Cincinnati Machine Pension Plan

Statement of

Investment Principles

Sixth Edition

1.0 Introduction

This Statement of Investment Principles (the "Statement") has been prepared by the Trustee of Cincinnati Machine Pension Plan (the "Plan"). This statement sets down the principles which govern the decisions about investments that enable the Plan to meet the requirements of:

- the Pensions Act 1995, as amended by the Pensions Act 2004; and
- the Occupational Pension Schemes (Investment) Regulations 2005 as amended by the Occupational Pension Schemes (Investment) (Amendment) Regulations 2010.
- the Occupational Pension Schemes (Investment and Disclosure) (Amendment and Modification) Regulations 2018.
- the Occupational Pension Schemes (Investment and Disclosure) (Amendment) Regulations 2019.

This Statement replaces all other versions and addenda.

The Principal Employer of the Plan has become insolvent and the Plan has entered an assessment period for the Pension Protection Fund (the "PPF").

2.0 Investment Governance Structure

The Trustee's primary role is to act in the best interests of the Plan's members.

The Trustee takes all investment decisions with advice from their investment adviser. Investment decisions include, but are not limited to:

- Asset allocation;
- Fund manager selection and deselection;
- Derisking;
- Currency hedging programmes;
- The use of derivatives for risk management purposes.

The Scheme Actuary's role includes, but is not limited to:

- Undertaking and presenting triennial (or more frequent if required) actuarial valuations and advising the Trustee on appropriate contribution rates;
- Providing the investment adviser with cashflow and liability information to enable asset allocation and journey planning to be undertaken;

The Trustee is a professional Trustee, and undertakes training where it is required to enable informed decisions to be made.

3.0 Investment Beliefs

The Trustee takes a forward-thinking approach to asset allocation, considering the long-term economic outlook. The Trustee recognises the limitations with financial models, and do not base decisions solely on such analysis.

Both passive and active mandates will be considered, depending on the efficiency of the market being invested in.

The Trustee does not have strong beliefs that they feel should constrain or influence their decision-making process and are not aware of any such beliefs within the membership of the Plan.

4.0 Investment Objectives

Investment objectives are set with reference to the liability profile of the Plan.

The Trustee has set out two main objectives for the investment strategy:

- To ensure sufficiently realisable investments to meet member payments when they fall due;
- To reduce risk as much as prudently possible - within the constraints of the first objective and liquidity requirements - with respect to interest rate and inflation sensitivity.

5.0 Risk Management

Integrated Risk Management

The Trustee fully understands the need to align the interests of all stakeholders in the Plan.

Risk Appetite

Given the size of the Plan and the backwards-looking nature of risk metrics, the Trustee has not set an absolute risk level for the Plan.

Risk Reduction Strategies

The Trustee embraces diversification as a means to reduce portfolio risk.

In addition, risk mitigation strategies will be implemented, such as adding to pooled funds that have exposure to bonds and/or interest rate and inflation swaps, hedging currency risk or adding tail risk protection, as a means to address specific portfolio or liability valuation driven risks, where it is appropriate and cost-effective to do so.

The Trustee delegates the day to day running of the Plan's investments to appropriately qualified fund managers, who are recommended by their investment adviser.

The Trustee will invest passively in certain asset classes where the risk of manager underperformance is not expected to be compensated by superior returns.

5.4 Cashflow Management

One of the key elements when setting investment strategy is the liquidity requirements of the Plan. The Trustee monitors ongoing liquidity needs quarterly and assesses whether there are sufficiently liquid assets available in the short term by stressing capital calls, member payments and hedging strategies.

6.0 Long Term Journey Plan

The Plan's investment strategy is currently under review by the Trustee who are considering the potential outcomes of the PPF assessment amongst several other factors.

The Plan's existing broad strategic asset allocation is based on 60% Growth and 40% Matching assets.

7.0 Asset Allocation

Growth Assets

The Trustee has not restricted the Plan by asset class and is willing to consider a broad range of investments, provided they fit within a framework of diversification across different drivers of return.

Matching Assets

The Plan holds a combination of physical bonds (both corporate and government), bond repurchase agreements (repos), and derivatives (swaps) which are used to provide a level of a protection against interest rates and inflation expectations. Instruments will be both nominal and index-linked in nature.

It is recognised that the size of the Plan restricts investment to pooled funds only and that market conditions and liquidity requirements will result in the mix of assets deviating from the target.

8.0 Fund Manager Selection

Fund manager selection is made by the Trustee following recommendations made by their investment adviser.

As part of the fund research process the investment adviser will consider each fund manager's approach to environmental, social and governance (ESG) issues, alongside other factors which may be considered financially significant. Other non-financial matters are generally not considered unless there is a strong reason to do so. Whilst this does not restrict the investment to only managers who have strong ESG principles, it will form part of the selection process.

9.0 Performance Monitoring

The Trustee periodically reviews the performance of the Plan’s assets.

Fund managers are monitored over the long term and it is accepted that, given the mandates in place, short term volatility may be experienced.

10.0 Financially material considerations, non-financial matters, the exercise of voting rights and engagement activities

Financially material considerations

The Trustee has considered financially material factors such as environmental, social and governance (‘ESG’) issues as part of the investment process to determine a strategic asset allocation over the length of time during which the benefits are provided by the Plan for members. It believes that financially material considerations (including climate change) are implicitly factored into the expected risk and return profile of the asset classes they are investing in.

In endeavouring to invest in the best financial interests of the beneficiaries, the Trustee has elected to invest through pooled funds. The Trustee acknowledges that it cannot directly influence the environmental, social and governance policies and practices of the companies in which the pooled funds invest. However, the Trustee does expect its fund managers and investment consultant to take account of financially material considerations when carrying out their respective roles.

The Trustee accepts that the Plan's assets are subject to the investment manager's own policy on socially responsible investment. The Trustee will assess that this corresponds with its responsibilities to the beneficiaries of the Plan with the help of its investment consultant.

An assessment of the ESG and responsible investment policies forms part of the manager selection process when appointing new managers and these policies are also reviewed regularly for existing managers with the help of the investment consultant. The Trustee will only invest with investment managers that are signatories for the United Nations Principles of Responsible Investment ('UN PRI') or other similarly recognised standard.

The Trustee will monitor financially material considerations through the following means:

- Obtain training where necessary on ESG considerations in order to understand fully how ESG factors including climate change could impact the Plan and its investments;
- Use ESG ratings information provided by its investment consultant, to assess how the Plan's investment managers take account of ESG issues; and
- Request that all of the Plan's investment managers provide information about their ESG policies, and details of how they integrate ESG into their investment processes, via its investment consultant.

If the Trustee determines that financially material considerations have not been factored into the investment managers' process, it will take this into account on whether to select or retain an investment.

Non-financially material considerations

The Trustee has not considered non-financially material matters in the in the selection, retention and realisation of investments.

Stewardship

The Trustee's policy on the exercise of rights attaching to investments, including voting rights, is that these rights should be exercised by the investment manager on the Trustee's behalf, having regard to the best financial interests of the beneficiaries.

The investment manager should engage with companies to take account of ESG factors in the exercise of such rights as the Trustee believes this will be beneficial to the financial interests of members over the long term. The Trustee will review the investment managers' voting policies, with the help of its investment consultant, and decide if they are appropriate.

The Trustee also expect the fund manager to engage with investee companies on the capital structure and management of conflicts of interest.

If the policies or level of engagement are not appropriate, the Trustee will engage with the investment manager, with the help of its investment consultant, to influence the investment managers' policy. If this fails, the Trustee will review the investments made with the investment manager.

The Trustee has taken into consideration the Financial Reporting Council's UK Stewardship Code and expect investment managers to adhere to this where appropriate for the investments they manage.

ESG and Climate Change Risks

There is a risk that ESG issues and climate change are not considered as part of the investment process and so may expose the portfolio to unexpected risks. This can lead to losses that may not have been factored into any expectations of future investment returns. The Trustee has considered ESG issues including climate change as part of the investment process.

11.0 Policy on arrangements with asset managers

Incentives to align investment managers investment strategy and decisions with the trustee's policies

The Plan invests in pooled funds and so the Trustee acknowledges the fund's investment strategy and decisions cannot be tailored to the Trustee's policies. However, the Trustee sets its investment strategy and then selects managers that best suits its strategy taking into account the fees being charged, which acts as the fund managers incentive.

The Trustee uses the fund objective/benchmark as a guide on whether its investment strategy is being followed and monitors this regularly.

Incentives for the investment manager to make decisions based on assessments about medium to long-term financial and nonfinancial performance of an issuer of debt or equity and to engage with issuers of debt or equity in order to improve their performance in the medium to long-term

The Trustee selects managers based on a variety of factors including investment philosophy, and process, which it believes should include assessing the long term financial and non-financial performance of the underlying company.

The Trustee also considers the managers voting and ESG policies and how it engages with the company as it believes that these can factors can improve the medium to long-term performance of the investee companies.

The Trustee will monitor the fund managers' engagement and voting activity on an annual basis as they believe this can improve long term performance. The Trustee expects their managers to make every effort to engage with investee companies but acknowledges that their influence may be more limited in some asset classes, such as bonds, as they do not have voting rights.

The Trustee acknowledges that in the short term, these policies may not improve the returns it achieves, but do expect those companies with better financial and non-financial performance over the long term will lead to better returns for the Plan.

The Trustee believes the annual fee paid to the fund managers incentivise them to do this.

If the Trustee feels that the fund managers are not assessing financial and non-financial performance or adequately engaging with the companies they are investing in, it will use these factors in deciding whether to retain or terminate a manager.

How the method (and time horizon) of the evaluation of the asset manager's performance and the remuneration for asset management services are in line with the trustee's policies

The Trustee reviews the performance of each fund periodically on a net of fees basis compared to its objective.

The Trustee assesses the performance periods of the funds over at least a 3-5 year period when looking to select or terminate a manager, unless there are reasons other than performance that need to be considered.

The fund managers' remuneration is considered as part of the manager selection process and is also monitored regularly with the help of its investment consultant to ensure it is in line with the Trustee's policies.

How the trustee monitors portfolio turnover costs incurred by the asset manager, and how they define and monitor targeted portfolio turnover or turnover range

The Trustee acknowledges that portfolio turnover costs can impact on the performance of their investments. Overall performance is assessed from time to time.

During the investment manager appointment process, the Trustee may consider both past and anticipated portfolio turnover levels. When underperformance is identified, deviations from the expected level of turnover may be investigated with the investment manager concerned if it is felt they may have been a significant contributor to the underperformance. Assessments reflect the market conditions and peer group practices. The Trustee acknowledges that for some asset classes, such as LDI, a higher turnover of contracts such as repurchase agreements, can be beneficial to the fund from both a risk and cost perspective.

The duration of the arrangement with the asset manager

The Trustee plans to hold each of its investments for the long term but will keep this under review.

Changes in investment strategy or change in the view of the fund manager can lead to the duration of the arrangement being shorter than expected.

12.0 Transparency

It is the Trustee's aim to be transparent and free from conflicts as fiduciary to the Plan.

The following information is available to members in line with best practice approach to communication:

- Statement of Investment Principles
- Annual Funding Statement
- Annual Report & Accounts for the Scheme
- Latest Actuarial Valuation
- Statement of Funding Principles
- Schedule of Contributions

13.0 Compliance

This Statement has been drawn up with reference to current legislation and best practice. In particular, the Trustee has considered the Myners' Principles and The Pensions Regulator's Investment Guidance for Defined Benefit Pension Schemes, as appropriate to the Plan.

The Statement will be reviewed following any significant changes to the Plan's investment strategy or once further certainty on the outcome of the Plan following assessment by the PPF is obtained.

Agreed as final version on behalf of the Trustee(s) of Cincinnati Machine Pension Plan

Dated **21 September 2020**

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