Stewart Hughes Ltd No.2 Retirement Benefits Scheme

Statement of Investment Principles

September 2020

Contents

Introduction

The law requires the Trustee Directors to produce formal "Statement of Investment Principles" for the Scheme's default arrangement and any other investment options. These Statements set out what the Trustee Directors aim to achieve with the investment options and their investment policies which guide how members' money is invested.

This document forms the Statement of Investment Principles for the Stewart Hughes Ltd. No 2 Retirement Benefits Scheme (the "Scheme"). The Statement must cover a number of technical points to comply with legislation as well as meet the expectations of the Pensions Regulator and needs of the Scheme's Auditors which, as far as possible, are shown separately in "for the record" boxes.

The Trustee Directors will publish the Statement of Investment Principles from 1 October 2019 and a statement each year from 1 October 2020 describing how this Statement has been followed in the last year.

Statement of Investment Principles

The aspects covered by this Statement of Investment Principles include the:

1 Statement of the aims and objectives for the default arrangement*;

2 Statement of investment beliefs, risks and policies**.

The Statement of Investment Principles for the Scheme's default arrangement *** comprises items 1 and 2.

Appendices

A. Investment implementation for the default arrangement;

For the record

* In accordance with Regulation 2A(1) of the Occupational Pension Schemes (Investment) Regulations 2005.

** In accordance with Regulation 2 of the Occupational Pension Schemes (Investment) Regulations 2005 as modified by subsequent Regulations and section 35 of the 1995 Act.

*** As required by the Occupational Pension Schemes (Charges and Governance) Regulations 2015

The Trustee Directors have taken proper written advice and consulted the Employer in the preparation of these Statements of investment Principles.

These Statements will be reviewed at least every three years or more frequently as required by the Regulations.

For and on behalf of the Trustee Directors of the Scheme

Name	Signed	Date
Mark Elborne	*ME*	29 September 2020

1 Statement of the aims and objectives for the default arrangement

Default Arrangement

The Scheme is designated as a qualifying workplace pension scheme for automatic enrolment purposes, therefore it is required to have a default fund. The Scheme only has one with-profits fund, which members are automatically allocated to, which is therefore the default arrangement. This is the only investment fund associated with the Scheme.

The main objective of the fund is to help deliver good member outcomes at retirement.

The default arrangement was set up many years ago with the then Scottish Mutual Assurance Limited. It is a traditional With-Profits arrangement and is now managed by Phoenix Life Limited. The arrangement has inherent investment guarantees and aims to provide a pension (or a lump sum) for members at retirement. The arrangement is managed consistently with the Principles and Practice of Financial Management as set out by Phoenix Life Limited in relation to ex-Scottish Mutual Assurance Limited With-Profits arrangements.

The expected levels of investment returns (after the deduction of charges) and risks for the fund used are consistent with the Trustee Directors' objectives for the default arrangement and consistent with a With-Profits arrangement which includes significant investment guarantees to the members. The expected investment returns and approach to managing investment risks including financially material considerations such as climate change are described in Section 2.

Full details of the current default arrangement are given in appendix A.

2 Statement of investment beliefs, risks and policies

Introduction

This Statement sets out the investment beliefs and policies which guide the Trustee Directors' decision making.

For the record

This Statement of investment beliefs, risks and policies should be read in conjunction with the Statements of the aims and objectives for both default arrangement. Collectively, these respectively form the Statements of Investment Principles for the Scheme and the default arrangement.

This Statement of investment beliefs has been prepared in accordance with the Occupational Pension Scheme (Investment) Regulations 2005 as amended by the Pension Protection Fund (Pensionable Service) and Occupational Pension Schemes (Investment and Disclosure) (Amendment and Modification) Regulations 2018 and the Occupational Pension Schemes (Investment and Disclosure) Regulations 2019.

Risks

Principal investment risks

The Trustee Directors believe that the three principal investment risks most members will face are:

1) Inflation risk – investment returns over members' working lives may not keep pace with inflation and, as a result, do not produce adequate retirement benefits.

Further from retirement, this risk should be countered by funds investing in equities and other growth orientated assets which are expected to produce returns well in excess of inflation over the longer term. Approaching retirement, the impact of this risk needs to be balanced against the other main risks members face.

2) Benefit conversion risk – investment conditions just prior to retirement may increase the cost of turning members' fund values into retirement benefits.

For members taking cash at retirement, funds investing in cash deposits and other short-term interest-bearing investments provide a high degree of (but not complete) capital security. Funds investing in a mix of different assets are expected to be broadly suitable for members planning income drawdown during retirement. For members buying an annuity at retirement, the value of funds investing in longer-dated bonds may be expected to broadly follow changes in annuity rates caused by long-term interest rates.

3) Volatility/Market risk – falls in fund values prior to retirement lead to a reduction in retirement benefits.

Funds investing in bonds or a mix of assets or investment techniques intended to manage short-term risks may be expected to be subject to lower levels of short-term fluctuations in values - although there may be occasions when this does not hold good.

Other investment risks

The Trustee Directors believe that other investment risks members may face include:

Active management risk – a fund manager's selection of holdings may not lead to investment returns in line with the fund's objectives and investment markets generally.

Currency risk – changes in exchange rates will impact the values of investments outside the UK when they are being bought or sold.

Interest rate risk – the value of funds which invest in bonds will be affected by changes in interest rates.

Default risk – for bond funds (where money is lent in return for the payment of interest), the company or government borrowing money fails to pay the interest due or repay the loan.

Liquidity risk – funds which invest in assets which cannot be easily bought or sold (such as property) may at times not be able to accept new investments or disinvestments of existing holdings.

Counterparty risk – the financial institutions holding a fund's assets may get into financial difficulties leading to a reduction in a fund's value.

Market risks - Shifts in market sentiment (for example, in response to economic news or geopolitical events) or momentum in general market trading can lead to widespread changes and/or volatility in asset values over the short-term.

Environmental, Social and Governance (ESG) risks – the extent to which ESG issues are not reflected in asset prices and/or not considered in investment decision making leading to underperformance relative to expectations.

Climate risk - The extent to which climate change causes a material deterioration in asset values as a consequence of factors including, but not limited to: policy change, physical impacts and the expected transition to a low-carbon economy.

Managing risks

Principal investment risks

The With-Profits arrangement, managed by Phoenix Life Limited, manages the three main investment risks. The fund seeks to provides a level of guarantee and additional return that, although not guaranteed, would be expected in total to deliver a return commensurate with inflation over the long term. The With-Profits arrangement is managed so to smooth the returns to members so ensuring members are not exposed to wide fluctuations in investment markets close to retirement. The With-Profits fund is also invested significantly in fixed interest instruments consistent with targeting a pension income in retirement.

Other investment risks

Trustee Directors delegate the management of the other risks, including ESG and climate change risks to Phoenix Life Limited who manage these risks in line with their Principles and Practices of Financial Management.

Financially material considerations

The Scheme uses a single With-Profits arrangement with Phoenix Life Limited and expects the fund manager to take financially material considerations into account when selecting which companies and markets to invest in. The Trustee Directors recognise that the consideration of financially material factors over the appropriate time horizon of the investments, including ESG factors, is relevant at different stages of the investment process. The Trustee Directors further recognise that the financial materiality of any factor, including ESG factors, is context specific and that whilst some factors may be relevant to certain stocks/assets, they may not be relevant to others. The Trustee Directors will consider such factors in the development and implementation of their investment arrangements, for the purposes of determining the selection, retention and realisation of investments, where there is sufficient data or evidence to allow them to systematically do so. Where there is not sufficient data or evidence, they will require that their investment manager ensures it takes such considerations into account within its decision making. The Trustee Directors have explicitly acknowledged the relevance of or ESG factors in framing their investment beliefs and these beliefs are reflected in the principles set out below and the broader implementation of strategy.

Expected returns on investments

The Trustee Directors believe that it is important to balance investment risks with the likely long-term returns from different types of assets used in funds (taking the funds' costs and charges into account).

Asset class	Expected long-term investment returns relative to inflation	Expected shorter- term volatility in fund values
Equities (i.e. company shares)	Strong return relative to inflation	Most volatile in the short-term
Property (e.g. offices, shops and warehouses)	Positive, but lower than equities	Lower than equities
Corporate Bonds (i.e. loan stocks issued by companies)	Positive, but lower than equities and property	Lower than equities or property
Fixed Interest Government Bonds (e.g. UK Gilts)	Positive, but lower than equities, property or corporate bonds	Lower than equities, property or corporate bonds
Index-Linked Government Bonds (e.g. UK Index-Linked Gilts	In line with inflation	Lower than equities, property or corporate bonds
Cash (and other short-term interest-bearing investments)	Return may not keep pace with inflation	Minimal with high degree (but not complete) of capital security

Long-dated Bonds (e.g. UK Gilts and Corporate Bonds with a duration of 15 years or more) – should give fund values which move broadly in line with the financial factors influencing annuity rates.

Responsible Investment (i.e. funds selecting assets to mitigate ESG and/or climate change risks) – the strategy of these funds is expected to give a better risk adjusted return over the long-term than the broader market for the type of assets involved (e.g. equities).

Investment beliefs

The Trustee Directors' investment decisions are made in the context of their investment beliefs that:

- Managing the principal investment risks is the most important driver of good long-term member outcomes;
- Investment markets may not always behave in line with long-term expectations during the shorter-term;
- As the Scheme invests for members over the long-term, financially material considerations including the impact of climate change will have a bearing on funds' expected levels of risk and return;
- Taking investment risk is usually rewarded in the long term;
- Investment risks can be reduced by spreading investments both within and across asset classes;
- Charges and costs (levied by fund manager and platform providers) can have a material effect on net returns.

Types of funds used

Delegation of investment decisions

The Scheme uses a single With-Profits arrangement provided by Phoenix Life Limited. and have delegated day to day investment decisions including the management of financially material considerations to Phoenix Life Limited's fund manager.

Manager incentives

The expenses of managing the With-Profits arrangement are taken off the investment return before bonuses are added to the member's policy. The management and deduction of expenses is set out in the Principles and Practices of Financial Management.

There is also an annual policy charge payable by the employer.

When selecting funds, the Trustee Directors will ask their investment advisor to consider the investment manager's remuneration strategies and appropriateness of each fund's investment guidelines to ensure that there is no inducement or scope to take an undue level of risk and that the investment manager will act in line with the interests of the Scheme's members.

In accordance with the 2015 Regulations, the Trustee Directors conduct an annual Value for Members assessment and will take action should the provider be found to be giving poor value. In addition, in accordance with guidance from the Pensions Regulator, the Trustee Directors will periodically review the Scheme's choice of provider to ensure their charges and services remain competitive. The Trustee Directors believe that these steps are the most effective way of incentivising the provider to deliver Value for Members, of which investment management charges and investment performance are key considerations.

The Trustees also undertake a review at least every three years in which the appropriateness of the investment options and the suitability of the Scheme's investment management arrangements are considered.

The Trustee Directors monitor the performance of the fund against its's performance target on a rolling annual basis. A material deviation from performance and risk targets or approach to portfolio management is likely to result in the fund being formally reviewed.

Portfolio turnover

The Trustee Directors do not expect the investment manager to take excessive short-term risk and will monitor the fund performance against objectives on a short, medium and long terms basis.

When selecting actively managed funds, the Trustee Directors will consider, with the help of their investment advisers, the expected level of turnover commensurate with a fund's investment objectives, the investment manager's investment processes and the nature of the fund's assets.

Where a fund has significantly under or outperformed its benchmark, the Trustee Directors will seek to ascertain where necessary whether higher or lower than normal turnover has been a contributory factor. The Trustees will challenge the platform provider and/or investment manager if there is a sudden change in portfolio turnover or if the level of turnover seems excessive.

Portfolio duration

The Trustee Directors recognise the long-term nature of defined contribution pension investments and chooses funds which are expected to deliver sustainable returns over the Scheme members' investment horizon. The Trustee Directors will carry out necessary due diligence on the underlying investment decision making process, to ensure the manager makes investment decisions over an appropriate time horizon aligned with the objectives for the related investment option.

The Trustee Directors expect that each fund will be used for at least three years, this being the period over which performance of the fund can be appropriately evaluated and the costs of change amortised, although all funds are subject to ongoing review against various financial and non-financial metrics in addition to their continued appropriateness within the investment strategy.

Security of assets

The funds are provided through a policy of insurance. As a result, the value of the funds may be affected in the event of the provider getting into financial difficulties. The Trustee Directors periodically review the credit rating of Phoenix Life Limited.

Realisation of investments

The Trustee Directors understands that the nature of a With-Profits arrangement means that members may potentially lose guarantees and not maximise their potential outcome from the arrangement if the policy is cashed in early. However, the Trustee Directors also acknowledge that members can surrender their policy and receive a fair value for that policy in the event of surrendering the policy in advance of the agreed target benefit date. The approach to surrender and the policy followed is set out by Phoenix Life Limited in their Principles and Practices of Financial Management. Furthermore, the types of investment that Phoenix Life Limited invest in within the With-Profits arrangement are expected to be compromised mainly of liquid assets (e.g. equities and bonds) that can be realised within a reasonable timescale.

Balance of investments

Overall, the Trustee Directors believe that the Scheme's With-Profits investment option invests in a balance of investments and is appropriate for managing the risks typically faced by members and also consistent with a typical With-Profits arrangement.

Stewardship

The Trustee recognises that stewardship encompasses the exercise of voting rights, engagement by and with the With-Profits provider with the underlying investment companies.

Members' financial interests

The Trustee Directors expect that the With-Profits provider will have the members' financial interests as their first priority when choosing investments.

Conflicts of interest

When given notice the Trustees will consider the impact of any conflicts of interest arising in the management of the funds used by the Scheme.

Responsibility for investment decisions has been delegated to the investment manager which includes consideration of the capital structure of investments and the appropriateness of any investment made. Where the manager is investing in new issuance, the Trustee Directors expect the investment manager to engage with the issuer about the terms on which capital is issued and the potential impact on the rights of new and existing investors.

The Trustee Directors will consider any conflicts of interest arising in the management of the funds used by the Scheme and will ensure that each investment manager has an appropriate conflicts of interest policy in place. The Investment manager is required to disclose any potential or actual conflict of interest [in writing] to the Trustee.

Voting and engagement

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

The Trustee Directors have adopted a policy of delegating voting decisions on stocks to the With-Profits provider and underlying fund manager on the basis that voting power will be exercised by them with the objective of preserving and enhancing long term shareholder value. The fund manager is expected to exercise the voting rights attached to individual investments in accordance with their own house policy.

Monitoring

The Trustee Directors will also periodically review the fund manager's voting patterns and may also monitor voting on particular companies or issues affecting more than one company.

Non-financial factors

The Trustee Directors have considered and recognise that some members may have strong personal views or religious convictions that influence where they believe their savings should, or should not, be invested. The Trustee Directors also recognise that within a With-Profits arrangement, which is pooled arrangement across many different populations of members, it is not possible to direct the manager in relation to non-financial factors when it comes to choosing investments. As this is a closed arrangement, and no members have actively expressed the desire for a specific ethical or faith-based option, the Trustee Directors have made the decision not to offer specific funds in this area.

For the record

The Trustee Directors obtain and consider proper advice from suitably experienced and qualified persons when choosing investments and preparing the Statement of Investment Principles.

The With-Profits arrangement is intended to deliver good member outcomes at retirement from an appropriate balance of investment growth relative to inflation and the then pertinent investment risks.

The With-Profits arrangement is a life insurance company based legal vehicle. The With-Profits arrangement may invest in quoted and unquoted securities traded in regulated UK and overseas markets:

- Equities (company shares);
- Fixed interest and index-linked bonds issued by governments and companies;
- Cash and other short-term interest bearing deposits;
- Commercial and residential property;
- Illiquid assets including infrastructure, forestry, private equity and private debt;
- Commodities through collective investment vehicles; and
- Derivatives to facilitate changes in where funds are invested or to help control investment risks.

Funds provided through a life insurance company must comply with the Financial Conduct Authority ("FCA") "Permitted Links" rules, which place limits on the degree of leverage a fund can use. Exchange Traded Funds may be used directly or indirectly to gain access to less easily traded and illiquid asset classes.

Subject to the With-Profits arrangements contractual terms and polices set out in Principles and Practices of Financial Management the underlying fund manager is given full discretion over the choice of securities. The With-Profits provider is expected to maintain well-diversified and suitably liquid portfolio of investments to back the With-Profits arrangement.

The Trustee Directors consider that these types of investments are suitable for the Scheme. The Trustee Directors are satisfied that the With-Profits arrangement used by the Scheme provides adequate diversification.

Appendix A
Investment implementation for the default arrangement

Default arrangement

The Scheme has a single fund which is a traditional With-Profits arrangement, now managed by Phoenix Life Limited who took over the management from Scottish Mutual Assurance Limited in 2009.

The With-Profits arrangement provides a guaranteed benefit at the member's target retirement date. The guaranteed benefit can increase with annual bonuses and potentially a terminal bonus at the target retirement date. The annual and terminal bonuses are dependent on investment returns on the underlying investments (net of management costs) relative to the already guaranteed returns and are at the discretion of Phoenix Life Limited within their stated policies in relation to the With-Profits arrangement, as set out in their Principles and Practices of Financial Management.

Due to the relatively significant levels of investment guarantees in the With-Profits arrangement, the provider will follow a diversified and cautious approach to investment. For traditional With-Profits pensions arrangements the target asset allocation is 25-35% in investments that are expected to generate a high level of returns in excess of inflation (equities, commercial property and alternative assets) with the remainder invested in fixed interest securities (government or corporate debt instruments) or cash.

As at 31 December 2019, ex Scottish Mutual traditional with-profits pension policies managed by Phoenix Life Limited were invested as follows:

Asset class	%
Company shares (equities)	24
Property	4
Other growth assets	2
Total growth assets	**30**
Fixed interest stocks – issued by the UK government	34
Fixed interest stocks – other (including corporate bonds)	34
Cash	2
Total fixed interest and cash	**70**

Funds and charges

The expenses of managing the With-Profits arrangement are taken off the investment return before bonuses are added to the member's policy. The management and deduction of expenses is set out in the Principles and Practices of Financial Management.

There is also an annual policy charge payable by the employer.

Transaction costs

Transaction costs arise when the fund manager buys and sells the assets held by each fund. These costs are taken into account when calculating the bonuses added to member's policies.

Appendix B

Summary of the approach to investment governance

For the record

The Trustee Directors' approach to investment governance complies with the provisions of the Scheme's Trust Deed and Rules as well as legislative requirements.

The Scheme's investment governance is also intended to meet the expectations set out in the Pensions Regulator's 2016 Code of Practice 13.

Exercising the Trustee Directors' Powers

The Trustee Directors will always aim to act in the best interests of the members.

The Trustee Directors have delegated day-to-day work on the Scheme's administration and investments. The current service providers to the Scheme together with how they are paid is set out in Appendix D.

Conflicts of interest

In the event of a conflict of interests, the Trustee Directors will ensure that contributions are invested in the sole interests of members and beneficiaries.

Monitoring

The Trustee Directors regularly monitor and review:

Investment Performance - The performance of the With-Profits arrangement funds in which the Scheme invests.

The Statements of Investment Principles - at least every three years and without delay after any significant change in investment policy or the demographic profile of the Scheme's membership. The Trustee Directors will consult the Employer on any changes.

Reporting

The Trustee Directors arrange for the preparation of:

- The Scheme's audited Annual Report and Accounts (which includes the Annual Governance Statement);
- The Annual Governance Statement by the Chair of Trustee Directors describing the Scheme's investment costs, value for members and governance during the previous year;
- Publication of an extract from the Annual Governance Statement by the Chair of Trustee Directors in a publicly searchable location on-line.
- An annual return to the Pensions Regulator.

Appendix D

Summary of the Scheme’s service providers.

The Scheme’s current service providers and their basis of remuneration are as follows:

Service	Provider	Remuneration basis
With-Profits arrangement	Phoenix Life Limited	Expenses deducted from the With-Profits fund in line with the policy set out in Phoenix Life Limited’s Principles and Practices of Financial Management for its with-profits arrangements
Fund managers	Selected by Phoenix Life Limited	Paid by Phoenix Life Limited from the expenses deducted from the With-Profits fund
Pension administrator	Phoenix Life Limited	Expenses deducted from the With-Profits fund in line with the policy set out in Phoenix Life Limited’s Principles and Practices of Financial Management for its with-profits arrangements
Auditor		Fixed fee
Investment Consultant	Hymans Robertson LLP	Time cost fees
Legal advisers	Eversheds Sutherlands LLP	Time cost fees