Statement of investment principles
October 2019 to March 2022
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Introduction

1.1 The Trustee of the National Employment Savings Trust (Nest) has produced this Statement of Investment Principles (SIP), which sets out how the Trustee invests the assets of Nest for the scheme’s default investment strategy and the additional investment fund choices scheme members can make.

1.2 This SIP has been prepared in accordance with all relevant legislative and best-practice guidelines. It outlines the principles and policies governing investment decisions made by or on behalf of the Trustee for the management of Nest’s assets, in respect of the default arrangement and the additional investment fund choices scheme members can make. It should be read in conjunction with our latest quarterly investment report.

1.3 This SIP will be reviewed by the Trustee and the Members’ Panel and Employers’ Panel every three years, and without delay after any significant change in the investment approach or the demographics of the scheme.

1.4 Before revising this SIP, the Trustee will obtain and consider the written advice of a person who is reasonably believed by the Trustee to be qualified by their ability in and practical experience of financial matters and to have the appropriate knowledge and experience of the management of the investments of trust based pension schemes. The Trustee will also consult with the Members’ Panel and Employers’ Panel on proposed revisions to the default investment strategy and additional investment fund choices scheme members can make before any SIP revisions.
Governance of the Nest Trustee

2.1 Investment powers and compliance with the Pensions Act 1995
The Nest Order 2010 gives the Trustee the sole power to invest the assets of Nest.

2.2 Nest’s assets, representing the balances on members’ pension accounts, will be invested in the best interests of Nest’s members and beneficiaries both for the default strategy and for any other investment choices members may make. In the event of a potential conflict of interest the assets will be invested in the sole interest of members and beneficiaries.

2.3 The Trustee’s policy for securing the assets is invested in members’ best interests and is determined following extensive and continuing research into scheme member characteristics, circumstances and attitudes. This research is a mixture of quantitative data on socio-economic characteristics of the scheme’s membership, qualitative research into members’ attitudes and aspirations for their retirement savings, and increasingly, management information about our members’ savings patterns and behaviour.

2.4 Where significant changes to the scheme membership are detected the Trustee reviews the appropriateness of the default strategy and additional investment fund choices accordingly.

2.5 With the Trustee’s understanding of members’ best interests, it has decided upon an investment approach that provides:
- a default fund (through a series of Nest Retirement Date funds) designed to provide appropriate outcomes for members retiring in different years
- a choice of other investment funds for scheme members who do not wish to invest in the default fund.

2.6 The Trustee is ultimately responsible for the governance and investment of Nest’s assets but may delegate certain decisions to appropriate committees, the Chief Investment Officer (CIO) and external investment fund managers.

2.7 The Trustee is satisfied due to regular reporting, trustee skills audits, ongoing training and continuous professional development, that it, the respective committees and the CIO, have sufficient expertise, information and resources to carry out their roles effectively.

2.8 In preparing this SIP for both the default arrangement and the additional investment fund choices scheme members can make, the Trustee has considered written advice from the CIO who is qualified to provide this advice by his ability and practical experience of financial and pension scheme matters.

2.9 The Trustee has established an investment committee to consider, make decisions and provide oversight on investment issues. The delegated powers provided by the Trustee to the investment committee comprise of both issues on which the committee can make decisions, and issues on which it makes recommendations to the Trustee. The terms of reference can be found on our website.

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2.4 Where significant changes to the scheme membership are detected the Trustee reviews the appropriateness of the default strategy and additional investment fund choices accordingly. Details of our member investment research can be found on our website.

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2.10 Nest has an in-house investment team led by the CIO. The in-house investment team has certain powers delegated to it by the investment committee within pre-agreed frameworks. These include asset allocation, fund manager selection and monitoring, investment performance reporting, investment risk management, the scheme’s policies in relation to financially material considerations over appropriate time horizons and stewardship activities over the assets held on behalf of its members. The in-house investment team is also delegated responsibility to ensure and report to the investment committee that its investment powers are exercised in a manner calculated to ensure security, quality, liquidity, profitability.

2.11 The following sections, except where explicitly referenced, sets out the Trustee’s policies in relation to the types of investment, the balance between such investments, the associated risks and the expected return on those investments in the context of both the default arrangement where most of Nest members reside, and the other investment fund choices scheme members may make.
Day-to-day management of Nest’s assets (default and non-default)

3.1 The day-to-day management of Nest’s assets is performed by external professional fund managers. The investment committee and Nest’s CIO are satisfied that the appointed fund managers have sufficient expertise and experience to carry out their role.

3.2 Fund managers are monitored on a regular basis and performance is reported to the investment committee quarterly. The appointment, and dismissal of fund managers is the ultimate responsibility of the investment committee, based on recommendations from the CIO. The monitoring of fund managers is the responsibility of the CIO with oversight by the investment committee.

3.3 Their activities are defined and constrained by detailed agreements. Fund managers have discretion to buy and sell investments within the terms of their agreements. Fees are negotiated individually when a fund manager is appointed and are reviewed periodically to provide ongoing value for money for members.

3.4 Fund managers are listed in the scheme’s annual report and accounts, which also contains information about investment performance, asset allocation and major investment decisions taken during the year.

3.5 The fund managers are selected through an open and transparent process run by the in-house investment team. The process aims to achieve best value for money for members. Professional advice from the Trustee’s external and Financial Conduct Authority authorised investment advisers is obtained and considered in the selection of these funds and fund managers. As part of this selection, a due diligence process is performed to ensure that the assets are invested with sufficient security and liquidity and that each of the fund managers is of the appropriate quality and calibre to ensure the quality and profitability of the assets. The ongoing monitoring of these funds and fund managers is delegated to the CIO and in-house investment team, to ensure all investments are undertaken in accordance with the Trustee’s powers of investment.
Types of assets held
(default and non-default)

4.1 The Trustees invest in a mix of real and monetary assets and a mix of pooled and direct investment vehicles, deemed suitable for pension schemes, balancing expected returns against volatility. The investment committee regularly monitors Nest’s funds to ensure that:
— they invest primarily in regulated markets
— investment in non-regulated markets is kept to a prudent level
— derivatives are used in a prudent and appropriate way to manage risk or manage the portfolio more efficiently and without excessive risk exposure to a single counterparty or other derivatives.

4.2 The Trustee carries out due diligence and take advice from their in-house investment team and may also take advice from their investment advisers to ensure new areas of investment are appropriate.

4.3 The investment committee has agreed with the CIO, a set of asset class ranges within which the in-house investment team can invest. Any proposal to amend these ranges must be agreed in advance with the investment committee.

4.4 The detail of the current asset allocation for the scheme’s default investment strategy and the additional investment fund choices scheme members can make, is published via the quarterly investment report on the Nest website.

The balance between different types of investments
(default and non-default)

5.1 Long term strategic asset allocation is driven by the specific characteristics of the scheme, in particular its demography, and members’ capacity and appetite for risk. The trustee also considers long term projections of the likely performance of different types of investments in different economic conditions.

5.2 The scheme’s strategic asset allocation is reviewed on an annual basis. The methodology for changing the strategic asset allocation is periodically revisited to ensure that changes to the strategic asset allocation are appropriate.

5.3 The investment committee is responsible for ensuring both the default strategy and the additional investment fund choices scheme members can make are, as far as practicable, sufficiently diversified so as not to be reliant on any particular asset class, issuer or group of undertakings. The investment committee is responsible for ensuring that investments in assets issued by the same issuer or by issuers belonging to the same group do not expose Nest members to excessive concentration of risk.

Liquidity
(default and non-default)

6.1 The liquidity profile of the investments is regularly reviewed. The majority of the scheme is invested in liquid assets. Some investments, such as property, are less easy to sell. Such illiquidity normally allows the Trustee to capture an improved return and is not expected to constrain their investment decisions.
7. The Trustee recognise that the scheme is exposed to a number of investment and operational risks. They give qualitative and quantitative consideration to these risks when deciding investment policy, strategic asset allocation, the fund manager structure, choice of fund managers, the terms of their agreements and other aspects of the ongoing management of the scheme.

7.2 The scheme maintains a risk register of the key risks, including investment risks, to which it is exposed. The register rates the impact and likelihood of the risks, and summarises existing mitigations and additional actions. It is reviewed quarterly by the investment committee. Further details on the types of risks identified are shown in Annex 1.

8. Expected return on investments (default and non-default)

8.1 The types of investment chosen by the scheme are selected and combined with the aim to achieve the specific objectives of the default strategy and the additional investment fund choices scheme members can make.

The Trustee seeks to take account of financially material considerations in the selection, retention and realisation of investments. The key inputs in setting the investment strategy are the long-term capital market assumptions of expected return and expected (volatility) risk. These capital market assumptions incorporate long-term forecasts of the key drivers of risk and return including economic growth, inflation and asset values.

The investment team reports to the investment committee on a quarterly basis the risk and return characteristics of the Retirement Date portfolios and additional investment fund choices, and how each third-party manager is delivering against their specific mandates.

8.2 Risks and opportunities are assessed for materiality and impact within a broader risk management framework, which takes account of the Trustee’s investment time horizon for a diverse member demographic. While our focus is predominantly long-term as is appropriate for a pension scheme, the risk management framework allows us to consider a variety of risks including the short to medium term outlook for economic growth and inflation as well as currency, interest rate and political risk.

9. Realisation of investments (default and non-default)

9.1 The Trustee will realise assets following member requests on retirement or earlier where required. In selecting assets, the Trustee considers the liquidity of the investments in the context of the likely needs of members.

10. Investment beliefs (default and non-default)

10.1 The Trustee has established a set of investment beliefs to provide an objective and transparent framework for consistent decision making. These beliefs act as a guide to enable effective delivery of all investment functions. The beliefs and the rationale behind them can be found at Annex 2.
Investment aims and objectives for the default strategy

11.1 The Trustee’s overarching investment objective for the default strategy is to target investment returns in excess of the Consumer Price Index (CPI) after all charges over the long term. The Trustee has selected types of investments and the balance between these investments to meet this return objective.

11.2 To support this overarching objective the Trustee has also agreed the following sub-objectives:

— to maximise the pension income and other pension benefits at retirement by taking appropriate risk
— to seek to deliver similar outcomes for cohorts of scheme members who have similar contribution histories
— to aim to dampen volatility in members’ pension accounts.

The Trustee recognises that there will at times be tensions between these supporting objectives and will seek to find an appropriate balance between them.

Delivering the investment objective for the default strategy

12.1 The Nest scheme and its default investment approach have been designed to ensure that scheme members who do not wish to take an active role in how their contributions are invested can do so in confidence. The availability of a well-constructed default strategy is an essential part of auto enrolment and is central to Nest’s investment approach.

12.2 Investment risk should be taken in varying amounts throughout a member’s time saving with Nest. The Trustee has therefore adopted a series of target date funds called the Nest Retirement Date Funds to deliver the default investment strategy. Each Nest Retirement Date Fund has an asset allocation that is consistent with the expected amount of risk that is appropriate for the age of a member and/or their expected retirement date and the amount of return required to meet the investment objectives of the Retirement Date Funds.

The default strategy glide path

13.1 The varying allocation between return seeking and income seeking assets through time is known as the ‘glide path’. The Trustee has split the glide path into three phases:

— the foundation phase
— the growth phase
— the consolidation phase.

13.2 The foundation phase refers to the early years of younger scheme members’ working lives as they develop the savings habit. This phase typically lasts five years. The objective for the foundation phase is to keep pace with CPI after all charges.

13.3 The growth phase is where the maximum growth in assets is being targeted through investing in asset classes that are expected to grow in value relative to inflation more than other investments. The objective for this phase is to outperform CPI plus 3 per cent a year after all charges over the long term.

13.4 The consolidation phase prepares a scheme member’s assets for retirement and typically begins ten years before their Nest Retirement Date Fund matures. Investments in this phase are progressively switched out of higher risk assets. The primary objective of the consolidation phase for funds maturing after 2020 is to outperform CPI after all charges while aiming to progressively dampen volatility as a scheme member’s fund approaches maturity. For Nest Retirement Date Funds maturing through 2020, the consolidation phase objective is to manage the risks associated with converting a member’s accumulated savings into a cash lump sum.
Responsible investing (default and non-default)

14.1 The Trustee considers sustainable investment factors, such as (but not limited to) those arising from environmental, social and governance (ESG) considerations, including climate change, in the context of the broader risk management framework. One of the Trustee’s investment beliefs is that, as long-term investors, incorporating ESG factors is integral to the investment management process.

14.2 The Trustee requires its fund managers, where appropriate, to have integrated ESG factors as part of their investment analysis and decision making process. Fund managers are monitored on a regular basis by the investment team with this regard. On an annual basis the investment committee receives a report on the fund managers’ voting performance and approach to responsible investing more generally.

14.3 The Trustee expects fund managers, where appropriate, to have integrated climate risk into their risk analysis and investment process and, where appropriate and practical, we will take it into account in the selection of new fund managers. When monitoring the performance of our fund managers, we will also regularly consider how they are performing with reference to climate risk issues.

14.4 The Trustee has an active policy of soliciting member views on non-financial matters in their investment decision making for one of the non-default investment funds – the ethical investment fund choice strategy. These views are taken into account in the selection, retention and realisation of investments in the ethical fund. The Trustee does not currently take into account member views on non-financial matters in the selection, retention and realisation of investments for the other additional investment fund choices.

14.5 The Trustee does not currently take into account member views on non-financial matters in the selection, retention and realisation of investments for the default investment strategy, as they have provided additional investment fund choices where member views on non-financial matters can be sought and expressed.

14.6 The Trustee surveys members about its responsible investment approach in general and provides to members and stakeholders an annual report on its responsible investment activities.
Responsible investing - stewardship
(default and non-default)

15.1 The Trustee has a duty to act responsibly with regards to the assets it owns on behalf of Nest members. The Trustee believes that in order to fulfil this duty and to protect and enhance the value of Nest’s investments over the long term, it must act as a responsible and vigilant asset owner and market participant.

15.2 As part of this duty the Trustee, or its agents on its behalf, exercises its ownership rights, including voting and engagement with investee companies on matters including performance, strategy, risks, social and environmental impact and corporate governance in order to safeguard sustainable returns in the long term. How the Trustee expects its voting and engagement rights to be exercised is set out in a scheme specific voting and engagement policy.

15.3 Nest takes its responsibilities as an asset owner seriously. As clients, we work closely with our fund managers to help us support good corporate behaviour. Part of our procurement process for choosing fund managers involves ensuring their voting policies are well thought out and documented. Having our own policy enables Nest to document our position and expectations to our fund managers on good corporate behaviour. We use it to monitor and hold our fund managers to account on the decisions they make. Having our own established policy in place helps us have healthy discussion and debate with our fund managers. We always seek to vote and engage in the interest of our members and encourage our fund managers to consider our voting policy in their voting decisions.

15.4 Where we have direct voting rights we work closely with our proxy voting agent to ensure Nest’s voting intentions are delivered in line with Nest’s voting policy.

15.5 Each year we publish a voting summary report setting out how all our fund managers have voted and how this compares to Nest’s voting policy. We report the votes our fund managers make every quarter.

15.6 In addition to engaging directly with companies, Nest’s in-house investment team also undertakes joint engagements with our fund managers, and other pension schemes. The in-house investment team works on the scheme’s behalf to engage with public, industry and regulatory bodies in the various markets in which the scheme invests to promote better practices.

15.7 Given the systemic nature of climate change, we seek to discharge our duties by robust engagement alongside our fund managers with investee companies to encourage alignment with a low carbon economy and with policy-makers and governments to advocate for the same.

15.8 The Trustees have signed up to the UK Stewardship Code and the UN supported Principles for Responsible Investment (PRI).

15.9 The Trustee reports to its members and stakeholders on its stewardship activities through its annual responsible investment report.
Policy on divestment

16.1 In general, divestment or exclusion goes against our principles of stewardship and responsible investment. However, in certain rare circumstances we believe it’s merited for the reasons set out in our divestment policy.

Further detail of our divestment policy and how it is implemented can be found on our website.

16.2 Nest supports internationally recognised norms of corporate practice. As such we actively seek to avoid investing in companies such as those directly involved in the production or sale of cluster weapons, anti-personnel landmines or chemical and biological weapons.

Additional investment fund strategy choices

17.1 Some members may wish to choose an alternative to the default strategy. The Trustee provides a focused choice to meet the identified member needs. The fund choice strategies currently include:

- **Nest Higher Risk Fund**
  Invests in return seeking assets

- **Nest Lower Growth Fund**
  Invests in very low volatility assets

- **Nest Ethical Fund**
  Invests primarily in ethical securities and ethical property

- **Nest Sharia Fund**
  A fund with an investment approach based on Islamic law

- **Nest Pre-retirement Fund**
  Invested for those who wish to buy an annuity in the near future.

17.2 The Trustee may add, change or remove any fund choice strategies in accordance with the terms set out in Nest’s Order and Rules.

17.3 The Trustee endeavours that, for members who choose an alternative fund choice strategy, the risk being taken in the fund also takes into account the expected retirement age of the member, where this is applicable and practicable.

Compliance with this SIP

18.1 The investment committee monitors compliance with this SIP on a quarterly basis. The trustee reviews the investment strategy is in line with the SIP on an annual basis and receives a written report from the CIO to this effect.
Annex 1

Risks

Inflation risk
The Trustee invests in a diversified range of assets which are likely to grow in real terms.

Pension conversion risk
In the consolidation phase, the Trustee increases the proportion of assets that more closely match how we expect scheme members to use their pots in retirement. This is particularly important in light of the changes introduced by ‘Freedom and choice’.

Market risk
The Trustee manages market risk primarily through investing in a diversified range of assets.

Counterparty risk
The Trustee, with the in-house investment team, its advisers and its fund managers, assesses and manages its counterparty risk.

Operational risk
The Trustee, with its suppliers, assesses and manages its operational risks.

Liquidity risk
As far as is practicable and necessary, the Trustee invests primarily in liquid assets which can be quickly realised as required.

Valuation risk
The Trustee invests primarily in liquid quoted assets in order to manage the valuation risk.

Environmental and social risks
These risk factors can have a significant effect on the long-term performance of the assets Nest holds. Where applicable these factors will be considered in the investment process.

Governance risk
This can have a significant effect on the long term performance of the companies we hold. Where applicable governance risk factors will be considered in the investment process.

Currency Risk
Investments denominated in currencies other than the scheme’s base currency carry the risk of adverse exchange-rate movements. Nest looks to manage currency risk by hedging a proportion of its foreign currency exposure back into sterling.

Reputational risk
The Trustee carefully selects its counterparties, manages its investments responsibly and considers all aspects of its reputation as part of its investment strategy.

Annex 2

Investment beliefs

1. As long-term investors, incorporating environmental, social and governance (ESG) factors is integral to the investment management process.
2. Taking investment risk is usually rewarded in the long term.
3. Diversification is the key tool for managing risk.
4. Risk-based asset allocation is the biggest driver of long-term performance.
5. Taking account of asset values and asset prices, economic conditions and long-term market developments enhances long-term performance and informs strategic decisions.
6. Indexed management, where available, is often more efficient than active management.
7. Good governance, including an appropriately resourced in-house investment function, is in the best interests of Nest’s members.
## Version record

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