Statement of Investment Principles for the Segregated Part C Section of the Interserve Pension Scheme

June 2022

1. Introduction

This Statement of Investment Principles ("SIP") sets out the policy of the Trustee of the Interserve Pension Scheme ("the Trustee") on various matters governing decisions about the investments of the Segregated Part C Section of the Interserve Pension Scheme ("the Section"), a Defined Benefit ("DB") Scheme.

The SIP is designed to meet the requirements of Section 35 (as amended) of the Pensions Act 1995 ("the Act"), the Occupational Pension Schemes (Investment) Regulations 2005 (as amended) and the Pension Regulator's guidance for defined benefit pension schemes (March 2017) and the Occupational Pension Schemes (Charges and Governance) Regulations 2015.

This SIP has been prepared after obtaining and considering written professional advice from LCP, the Section's investment adviser, whom the Trustee believes to be suitably qualified and experienced to provide such advice. The advice considers the suitability of investments including the need for diversification given the circumstances of the Section and the principles contained in this SIP. The Trustee has consulted with the relevant employer in producing this SIP. All employers with active members in the Section have nominated Mitie FM Limited to act on their behalf in the consultation process.

The Trustee will review this SIP from time to time and, with the help of its advisers, will amend it 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.

- **Appendix 1** sets out details of the Section's investment governance structure, including the key responsibilities of the Trustee, investment advisers and investment managers. It also contains a description of the basis of remuneration of the investment adviser and the investment managers.
- **Appendix 2** sets out the Trustee's policy towards risk appetite, capacity, measurement and management.

2. Investment objectives

The Trustee is aware that there are various measures of funding and has given due weight to those considered most relevant to the Section.

The primary objective is to ensure that the Section should be able to meet benefit payments as they fall due. In addition to this primary objective, the Trustee has additional objectives. These are as follows:

- that the expected return on the Section's assets is maximised whilst managing and maintaining investment risk at an appropriate level. What the Trustee determines to be an appropriate level of risk is set out in Appendix 2.
- to ensure that the Section has a long-term journey plan in place (in agreement with the Principal Employer) which is designed to help it achieve full funding on the agreed technical provisions basis. Progress against this long-term journey plan will be reviewed on a regular basis.

3. Investment strategy

The Trustee, with the help of its advisers and in consultation with the employer, agreed a suitable investment strategy following the results of the 31 December 2020 actuarial valuation. This resulted in the asset allocation below.

Asset class	Strategic allocation
Diversified growth	10.0%
Global equities	15.0%
Infrastructure	7.5%
Asset-backed securities	12.5%
Corporate bonds	10.0%
Liability-driven investment ("LDI") and cash	45.0%
Total	100.0%

There is no formal rebalancing policy. The Trustee monitors the asset allocation from time to time. If material deviations from the strategic allocation occur the Trustee will consider with its advisers whether it is appropriate to rebalance the assets, considering factors such as market conditions and anticipated future cash flows.

4. Considerations in setting the investment arrangements

When deciding how to invest the Section's assets, the Trustee considers several risks, including, but not limited to, those set out in Appendix 2. Some of these risks are more quantifiable than others, but the Trustee has tried to allow for the relative importance and magnitude of each risk.

The Trustee considered a wide range of asset classes for investment, taking account of the expected returns and key individual risks associated with those asset classes as well as how these risks can be mitigated where appropriate. The key financial assumptions made by the Trustee are set out on the following page:

Asset class	Expected return above gilts (pa)
Diversified growth	2.9%
Global equities	4.8%
Infrastructure	4.2%
Asset-backed securities	1.6%
Corporate bonds	0.7%
LDI	0.0%

In setting the strategy for the Section the Trustee considered:

- the Section's investment objectives, including the target return required to meet the Trustee's investment objectives;
- the best interests of all members and beneficiaries;
- the risks, rewards and suitability of a number of possible asset classes and investment strategies and whether the return expected for taking any given investment risk is considered sufficient given the risk being taken;
- the need for appropriate diversification between different asset classes to ensure that both the Section's overall level of investment risk and the balance of individual asset risks are appropriate;
- any other considerations which the Trustee considers financially material over the time horizon that the Trustee considers is needed for the funding of future benefits by the investments of the Section;
- the Trustee's investment beliefs about how investment markets work, and which factors are most likely to impact investment outcomes;
- the Section's cash flow requirements in order to meet benefit payments in the near to medium term; and
- the circumstances of the Section, including the profile of the benefit cash flows (and the ability to meet these in the near to medium term), the funding level, and the strength of the employer covenant.

The Trustee's key investment beliefs, which influenced the setting of the investment arrangements, are as follows:

- asset allocation is the primary driver of long-term returns;
- risk-taking is necessary to achieve return, but not all risks are rewarded;
- equity, credit and illiquidity are the primary rewarded risks;
- risks that do not have an expected reward should generally be avoided, hedged or diversified;
- investment markets are not always efficient and there may be opportunities for good active managers to add value;

- environmental, social and governance ("ESG") factors are likely to be one area of market inefficiency and so managers may be able to improve risk-adjusted returns by taking account of ESG factors;
- investment managers who can consistently spot and profitably exploit market opportunities are difficult to find and therefore passive management, where available, is usually better value;
- long-term environmental, social and economic sustainability is one factor that trustees should consider when making investment decisions; and
- costs have a significant impact on long-term performance and therefore obtaining value for money from the investments is important.

5. Implementation of the investment arrangements

Before investing in any manner, the Trustee obtains and considers proper written advice from its investment adviser on the question of whether the investment is satisfactory, having regard to the need for suitable and appropriately diversified investments.

Details of the investment managers are set out in the separate Investment Policy Implementation Document.

The Trustee has signed agreements with the investment managers setting out in detail the terms on which the portfolios are to be managed. The investment managers' primary role is the day-to-day investment management of the Section's investments. The managers are authorised under the Financial Services and Markets Act 2000 (as amended) to carry out such activities.

The Trustee and investment managers to whom discretion has been delegated exercise their powers to giving effect to the principles in this Statement of Investment Principles, so far as is reasonably practicable.

The Trustee has limited influence over managers' investment practices because all the Section's assets are held in pooled funds, but it encourages its managers to improve their practices where appropriate.

The Trustees' view is that the fees paid to the investment managers, and the possibility of their mandate being terminated, ensure they are incentivised to provide a high quality service that meets the stated objectives, guidelines and restrictions of the fund. However, in practice managers cannot fully align their strategy and decisions to the (potentially conflicting) policies of all their pooled fund investors in relation to strategy, long-term performance of debt/equity issuers, engagement and portfolio turnover.

It is the Trustees' responsibility to ensure that the managers' investment approaches are consistent with its policies before any new appointment, and to monitor and to consider terminating any existing arrangements that appear to be investing contrary to those policies. The Trustee expects investment managers, where appropriate, to make decisions based on assessments of the longer term financial and non-financial performance of debt/equity issuers, and to engage with issuers to improve their performance. It assesses this when selecting and monitoring managers.

The Trustee evaluates investment manager performance by considering performance over both shorter and longer-term periods as available. The duration of a manager's appointment will depend on strategic considerations and the outlook for future performance. Generally, the Trustee would be unlikely to terminate a mandate on short-term performance grounds alone.

The Trustee's policy is to evaluate each of its investment managers by reference to the manager's individual performance as well the role it plays in helping the Section's meet its overall long-term objectives, taking account of risk, the need for diversification and liquidity. Each manager's remuneration, and the value for money it provides, is assessed in light of these considerations.

The Trustee recognises that portfolio turnover and associated transaction costs are a necessary part of investment management and that the impact of portfolio turnover costs is reflected in performance figures provided by the investment managers. The Trustee expects its investment consultant to incorporate portfolio turnover and resulting transaction costs as appropriate in its advice on the Section's investment mandates.

6. Realisation of investments

The investment managers have discretion over the timing of realisation of investments of the Section within the portfolios that they manage, and in considerations relating to the liquidity of investments.

When appropriate, the Trustee, on the administrators' recommendation, decides on the amount of cash required for benefit payments and other outgoings and informs the investment managers of any liquidity requirements. The Trustee's preference is for investments that are readily realisable, but recognise that achieving a well-diversified portfolio may mean holding some investments that are less liquid. In general, the Trustee's policy is to use cash flows to rebalance the Section's assets towards the strategic asset allocation, and also receive income from some of the portfolios where appropriate.

7. Consideration of financially material and non-financial matters

The Trustee has considered how environmental, social, governance and ethical factors should be taken into account in the selection, retention and realisation of investments, given the time horizon of the Section and its members.

The Trustee expects its investment managers to take account of financially material considerations (including climate change and other ESG considerations). The Trustee seeks to appoint managers that have appropriate skills and processes to do this, and from time to time reviews how its managers are taking account of these issues in practice.

The Trustee has limited influence over managers' investment practices where assets are held in pooled funds, but encourages its managers to improve their practices where appropriate.

The Trustee does not take into account any non-financial matters (ie matters relating to the ethical and other views of members and beneficiaries, rather than considerations of financial risk and return) in the selection, retention and realisation of investments.

8. Stewardship

The Trustee recognises its responsibilities as owners of capital, and believes that good stewardship practices, including monitoring and engaging with investee companies, and exercising voting rights attaching to investments, protect and enhance the long-term value of investments. The Trustee has delegated to its investment managers the exercise of rights attaching to investments, including voting rights, and engagement with issuers of debt and equity and other relevant persons about relevant matters such as performance, strategy, risks and ESG considerations.

The Trustee does not monitor or engage directly with issuers or other holders of debt or equity. It expects the investment managers to exercise ownership rights and undertake monitoring and engagement in line with the managers' general policies on stewardship, as provided to the Trustee from time to time, considering the long-term financial interests of the beneficiaries.

The Trustee seeks to appoint managers that have strong stewardship policies and processes, reflecting where relevant the recommendations of the UK Stewardship Code issued by the Financial Reporting Council, and from time to time the Trustee reviews how these are implemented in practice.

SIP signed for and on behalf of the Trustee of the Scheme:

Signed: ____

Investment governance, responsibilities, decision-making and fees

The Trustee has decided on the following division of responsibilities and decision-making for the Section. This division is based upon the Trustee's understanding of the various legal requirements placed upon it, and its view that the division of responsibility allows for efficient operation and governance of the Section overall. The Trustee's investment powers are set out within the Section's governing documentation.

1. Trustee

In broad terms, the Trustee is responsible in respect of investment matters for:

- developing a mutual understanding of investment and risk issues with the employer;
- setting the investment strategy, in consultation with the employer;
- formulating a policy in relation to financially material considerations, such as those relating to ESG considerations (including but not limited to climate change);
- formulating a policy on taking account of non-financial matters in the selection, retention and realisation of investments;
- setting the policy for rebalancing between asset classes;
- setting a policy on the exercise of rights (including voting rights) and undertaking engagement activities in respect of the investments;
- putting effective governance arrangements in place and documenting these arrangements in a suitable form;
- appointing (and, when necessary, dismissing) investment managers, investment advisers, actuary and other service providers;
- monitoring the exercise of the investment powers that they have delegated to the investment managers and monitoring compliance with Section 36 of the Act;
- communicating with members as appropriate on investment matters, such as the Trustee's assessment of its effectiveness as a decision-making body, the policies regarding responsible ownership and how such responsibilities have been discharged;
- reviewing the investment policy as part of any review of the investment strategy;
- reviewing the content of this SIP from time to time and modifying it if deemed appropriate; and
- consulting with the employer when reviewing the SIP.

2. Investment managers

In broad terms, the investment managers will be responsible for:

- managing the portfolios of assets according to their stated objectives, and within the guidelines and restrictions set out in their respective investment manager agreements and/or other relevant governing documentation;
- taking account of financially material considerations (including climate change and other ESG considerations) as appropriate when managing the portfolios of assets;
- exercising rights (including voting rights) attaching to investments and undertaking engagement activities in respect of investments;
- providing the Trustee with regular information concerning the management and performance of their respective portfolios; and
- having regard to the provisions of Section 36 of the Act insofar as it is necessary to do so.

The custodians of the portfolios (whether there is a direct relationship between the custodian and the Trustee or not) are responsible for safe keeping of the assets and facilitating all transactions within the portfolios.

3. Investment adviser

In broad terms, the investment adviser will be responsible, in respect of investment matters, as requested by the Trustee, for:

- on advising how material changes within the Section’s benefits, membership, and funding position may affect the manner in which the assets should be invested and the asset allocation policy; and
- participating with the Trustee in reviews of this SIP.

4. Fee structures

The Trustee recognises that the provision of investment management and advisory services to the Section results in a range of charges to be met, directly or indirectly, by deduction from the Section’s assets.

The Trustee has agreed Terms of Business with the Section’s investment advisers, under which work undertaken is charged for on a “time-cost” basis.

The investment managers receive fees calculated by reference to the market value of assets under management and also in some cases a performance related fee. The fee rates are believed to be consistent with the manager’s general terms for institutional clients and are considered by the Trustee to be reasonable when compared with those of other similar providers.

The fee structure used in each case has been selected with regard to existing custom and practice, and the Trustee's view as to the most appropriate arrangements for the Section. However, the Trustee will consider revising any given structure if and when it is considered appropriate to do so.

5. Performance assessment

The Trustee is satisfied, considering the external expertise available, that there are sufficient resources to support its investment responsibilities. The Trustee believes that it has sufficient expertise and appropriate training to carry out its role effectively.

It is the Trustee's policy to assess the performance of the Section's investments, investment providers and professional advisers from time to time. The Trustee will also periodically assess the effectiveness of its decision-making and investment governance processes and will decide how this may then be reported to members.

6. Working with the Section's employer

When reviewing matters regarding the Section's investment arrangements, such as the SIP, the Trustee seeks to give due consideration to the employer's perspective. While the requirement to consult does not mean that the Trustee needs to reach agreement with the employer, the Trustee believes that better outcomes will generally be achieved if the Trustee and employer work together collaboratively.

Policy towards risk

1. Risk appetite and risk capacity

Risk appetite is a measure of how much risk the Trustee is willing to bear within the Section in order to meet its investment objectives. Taking more risk is expected to mean that those objectives can be achieved more quickly, but it also means that there is a greater likelihood that the objectives are missed, in the absence of remedial action. Risk capacity is a measure of the extent to which the Trustee can tolerate deviation from its long term objectives before attainment of those objectives is seriously impaired. The Trustee aims to strike the right balance between risk appetite and risk capacity.

When assessing the risk appetite and risk capacity, the Trustee considered a range of qualitative and quantitative factors, including:

- the strength of the employer's covenant and how this may change in the near/medium future;
- the agreed journey plan and employer contributions;
- the Section's long-term and shorter-term funding targets;
- the Section's liability profile, its interest rate and inflation sensitivities, and the extent to which these are hedged;
- the Section's cash flow and target return requirements; and

2. Approach to managing and monitoring investment risks

The Trustee considers that there are a number of different types of investment risk that are important to manage and monitor. These include, but are not limited to:

2.1. Risk of inadequate returns

A key objective of the Trustee is that, over the long-term, the Section should generate its target return so that it has adequate assets to meet its liabilities as they fall due. The Trustee therefore invests the assets of the Section to produce a sufficient long-term return in excess of the liabilities. There is also a risk that the performance of the Section's assets and liabilities diverges in certain financial and economic conditions in the short term. This risk has been taken into account in setting the investment strategy and is monitored by the Trustee on a regular basis.

2.2. Equity risk

The Trustee believes that equity risk is a rewarded investment risk, over the long term. The Trustee considers exposure to equity risk in the context of the Section's overall investment strategy and believes that the level of exposure to this risk is appropriate.

2.3. Risk from lack of diversification

This is the risk that failure of a particular investment, or the general poor performance of a given investment type, could materially adversely affect the Section's assets. The Trustee believes that the Section's assets are adequately diversified between different asset classes and within each asset class. This was a key consideration when determining the Section's investment arrangements and is monitored by the Trustee on a regular basis.

2.4. Investment manager risk

This is the risk that an investment manager fails to meet its investment objectives. Prior to appointing an investment manager, the Trustee receives written advice from a suitably qualified individual and will typically undertake an investment manager selection exercise. The Trustee monitors the investment managers on a regular basis to ensure they remain appropriate for its selected mandate.

2.5. Liquidity/marketability risk

This is the risk that the Section is unable to realise assets to meet benefit cash flows as they fall due, or that the Section will become a forced seller of assets in order to meet benefit payments. The Trustee is aware of the Section's cash flow requirements and believes that this risk is managed by maintaining an appropriate degree of liquidity across the Section's investments and by investing in income generating assets, where appropriate.

2.6. Environmental, social and governance (ESG) risks

Environmental, social and corporate governance (ESG) factors are sources of risk to the Section's investments, some of which could be financially material, over both the short and longer term. These potentially include risks relating to factors such as climate change, unsustainable business practices, and unsound corporate governance. The Trustee seeks to appoint investment managers who will manage these risks appropriately on their behalf and from time to time reviews how these risks are being managed in practice.

2.7. Collateral adequacy risk

The Section is invested in leveraged Liability Driven Investment ("LDI") arrangements to provide protection ("hedging") against adverse changes in interest rates and inflation expectations. The LDI manager may from time to time call for additional cash to be paid to the LDI portfolio in order to support a given level of leverage. Collateral adequacy risk is the risk that the Trustee when requested to do so will not be able to post additional cash to the LDI fund within the required timeframe. A potential consequence of this risk is that the Section's interest rate and inflation hedging could be reduced and that the Section's funding level could suffer subsequently as a result. In order to manage this risk, the Trustee ensures that the Section has a sufficient allocation to cash and other highly liquid assets which can be readily realised, so that cash can be posted to the LDI manager at short notice.

2.8. Credit risk

This is the risk that one party to a financial instrument will cause a financial loss for the other party by failing to discharge an obligation.

The Section is indirectly exposed to credit risks arising from the underlying investments held by the portfolios, for example where they invest in bonds. The indirect exposure to credit risk arises from the Section's investments in diversified growth fund, the asset-backed securities fund, corporate bond fund and the LDI portfolio.

The managers of these funds manage credit risk by having a diversified exposure to bond issuers, conducting thorough research on the probability of default of those issuers. The magnitude of credit risk within each fund will vary over time, as the manager changes the underlying investments in line with its views on markets, asset classes and specific bonds. Within the LDI portfolio, there is exposure to credit risk as the LDI portfolio manager uses derivative instruments to match a portion of the Section's liabilities.

2.9. Currency risk

Whilst the majority of the currency exposure of the Section's assets is to Sterling, the Section is subject to currency risk because some of the Section's investments are held in overseas markets. The Trustee considers the overseas currency exposure in the context of the overall investment strategy and believes that the currency exposure that exists diversifies the strategy and is appropriate.

All of the Section's investments are accessed via a Sterling share class. Therefore the Section is not subject to direct currency risk. The Section's assets that are exposed to indirect currency risk are the equity fund, the diversified growth fund, the asset-backed securities fund and the infrastructure fund, which invest in non-Sterling investments.

The exposure to foreign currencies within the pooled funds will vary over time as the manager changes the underlying investments but is not expected to be a material driver of returns over the longer term. Decisions about the exposure to foreign currencies within the funds held are at the discretion of the appointed investment managers.

2.10. Interest rate and inflation risk

The Section's assets are subject to interest rate and inflation risk because some of the Section's assets are held in bonds and interest rate swaps, both through segregated investments and investments via pooled funds. However, the interest rate and inflation exposure of the Section's assets hedges the corresponding risks associated with the Section's liabilities.

The Trustee considers interest rate and inflation risks to be generally unrewarded investment risks and therefore hedges part of these risks using a mixture of bonds as well as a leveraged LDI arrangement.

The net effect of the Trustee's approach to interest and inflation risk will be to reduce the volatility of the funding level, and so the Trustee believes that it is appropriate to manage exposures to these risks in this manner and to review them on a regular basis.

2.11. Other non-investment risks

The Trustee recognises that there are other, non-investment, risks faced by the Section, and takes these into consideration as far as practical in setting the Section's investment arrangements as part of its assessment of the other aspects of the Section's Integrated Risk Management framework.

Examples include:

- longevity risk (the risk that members live, on average, longer than expected); and
- sponsor covenant risk (the risk that, for whatever reason, the sponsoring employer is unable to support the Section as anticipated).

Together, the investment and non-investment risks give rise generally to funding risk. This is the risk that the Section's funding position falls below what is considered an appropriate level. The Trustee regularly reviews progress towards the Section's funding target, both in the longer-term as well as against short-term milestones, comparing the actual versus the expected funding level.

By understanding, considering and monitoring the key risks that contribute to funding risk, the Trustee believes that it has appropriately addressed and are positioned to manage this general risk.