manager's approach to sustainable investment (including engagement) with its own before making an investment on the Scheme's behalf. The Trustees expect the Fiduciary manager to engage with the investment managers where the Fiduciary Manager considers this appropriate regarding their approach to stewardship with respect to relevant matters including capital structure of investee companies, actual and potential conflicts, other stakeholders and ESG impact of underlying holdings. In addition, the Trustees expect the Fiduciary Manager to review the investment managers' approach to sustainable investment (including engagement) on a periodic basis and engage with the investment managers to encourage further alignment as appropriate. Where an investment manager's processes are deemed insufficient by the Fiduciary Manager and the investment manager does not take steps to improve their approach, the investment manager's position in the portfolio may be reviewed and/or a decision may be taken not to proceed with an investment.
- 21 The Fiduciary Manager considers a range of sustainable investment factors, such as, but not limited to, those arising from ESG considerations, including climate change, in the context of a broader risk management framework. The degree to which these factors are relevant to any given strategy is a function of time horizon, investment style, philosophy and particular exposures which the Fiduciary Manager takes into account in the assessment.

- 22 The Fiduciary Manager encourages and expects the Scheme's investment managers to sign up to local or other applicable Stewardship Codes, in-keeping with good practice, subject to the extent of materiality for certain asset classes. The Fiduciary Manager itself is a signatory to the Principles for Responsible Investment (PRI) and the UK Stewardship Code and is actively involved in external collaborations and initiatives.
- 23 The Trustees' policy is to delegate responsibility for the exercising of rights (including voting rights) attaching to investments to the investment managers. The Fiduciary Manager has appointed Hermes EOS to undertake public policy engagement on its behalf as well as company-level engagement.
- 24 The Trustees expect the Fiduciary Manager to consider the fee structures of investment managers and the alignment of interests created by these fee structures as part of its investment decision making process, both at the initial appointment of an asset manager and on an ongoing basis. Investment managers are generally paid an ad valorem fee, in line with normal market practice, for a given scope of services which includes consideration of long-term factors and engagement. The Trustees expect the Fiduciary Manager to review and report on the costs incurred in managing the Scheme's assets regularly, which includes the costs associated with portfolio turnover. In assessing the appropriateness of the portfolio turnover costs at an individual manager level, the Trustees expect the Fiduciary Manager to have regard to the actual portfolio turnover and how this compares with the expected turnover range for that mandate.

## Other matters

- 25 The Scheme is a Registered Pension Scheme for the purposes of the Finance Act 2004.
- 26 The Scheme's AVC arrangement provides benefits with the value of members' funds being determined by the value of accumulated contributions adjusted for investment returns net of charges. In selecting appropriate investments, the Trustees are aware of the need to provide a range of investment options, which broadly satisfy the risk profiles of all members.
- 27 The Trustees recognise a number of risks involved in the investment of the Scheme's assets, and, where applicable, monitors these risks in conjunction with the Fiduciary Manager.

### **Solvency risk and mismatch risk:**

- are measured through a qualitative and quantitative assessment of the expected development of the funding level.
- are managed through the development of a portfolio consistent with delivering the Scheme's investment objective.

### **Investment Manager risk:**

- is measured by the expected deviation of the return relative to the benchmark set.
- is managed by considering when to employ active versus passive management given prospective net of fees returns, consideration of the appropriate amount of the Scheme to allocate to any active portfolios and by monitoring the actual deviation of returns relative to the benchmark and factors supporting the managers' investment process.

### **Liquidity risk:**

- is measured by the level of cash flow required by the Scheme over a specified period.
- is managed by the Scheme's administrators assessing the level of cash held in order to limit the impact of the cash flow requirements on the investment policy and through holding assets of appropriate liquidity.

**Currency risk:**

- is measured by the level of exposure to non-Sterling denominated assets.
- is managed by the implementation of a currency hedging programme (carried out within some of the pooled investment vehicles) which reduces the impact of exchange rate movements on the Scheme's asset value.

**Custodial risk:**

- is addressed through investment in pooled vehicles, with the investment managers being responsible for selection of suitable custodians. In addition the Scheme's global custodian, is responsible for sweeping un-invested cash balances into pooled cash funds, which will be managed by an investment manager who, in line with other investment managers of pooled vehicles for the Scheme is responsible for selecting the custodian for the cash funds.

**Interest rate and inflation risk:**

- are measured by comparing the likely movement in the Scheme's liabilities and assets due to movements in inflation and interest rates.
- are managed by holding a portfolio of matching assets (physical bonds and/or derivatives) that enable the Scheme's assets to broadly match movements in the value of the liabilities due to inflation and interest rates.

**Political risk:**

- is measured by the level of concentration of any one market leading to the risk of an adverse influence on investment values arising from political intervention.
- is managed by regular reviews of the actual investments relative to policy and through the level of country diversification within the policy.

**Sponsor risk:**

- is measured by receiving regular financial updates from the Company and periodic independent covenant assessments.
- is managed through an agreed contribution and funding schedule.

**Derivatives risk:**

- Counterparty risk – this risk is mitigated through collateral management, diversifying exposure across counterparties, and the use of robust derivatives documentation.
- Basis risk – the returns from backing assets used to meet the payable leg of a derivative contract may not match exactly. This risk is addressed through the investment policy adopted by the Trustees for the backing assets and the investment managers' asset management capabilities.

- Liability risk – pension liabilities can only be estimated and there is a risk of divergence between the performance of the derivatives and the actual value of the liabilities (for example, due to changes in assumptions or demographics). This risk is mitigated by updating the liability hedging benchmark at appropriate regular intervals.
- Legal and operation risk – the successful operation of derivatives depends on the various legal documents governing the derivative contracts and the correct completion of some operational tasks. The Trustees take appropriate advice when putting in place legal documents, reviewing legal documents already in place and appointing and monitoring providers capable of carrying out the required operational tasks.
- Leverage risk – the level of leverage may rise to an unmanageable or unsustainable level. This risk is mitigated by:
  - The monitoring and rebalancing of leverage levels by the investment manager within and pooled Liability Driven Investment funds
  - A sufficient and appropriately liquid portfolio being maintained to meet any cash injections required
- The Trustees are also aware of the risks relating to the initial terms of entry in derivative contracts (for example, purchasing the contracts at a competitive price) and the valuation of the derivatives on an ongoing basis. With the help of their advisors, the Trustees monitor these positions on a regular basis.