

## The North British Distillery Company Limited Pension Scheme

### Statement of Investment Principles

#### **Background**

This Investment Statement sets out the principles governing decisions about investments for The North British Distillery Company Limited Pension Scheme (“the Scheme”) to meet the requirements of The Pensions Act 1995, as amended by the Pensions Act 2004, and The Occupational Pension Schemes (Investment) Regulations 2005. It is subject to periodic review by the Trustees at least every three years and more frequently as appropriate.

In preparing this Statement, the Trustees have consulted with the principal employer (The North British Distillery Company Ltd) and have taken professional advice from their Investment Consultant (KPMG).

The Trustees are aware of the Myners principles, which set out a code of conduct for investment decision making and governance, and have reviewed their responsibilities and activities in the context of these principles.

#### **Investment objective**

The Scheme closed to new entrants, but remained open to future benefits accrual on 1 January 2008. Subsequently, on 31 December 2014, the Scheme closed to future benefit accrual.

The primary objective of the Scheme is to provide pension and lump sum benefits for the current members on their retirement, and/or benefits on death, before or after retirement for their dependents, on a defined benefit basis. There is also a longer term aspiration of the Scheme achieving a full insurance buyout at some point in the future.

The Trustees’ medium term objective is to reach and maintain a funding position of 100% of technical provisions – such a target being consistent with the strength of the employer covenant and the Trustees’ investment risk tolerance. The long term funding objective is to reach a funding position such that all Members’ benefits can be secured within an insurance contract (i.e. reach full funding on an insurance buy-out basis). The Trustees also consider the Scheme’s funding position on other relevant bases for valuation and accounting. Funding positions are monitored regularly by the Trustees and formally reviewed at each triennial valuation, or more frequently as required by the Pensions Act 2004.

#### **Investment strategy**

The Trustees have translated their objectives into a suitable strategic asset allocation benchmark for the Scheme (the “strategic benchmark”). All day to day investment decisions have been delegated to a number of authorised investment managers. The strategic benchmark (set out in the Appendix A) is reflected in the choice and mix of funds in which the Scheme invests. The Scheme benchmark is

consistent with the Trustees' views on the appropriate balance between seeking an enhanced long term return on investments and accepting greater short-term volatility and risk.

The investment strategy takes due account of the maturity profile of the Scheme, together with the level of disclosed surplus or deficit (relative to the Technical Provisions and Gilts, as a proxy for an insurance buy-out, funding basis). The Trustees monitor fund performance relative to their agreed asset allocation benchmark. It is intended that investment strategy will be reviewed at least every three years following actuarial valuations of the Scheme, and will normally be reviewed annually. In monitoring performance and setting strategy, the Trustees seek written advice from a suitably qualified person as required.

The Scheme has exposure to both public and private investment markets, and employs a mix of both active and passive management. The investment management structure of the Scheme is discussed in more detail in the Myners Code Adherence document.

### **Choosing investments**

The Trustees, after seeking appropriate investment advice, have chosen the investment managers to implement the agreed strategy. However, specific investment choices have been delegated to these managers subject to their respective benchmarks and asset guidelines. The managers invest in their in-house pooled funds in order to achieve the desired asset allocation.

The Trustees have appointed Baillie Gifford & Co ("Baillie Gifford"), Legal and General Investment Management ("LGIM"), M&G Investment Management ("M&G"), Apollo Global Management ("Apollo") and CQS Investment Management ("CQS") as investment managers. Each manager is authorised under the Financial Services and Markets Act 2000 to undertake investment business.

With the exception of the LGIM index-linked bond portfolios and liability driven investment ("LDI") funds, assets are managed on an active basis: that is, the managers seek to exceed the performance of the benchmark index. LGIM manages the index-linked bond portfolio and LDI fund assets on behalf of the Trustees on a passive basis, whereby the objective is to match, rather than exceed, the performance of the nominated benchmark.

The Trustees consider the different managers and asset classes described above, and the balance between them, to be suitable given the circumstances of the Scheme. This combination results in a diversified mix of assets, geographic spread and number of investments held. An analysis of Scheme investments by fund manager and asset class, as at 30 June 2019, is set out in Appendix A.

The Scheme may invest in quoted and unquoted securities of UK and overseas markets including equities, fixed interest and index linked bonds, cash, property, either directly or through pooled funds. The Scheme also makes use of derivatives and contracts for difference for the purpose of efficient portfolio management or to hedge specific risks. The Trustees consider all of these classes of investment to be suitable in the circumstances of the Scheme.

A summary of the policies the Trustees' have in place in relation to the investment management arrangements for the Scheme are summarised in Appendix C.

## **Risk**

The Trustees analyse the level of risk and the drivers of risk with the Scheme's investment strategy in detail when reviewing the Scheme's investment strategy.

On an ongoing basis, the Trustees monitor risk in two ways. As indicated above, they have established a strategic asset allocation benchmark for the Scheme (given in the Appendix A). They assess risk relative to that benchmark by monitoring the Scheme's asset allocation and investment returns relative to the benchmark. They also assess risk relative to liabilities by monitoring the delivery of benchmark returns relative to liabilities.

The Trustees provide a practical constraint on Scheme investments deviating greatly from the Trustees' intended approach by adopting a specific asset allocation benchmark and by monitoring the underlying asset class weights relative to this benchmark on a regular basis.

The investment strategy is suitably diversified, with the balance of different asset classes and investment managers mitigating the impact (at the aggregate level) of underperformance by any single manager.

The Scheme also employed LGIM to operate an implementation framework for the Scheme's liability hedging strategy, in order to reduce interest rate and inflation risks. The framework employed a combination of market based and time based implementation triggers to increase hedge levels from a target of 28% in May 2015 to 60% in early 2017. The pace of the time-based hedge increase was increased in Q1 2016 in order to shorten the expected timeframe to achieve the target 60% hedge. Subsequently at the meeting held in March 2017, the Trustees agreed to rebalance the hedge, following receipt of updated liability cashflow information, to an updated target of 70%, and again in July 2019 to an updated target of 80%.

Further information on the risks, financially material considerations and non-financial matters that have been considered when deciding on the Scheme's investment strategy are set out in Appendix B.

## **Expected return on investments**

The investment strategy aims to achieve a return on Scheme assets which, taken in conjunction with contributions, is sufficient, over time, to match growth in the Scheme's pension liabilities.

The overall performance target (i.e. the expected return on the Scheme's investments) has been set at +2.9% over gilts.

## **Realisation of investments**

The Trustees operate a bank account for daily cash flow needs and a formal cashflow policy is in place.

The significant majority of the Scheme's investments may be realised quickly if required. The diversified credit allocation, which has a target weight of 6% within the strategic benchmark, has a monthly dealing date. The semi-liquid credit allocation, which has a target weight of 26%, is split with a 7.5% allocation to

Apollo with the remainder, 18.5% to CQS. The CQS fund has monthly liquidity available, whilst the Apollo fund has quarterly liquidity available. All other asset allocations can be realised either daily or weekly.

### **Environmental, Social and Governance considerations**

The Trustees recognise that environmental, social and governance (“ESG”) considerations are among the factors which investment managers will take into account, where relevant, when selecting investments for purchase, retention or sale. The managers have been delegated by the Trustees to act accordingly in this respect

The Trustee’s investment managers provide annual reports on how they have engaged with issuers regarding ESG considerations. The Trustees also receive information from their investment advisers on the investment manager’s approach to engagement. In the case where managers have not acted in accordance with their policies and frameworks or if the manager’s policies are not in line with the Trustees’ policies with regards to ESG factors, there is scope for further monitoring and engagement by the Trustees beyond the annual reports and regular updates.

LGIM adopts an index tracking basis for its index-linked bond mandate which largely requires full replication of the index in which it invests; consequently, there is little discretion over the choice of security in which investment is made.

LGIM, Baillie Gifford, and M&G have adopted the UN Principles of Responsible Investment (“UNPRI”). CQS are not currently a signatory of the UNPRI, however, they recognise the importance of Socially Responsible investing and are currently evaluating the UNPRI with a view to adopting. Apollo has adopted the American Investment Council’s Principles of Responsible Investment (“AICPRI”).

### **Exercise of voting rights**

The Trustees have delegated the exercise of voting rights to the investment managers on the basis that voting power will be exercised by them with the objective of preserving and enhancing long term shareholder value. Accordingly, the managers have produced written guidelines of their process and practice in this regard. The managers are encouraged to vote in line with their guidelines in respect of all resolutions at annual and extraordinary general meetings of companies.

### **Additional voluntary contributions (AVCs)**

A number of members have made AVC contributions. However, the AVC arrangement is now closed to all members, following cessation of accrual within the Scheme from 31 December 2014.

Signed for and on behalf of the Trustees of the  
The North British Distillery Company Limited Pension Scheme  
October 2019.

**Juniper Partners Limited**  
Trustee

**ACMCA Limited**  
Trustee

**Alan Kilpatrick**  
Trustee

**Fraser MacDonald**  
Trustee

**David Rae**  
Trustee

**William Copland**  
Trustee

**Appendix A**

Asset split by fund manager (as at 30 June 2019)

<b>Fund Manager</b>	<b>£m</b>	<b>%</b>	<b>Mandate</b>	<b>Assets</b>
L&G	37.3	31.7	Passive	Index-Linked Gilts and Liability Driven Investment Funds.
Baillie Gifford	43.2	36.7	Active	Global Equities and Diversified Growth
M&G	5.1	4.3	Active	Diversified Credit
Apollo	9.5	8.0	Active	Semi-liquid Credit
CQS	22.0	18.7	Active	Semi-liquid Credit
Trustee Bank Account	0.7	0.6	n/a	Cash
<b>Total</b>	<b>117.8</b>	<b>100.0</b>		

Figures may not sum due to rounding

Asset split by asset class (as at 30 June 2019)

<b>Asset Class</b>	<b>Strategic Benchmark (%)</b>	<b>Actual (%)</b>	<b>Expected Return<sup>1</sup> (%)</b>	<b>Volatility<sup>1</sup> (%)</b>
Global Equity	10.0	10.9	4.5	20.5
Diversified Growth	30.0	25.7	3.5	12.5
Diversified Credit	6.0	4.3	2.5	11.0
Index Linked Gilts & LDI	28.0	31.7	0.0	11.1
Semi-liquid Credit	26.0	26.7	3.5	9.0
Cash	-	0.6	0.0	0.9
<b>Total</b>	<b>100.0</b>	<b>100.0</b>	<b>2.9</b>	<b>8.9</b>

<sup>1</sup> Expected return and total volatility assumptions quoted relative to Gilts and based on KPMG's central assumptions as at 30 June 2019  
Figures may not sum due to rounding

## Gilt and Liability Driven Investment split by fund (as at 30 June 2019)

Asset Class	Actual (%)	Leverage
Over 5yr Index Linked Gilts Fund	16.4	1.0
Over 15yr Index Linked Gilts Fund	4.5	1.0
2030 Leveraged Index Linked Gilt	8.0	3.8
2034 Leveraged Index Linked Gilt	4.0	4.2
2037 Leveraged Index Linked Gilt	5.4	3.1
2038 Leveraged Gilt Fund	10.0	3.2
2042 Leveraged Index Linked Gilt	7.4	2.6
2045 Leveraged Gilt Fund	3.4	3.6
2047 Leveraged Index Linked Gilt	3.3	3.0
2049 Leveraged Gilt Fund	12.8	2.8
2050 Leveraged Index Linked Gilt	4.3	2.4
2055 Leveraged Index Linked Gilt	10.1	2.0
2062 Leveraged Index Linked Gilt	5.4	1.4
2068 Leveraged Index Linked Gilt	5.1	1.5
<b>Total</b>	<b>100.0%</b>	<b>2.4</b>

Figures may not sum due to rounding

Leverage is defined as notional exposure (£gilts)/physical exposure (£gilts+£cash)

## Managers Fees split by fund (as at 30 June 2019)

Manager	Fund	Fees (p.a.)
Baillie Gifford	Global Alpha Fund	0.65%
Baillie Gifford	Diversified Growth Fund	0.65%
M&G	Alpha Opportunities Fund	0.50%
L&G	Over 5yr Index-Linked Gilts; Over 15yr Index-Linked Gilts	Tiered (ranging from 0.03% to 0.10%)
L&G	LDI Funds	0.24%
Apollo	Total Return Fund	0.68%
CQS	Multi Asset Fund	0.65%

## Appendix B – Risks, Financially Material Considerations and Non-Financial matters

A non-exhaustive list of risks and financially material considerations that the Trustees have considered and sought to manage is shown below.

The Trustees of the Scheme seek to adopt an integrated risk management approach. The three key risks associated in this framework and how they are managed are stated below:

Risks	Definition	Policy
Investment	The risk that the Scheme's position deteriorates due to the assets underperforming.	<ul style="list-style-type: none"> <li>Selecting an investment objective that is achievable and is consistent with the Scheme's funding basis and the principle employer's covenant strength.</li> <li>Investing in a diversified portfolio of assets.</li> </ul>
Funding	The extent to which there are insufficient Scheme assets available to cover ongoing and future liability cash flows.	<ul style="list-style-type: none"> <li>Funding risk is considered as part of the investment strategy review and the actuarial valuation.</li> <li>The Scheme's Trustees will agree an appropriate basis in conjunction with the investment strategy to ensure an appropriate journey plan is agreed to manage funding risk over time.</li> </ul>
Covenant	The risk that the sponsoring company becomes unable to continue providing the required financial support to the Scheme	<ul style="list-style-type: none"> <li>When developing the Scheme's investment and funding objectives, the Scheme's Trustees take account of the strength of the covenant ensuring the level of risk the Scheme is exposed to is at an appropriate level for the covenant to support.</li> </ul>

The Scheme is exposed to a number of underlying risks relating to its investment strategy. These are summarised below:

Risk	Definition	Policy
Interest rates and inflation	The risk of mismatch between the value of the Scheme's assets and present value of liabilities from changes in interest rates and inflation expectations.	To hedge 80% of these risks on a Gilts flat liability basis.
Liquidity	Difficulties in raising sufficient cash when required without adversely impacting the fair market value of the investment.	To maintain a sufficient allocation to liquid assets so that there is a prudent buffer to pay members benefits as they fall due (including transfer values) and provide collateral to the LDI manager.
Market	Experiencing losses due to factors that affect the overall performance of the financial markets.	To remain appropriately diversified and hedge away any unrewarded risks, where practicable.
Credit	Default on payments due as part of a financial security contract.	To diversify this risk by investing in a range of credit markets across different geographies and sectors. To appoint investment managers who



		actively manage this risk by seeking to invest only in debt securities where the yield available sufficiently compensates the Scheme's investors for the risk of default.
Environmental, Social and Governance	Exposure to Environmental, Social and Governance factors, including but not limited to climate change, which can impact the performance of the Scheme's investments.	To appoint managers who satisfy the following criteria, unless there is a good reason why the manager does not satisfy each criteria: 1. Responsible Investment ('RI') Policy / Framework 2. Implemented via Investment Process 3. A track record of using engagement and any voting rights to manage ESG factors 4. ESG specific reporting 5. UN PRI Signatory The Trustees monitor the managers on an ongoing basis.
Currency	The potential for adverse currency movements to have an impact on the Scheme's investments.	Allow the Scheme's active managers who invest in overseas securities the flexibility to hedge overseas currency exposure to manage risk.
Non-financial	Any factor that is not expected to have a financial impact on the Scheme's investments.	Non-financial matters are not taken into account in the selection, retention or realisation of investments.

### Appendix C – Investment Management Arrangement Policies

The Trustees have the following policies in relation to the investment management arrangements for the Scheme:

<p><b>How the investment managers are incentivised to align their investment strategy and decisions with the Trustees' policies.</b></p>	<p>As the Scheme is invested in pooled funds, there is not scope for these funds to tailor their strategy and decisions in line with the Trustees' policies. However, the Trustees invest in a portfolio of pooled funds that are aligned to the strategic objective.</p>
<p><b>How the investment managers are incentivised to make decisions based on assessments of medium to long-term financial and non-financial performance of an issuer of debt or equity and to engage with them to improve performance in the medium to long-term.</b></p>	<p>The Trustees' review the investment managers' performance relative to medium and long-term objectives as documented in the investment management agreements.</p> <p>The Trustees monitor the investment managers' engagement and voting activity on an annual basis as part of their ESG monitoring process.</p>
<p><b>How the method (and time horizon) of the evaluation of investment managers' performance and the remuneration for their services are in line with the Trustees' policies.</b></p>	<p>The Trustees' review the performance of all of the Scheme's investments on a net of cost basis to ensure a true measurement of performance versus investment objectives.</p> <p>The Trustees evaluate performance over the time period stated in the investment managers' performance objective, which is typically 3 to 5 years.</p>
<p><b>The method for monitoring portfolio turnover costs incurred by investment managers and how they define and monitor targeted portfolio turnover or turnover range.</b></p>	<p>The Trustees do not directly monitor turnover costs. However, the investment managers are incentivised to minimise costs as they are measured on a net of cost basis.</p>
<p><b>The duration of the Scheme's arrangements with the investment managers</b></p>	<p>The duration of the arrangements is considered in the context of the type of fund the Scheme invests in.</p> <ul style="list-style-type: none"> <li>○ The Scheme does not currently invest in closed ended funds.</li> <li>○ For open ended funds, the duration is flexible and the Trustees will from time-to-time consider the appropriateness of these investments and whether they should continue to be held.</li> </ul>