Addendum to the Statement of Investment Principles

For the Castle Pension Scheme

Effective from: December 2023

This addendum to the Statement of Investment Principles (“SIP”) for the Castle Pension Scheme (“the Scheme”) has been produced by Castle Pension Scheme Trustees Limited (“the Trustee”). It sets out a description of various matters which are not required to be included in the SIP, but which are relevant to the Scheme’s investment arrangements.

Part 1:
Investment governance, responsibilities, decision-making and fees

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

1. Trustee

The Trustee's responsibilities include:

- Developing a mutual understanding of investment and risk issues with the employer.
- Setting investment policies, including those relating to financially material factors and the exercise of rights and engagement activities in respect of the investments.
- Putting effective governance arrangements in place and documenting these arrangements in a suitable form.
- Monitoring, reviewing, engaging with and replacing investment managers, investment advisers, actuary, and other service providers.
- Monitoring the exercise of investment powers that it has delegated to the investment managers and monitoring compliance with Section 36 of the Pensions Act 1995 (as amended).
- Communicating with members as appropriate on investment matters.
- Reviewing the SIP and modifying it as necessary.
- Consulting with the employer when reviewing the SIP.

To assist with the decisions on investment matters, the Trustee has delegated certain responsibilities to a Joint Investment Sub-Committee ("the JISC") which comprises members of the Trustee Boards of the Hanson Pension Schemes[1]. The powers of the JISC are set out in a separate document called the *"Terms of Reference for the Joint Investment Sub-Committee (JISC) of the Hanson Pension Schemes"*. A summary of these powers is provided below.

2. The JISC

In broad terms, the JISC has been delegated the responsibility to:

- Make appropriate recommendations to the Trustee regarding the Scheme's investment strategy.
- Appoint appropriate investment managers within each broad asset class.
- Make alterations to the managers within each broad asset class, including discretion to alter the mandates of the chosen managers.
- Monitor the Scheme's investment managers and the performance of the investment strategy.
- Take decisions involved with rebalancing the Scheme's investment strategy.
- Take decisions on disinvestments required to meet the cash flow requirements of the Scheme.

3. Investment managers

The investment managers' responsibilities include:

- 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 Environmental, Social and Governance ("ESG") considerations) as appropriate in managing the assets.
- Exercising rights (including voting rights) attaching to investments and

[1] The Hanson Pension Schemes for the purpose of the JISC are the Hanson Industrial Pension Scheme, the Castle Pension Scheme and the Powerhouse Retail Group of the Electricity Supply Pension Scheme.

undertaking engagement activities in respect of investments.

- Providing regular information concerning the management and performance of their respective portfolios, including information on voting and engagement undertaken.
- Having regard to the provisions of Section 36 of the Act insofar as it is necessary to do so.

The custodians of the portfolios are responsible for safe keeping of the assets and facilitating all transactions within the portfolios.

4. Investment adviser

The investment adviser's responsibilities include:

- Advising on how material changes within the Scheme's benefits, membership, and funding position may affect the manner in which the assets should be invested.
- Advising on the selection, and review, of the investment managers, incorporating its assessment of the nature and effectiveness of the managers' approaches to financially material considerations (including climate change and other ESG considerations).
- Assisting the Trustee with reviews of this SIP.

5. Fee structures

The provision of investment management and advisory services to the Scheme results in a range of charges to be met, directly or indirectly, by deduction from the Scheme's assets. The Trustee has agreed terms with the Scheme's actuarial and investment advisers, under which work undertaken is charged for by an agreed fixed fee or on a "time-cost" basis.

The investment managers receive fees calculated by reference to the market value of assets under management. The fee rates are believed to be consistent with the managers' general terms for institutional clients and the Trustee considers these 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 Scheme, and it keeps the fee structures under review.

6. Performance assessment

The Trustee is satisfied that there are adequate resources to support its investment responsibilities, and that it has sufficient expertise to carry out its role effectively.

It is the Trustee's policy to assess the performance of the Scheme'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.

7. Working with the sponsoring employer

When reviewing matters regarding the Scheme's investment arrangements, such as the SIP, the Trustee seeks to give due consideration to the employer's perspective. Whilst 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 it works with the employer collaboratively.

Part 2:
Policy towards risk

1. Risk capacity and appetite

Risk capacity is the maximum level of risk that the Trustee considers to be appropriate to take in the investment strategy. Risk appetite is how much risk the Trustee believes is appropriate to take to meet the 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.

When assessing risk and reviewing the investment strategy, the Trustee considers:

- The strength of the employer covenant and how this may change over time.
- The agreed journey plan and employer contributions.
- The Scheme's long-term and shorter-term funding targets.
- The Scheme's liability profile, its interest rate and inflation sensitivities, and the extent to which these are hedged.
- The Scheme's cash flow and target return requirements.
- The level of expected return and expected level of risk (as measured by Value at Risk ("VaR")), now and as the strategy evolves.

2. Approach to managing and monitoring risks

There are different types of investment risk that are important to manage, and the Trustee monitors these on a regular basis. These include, but are not limited to:

Strategic risk

This is the risk that the performance of the Scheme's assets and liabilities diverges in certain financial and economic conditions. This risk has been considered in the Trustee's investment strategy reviews and will be monitored by the Trustee on a regular basis.

The Trustee will review the Scheme's investment strategy at least every three years in light of the various risks faced by the Scheme.

Risk of inadequate returns

A key objective is that the assets produce a sufficient long-term return in excess of the liabilities, and the Trustee has set an appropriate target return for the assets accordingly. There is a risk that the return experienced is not sufficient. This risk has been considered in setting the investment strategy.

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 professional advice, and it will typically undertake a manager selection exercise. The Trustee monitors the investments regularly against its objectives and receives ongoing professional investment advice as to their suitability.

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 (e.g., equities), could materially adversely affect the Scheme's assets. The Trustee believes that the Scheme's assets are adequately diversified between different asset classes and within each asset class. This was a key consideration when determining the investment arrangements.

Illiquidity/marketability risk

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

Climate-related risks

Climate change is a source of risk, which could be financially material over both the short and longer term. This risk relates to the transition to a low carbon economy, and the physical risks associated with climate change (e.g., extreme weather). The Trustee seeks to appoint investment managers who will manage this risk appropriately, and the Trustee monitors how this risk is being managed in practice.

Other environmental, social and governance (ESG) risks

ESG factors are sources of risk, which could be financially material over both the short and longer term. These include risks relating to unsustainable or socially harmful business practices, and unsound corporate governance. The Trustee seeks to appoint investment managers who will manage these risks appropriately and monitor how these risks are being managed in practice.

Counterparty risk

This is the risk that one party to a contract (such as a derivative instrument) causes a financial loss to the other party by failing to discharge a contractual obligation. This risk applies in particular for those contracts that are traded directly between parties, rather than traded on a central exchange.

Counterparty risk is managed by the Scheme's managers through careful initial selection and ongoing monitoring of trading counterparties, counterparty diversification and a robust process of daily collateralisation of each contract. This ensures that counterparty risk is limited, as far as possible, to one day's market movements.

Collateral adequacy risk

Many pension schemes use leverage within their LDI portfolios to provide hedging protection against adverse changes in interest rates and inflation expectations. If leverage is employed, depending on market movements, additional cash may need to be invested in the LDI portfolio to support a given level of leverage. Collateral adequacy risk is the risk that the cash required to maintain the hedging protection is not available for use within the LDI portfolio within the required timeframe.

As at the effective date of this Addendum the Scheme's LDI portfolio is being run without leverage and managing the mandate on this basis is the preference of the Trustee. Moving to a non-leveraged LDI solution has therefore significantly reduced collateral adequacy risk for the Scheme.

Credit risk

The Scheme is subject to credit risk because it invests in bonds via pooled funds. This risk is managed by only investing in pooled funds that have a diversified exposure to different credit issuers, and only invest in bonds that are classified as "investment grade".

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 Scheme's overall investment strategy and believes that the level of exposure to this risk is appropriate.

Currency risk

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

Interest rate and inflation risk

The Scheme's assets are subject to interest rate and inflation risk because some of the Scheme's assets are held in bond funds and Liability Driven Investment ("LDI") funds. However, the interest rate and inflation exposure of the Scheme's assets provide protection (hedges) part of the corresponding risks associated with the Scheme's liabilities. Given that this should reduce the volatility of the funding level, the Trustee believes that it is appropriate to manage exposures to these risks in this manner.

Valuation risk

Some of the Scheme's assets (such as listed equities) can be valued regularly based upon observable market prices. For other assets (such as property and infrastructure), prices may only be estimated relatively infrequently using one or more of a range of approximate methods – e.g., mathematical models or recent sales prices achieved for equivalents.

At times of market stress, there is a risk for all assets that the valuations provided by investment managers do not reflect the actual sale proceeds which could be achieved if the assets were liquidated at short notice. This risk is particularly relevant for assets such as property and infrastructure. The Trustee considers exposure to valuation risk in the context of the Scheme's overall investment strategy and believe that the level of exposure to this risk is appropriate.

Other non-investment risks

The Trustee recognises that there are other non-investment risks faced by the Scheme. The Trustee takes these into consideration as far as practical in setting the investment arrangements.

Examples include:

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

Together, the investment and non-investment risks give rise generally to funding risk. This is the risk that the Scheme's funding position falls below what is considered an appropriate level. The Trustee regularly reviews progress towards the Scheme’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 and considering each of the risks that contribute to funding risk, the Trustee believes that it has addressed and is positioned to manage this general risk.

Part 3:
Investment manager arrangements

The table below shows the strategic allocation of the assets between the investment managers agreed in the last review:

Asset class	Managers	Benchmark allocation %	Range %
Equities	LGIM	5	
Total equities		**5**	**3-7**
Infrastructure	IFM	8	
Total alternative assets		**8**	**6-10**
LDI	CTI	77	
Corporate bonds	Insight	10	
Total matching assets		**87**	**83-91**
TOTAL		**100**	

Further details of the investment managers, including details of the performance objective and benchmark for each portfolio, are set out in the sections below.

LGIM (equities)

The Trustee has appointed LGIM to manage a portion of the Scheme's equity investments.

The Scheme's investment is represented by units in the World Equity Index Fund. The Fund aims to track the performance of the developed world equity market as represented by the MSCI World Index.

IFM (infrastructure)

The Trustee has appointed IFM to manage the Scheme's allocation to infrastructure.

The Scheme's investment is represented by holdings in IFM's Global Infrastructure Fund. IFM's objective is to target a total return of 8-12% p.a. net of fees depending on the stage of the economic cycle.

Insight (corporate bonds)

The Trustee has appointed Insight to manage the Scheme's corporate bond holdings, which are represented by units in Insight's Buy and Maintain Bond Fund.

Insight will manage the fund on a buy and maintain basis. Insight's objective is to hold appropriate corporate bonds until they mature while maintaining a target duration for the fund. Insight has discretion to make changes to corporate bonds held if concerned about the likelihood of default. The Trustee will monitor Insight's performance against a custom index for buy and maintain corporate bond portfolios.

CTI (LDI)

The Trustee has appointed CTI to manage the Scheme's LDI mandate which is represented by units in the funds below:

Fund	Benchmark
Unleveraged Gilt Funds	To provide unleveraged exposure to nominal (or real) Gilts and related instruments and aims to match the performance of a benchmark that represents a typical (or short duration) pension fund's liability profile as determined by the Alternative Investment Fund Manager ("AIFM")
Sterling Liquidity Fund	SONIA

The LDI portfolio has been designed in conjunction with the hedging provided by the Scheme's Buy and Maintain portfolio such that it has broadly the same sensitivity to long term interest rates and inflation expectations as an appropriate portion of the Scheme's liability cash flows. The proportions are agreed by the Trustee from time to time. In this way, the Trustee expects any changes in interest rates and inflation to have broadly the same impact on the LDI portfolio as on the relevant proportion of the liabilities those assets are matching.

The Trustee will review the allocation of the underlying funds in the LDI mandate whenever new liability cashflows are produced by the Scheme Actuary.

The Scheme is currently targeting interest rate and inflation hedge ratios of 90%.

Custodians

Northern Trust Company has been appointed by the Trustee to provide custodian services for the Scheme's holdings managed by Insight.

Additional Voluntary Contributions

While the main Scheme assets are invested as above, AVCs are invested in a number of different funds. All of the AVC policies are closed to future contributions from members, since the Scheme's closure to future accruals in September 2010.

Assets in respect of the members' AVCs are invested in funds provided by Friends Life (managed by BlackRock) and with-profits contracts with Utmost.

There is also a CIF AVC 1 vehicle where members AVCs are invested in a cash fund with LGIM.

With the help of the Trustee's advisers the AVC arrangements are periodically reviewed to ensure they remain appropriate for the investment needs of the members.

Part 4:
Monitoring and engaging with managers on voting and engagement

This section sets out the Trustee's effective system of governance ("ESOG") in relation to stewardship. This includes monitoring the voting and engagement activities that the Trustee's investment managers undertake on its behalf, engaging with them regarding the Trustee's expectations in relation to stewardship, and encouraging improvements in their stewardship practices. The Trustee will review this ESOG periodically, and at least triennially.

Stewardship priorities

The Trustee has selected some priority themes to provide a focus for its monitoring of investment managers' voting and engagement activities. The Trustee will review them regularly and update them if appropriate. The Trustee's current priorities are **Pollution, Remuneration and Human Rights**.

The Trustee chose these priorities because they are market-wide areas of risk that are financially material for the investments and can be addressed by good stewardship. Therefore, the Trustee believes it is in its members' best interests that its managers adopt strong practices in these areas.

The Trustee has written to its investment managers to notify them of its stewardship priorities.

Manager selection

The Trustee aims to appoint investment managers that have strong responsible investment skills and processes. The Trustee therefore favours investment managers who are signatories to the Principles for Responsible Investment, the UK Stewardship Code as well as the Net Zero Asset Managers Initiative.

When selecting new managers, The Trustee considers its investment consultant's assessment of potential managers' capabilities in this area. If the Trustee meets prospective managers, it usually asks questions about responsible investment, focusing on its stewardship priorities.

Manager monitoring

The Trustee receives information regularly to enable it to monitor its managers' responsible investment practices and check how effective they're being. This information includes metrics such as the Trustee's investment consultant's responsible investment grades for each manager, whether they are signatories to responsible investment initiatives, and (where available) carbon emissions data for the Scheme's mandates. It also includes a selection of voting, engagement examples relating to the Trustee's stewardship priorities. The examples are chosen to reflect the Trustee's stewardship priorities and material mandates over the course of the scheme year (although not necessarily every priority for every mandate).

Annual responsible investment review

Each year, the JISC undertakes a more comprehensive review of its managers' responsible investment practices. This includes the Trustee's investment consultant's qualitative responsible investment assessments for each manager, a summary of the managers' voting and engagement policies and summary statistics for their voting and engagement over the previous year where available.

Ongoing cycle of manager engagement

Given that responsible investment is rapidly evolving, the Trustee expects most managers will have areas where they could improve. The Trustee therefore aims to have an ongoing dialogue with its managers to clarify its expectations and encourage improvements.

The Trustee reviews the information outlined above to identify any concerns, for example where the managers' actions are not aligned with its views. Where there are concerns, the Trustee typically seeks further information through its investment consultants. If a concern is confirmed, it will consider what further action is appropriate.

Implementation statement including most significant votes

Following the end of each Scheme year, the Trustee prepares a statement which explains how it has implemented its Statement of Investment Principles during the year. The Trustee publishes it online for its members to read.