Statement of investment principles

Implementation statement 2023/24

This statement shows how the Trustee followed and acted on the principles contained in our **Statement of investment principles** (SIP).

Every three months, our investment committee carefully checks we're investing for our members in a way that matches what we've set out in our SIP. The Board also conducts a review each year, confirming the investments we're managing are in line with the investment strategy outlined in the SIP.

The SIP was formally reviewed by the Board in July 2023 as part of our three-year cycle of assessing whether the default strategy and fund choices remain suitable for our membership.

The main updates to the SIP in July following the triennial review included:

- Updated investment beliefs
- Updated investment objectives
- Updated approach to how we do asset allocation

More information on these changes are detailed on pages 8 and 10 of the SIP.

The Trustee is satisfied all investments during the year were made in accordance with the SIP. This includes the activities listed in this report. Where there may be unfamiliar concepts or terms, we've included a glossary at the end of this document.

Day-to-day management of assets

This part of the SIP aims to ensure the Trustee has clearly defined processes in place to select and monitor external fund managers. The objective of these arrangements is to achieve good outcomes and better value for money for Nest Scheme members.

- Last year, Nest commissioned CEM benchmarking[1] to undertake a benchmarking exercise on our fund manager fees to check we are getting good value for our members. This was presented to the investment committee in July, showing Nest can demonstrate real value for money for the way our portfolio is managed.

Nest is confident the management of assets and Nest's arrangement with fund managers is sound and continues to operate in members' best interests.

Monitoring and governance

Nest has rigorous governance processes in place to reflect Nest's position as a publicly accountable Scheme. This ensures our investment and stewardship activities and processes are supported and overseen formally by the bodies responsible Nest's investment activities – the Board and investment committee.

[1] **Home | CEM Benchmarking**

The Scheme's investment team holds quarterly fund manager monitoring meetings to discuss managers' performance, update each other on key fund manager meetings and review any potential problems or breaches to the mandates, including performance in relation to environmental, social and governance (ESG) factors.

Where we have serious concerns, managers are placed on a watchlist and prioritised for engagement. The watchlist is reviewed every quarter and if concerns persist, we may decide to terminate a mandate.

- As of 31 March 2024, three fund managers were on this watchlist due to issues with investment strategies, performance and stewardship. We have discussed our concerns with them directly.

Nest has decided that in addition to the three-month review, a systematic 'deep dive' of individual fund managers should take place. This manages the risks associated with having long-term partnerships with fund managers – some of which have been in place for more than a decade – and ensures the mandate in place continues to be adhered to and Nest members are getting best value for money.

- A review of the UBS mandate took place in October 2023. UBS has been managing Nest's allocation to developed market equities since the Scheme started investing in 2011. The mandate has evolved over time as Nest's requirements have changed, most notably moving from a pooled to a segregated mandate, and from tracking a standard market cap index to a strategy jointly developed by Nest and UBS, incorporating climate tilts aligned with Nest's net zero targets. This was the first mandate to be put through the test and the outcome reaffirmed Nest's confidence in the successful partnership it has in place with UBS.

Nest also undertakes an annual review of Nest Invest's adherence to the Investment Management Agreement (IMA) in place between Nest Invest, which was established in January 2020, and Nest Corporation. Key questions asked include whether the services set out in the IMA have been successfully provided by Nest Invest to Nest Corporation over the year, and what evidence/assurance exists of this provision, and whether any breaches of the IMA have occurred during the year.

- In April 2023, Nest undertook a review of the IMA in place between Nest Invest and Nest. This was the third review of the IMA and concluded there were no breaches during 2022.

Creating Nest's default Target Date Funds

The Trustee has developed a new approach to asset allocation for the scheme's default fund. The Trustee this year is now using five portfolio building blocks in different proportions for each of the Nest Retirement Date Funds. The building blocks are: Illiquid Capital Preservation, Liquid Capital Preservation, Growth, Income, and Longevity Risk Management and are designed to meet specific member needs throughout a member's journey saving with Nest.

By varying allocations between growth-seeking, capital preservation and income-seeking assets, as well as varying the allocations to liquid and illiquid assets, through time, the Trustee aims to best meet members' different investment risk needs at different stages of life.

This graphic shows the different levels in creating Nest's Target Date Funds, in descending order: member funds, portfolio building blocks, asset classes.

Recent asset allocation changes

- Nest believes the gilt market now offers more attractive investment returns for its members than it has for a long time, particularly those wanting certainty of income around retirement. The Scheme met with existing Nest fund managers already helping it invest in developed market fixed income about accessing UK gilt strategies. Subsequently BlackRock and Royal London Asset Management were instructed in July 2023 to manage three gilt funds of varying maturity.
- Nest worked on gradually increasing the allocation to long gilts in both the Longevity and the Nest Guided Retirement Fund (NGRF) Later Life portfolios, which was achieved by reducing the Scheme's exposure to cash.

Further updates

- As of 31 March 2024, 64% of Nest's total investments were held in segregated accounts. This has helped to drive down investment costs, improve our control over how the investment fund mandates operate, and improve the way we can achieve our broader responsible investment ambitions and objectives of our climate change policy.

Types of assets held

This part of the SIP aims to ensure that when the Trustee invests in different types of assets and financial instruments, they are suitable for all Nest Scheme members at different stages of saving for a pension.

The Trustee is confident the Scheme's assets are mainly invested in regulated markets and that investments in non-regulated markets have been carefully considered and any risks suitably managed in the investment approach.

- As of 31 March 2024, the majority (83%) of Nest's total investments were in regulated markets.

Since January 2020, Nest Invest has provided authorised advice to Nest about new types of assets and the suitability of new fund managers we have appointed. A recent example includes providing a Section 36 letter to the investment committee in October 2023 on setting up a new thematic equity mandate, managed by Lombard Odier Investment Managers.

- In 2023, Nest undertook a procurement exercise to appoint a fund manager covering thematic equities. Thematic equity investment will allow Nest to invest actively in key themes such as climate change mitigation and adaptation, natural capital and social issues, that are likely to provide additional investment growth opportunities. Lombard Odier Investment Managers were appointed in February 2024 to manage this multi-thematic equity fund.

Nest has appointed Amundi to help manage our asset allocation more efficiently through the limited use of derivatives. Our Efficient Portfolio Management (EPM) fund uses short-term contracts to minimise a drag on performance for cash we've set aside for deployment in private markets, trades which often require larger contributions.

The use of derivatives is set out in the investment management agreement between Nest Corporation and Nest Invest, and Nest Invest continues to monitor the use of derivatives within the Scheme's overall portfolio.

- Some of Nest's fund managers used derivatives in the 12 months to 31 March 2024, primarily for foreign currency management and not leveraging of investment positions.
- As of 31 March 2024, Nest had a small, short position in developed market equity futures in our EPM fund which was equivalent to 0.65% of Nest's portfolio.

Ongoing procurements

In September 2023, Nest announced a procurement for a mandate investing in timberland. Nest Invest's research into the asset class has shown it offers additional diversification, and an alternative source of sustainable growth.

- To support the procurement process, Nest procured the services of an investment consultant with specific expertise in natural capital and global timberland & forestry. The investment consultant, alongside the Nest team, undertook a comprehensive due diligence process. This included visits to three sites managed by shortlisted managers to speak with staff and contractors on the ground. It gave the Nest team the chance to compare their approaches to managing and maintaining their forests, including the balance of clearance and new growth, positioning and size of fire breaks and proximity to communities, roads and mills. The successful fund manager/s will be announced in 2024.

The balance between different types of investments

This part of the SIP aims to ensure the Trustee considers the investment strategies for each of Nest Scheme's default fund strategies and the fund choices that members can make away from the default approach. This includes ensuring the funds aren't overly concentrated in one or similar types of assets.

The Trustee is confident the Scheme's portfolio offers suitable and sufficient investment options, and that the Scheme's default and alternative funds remain appropriately diversified across asset classes, geographical regions and fund managers[2].

- To demonstrate this diversification, the table below illustrates the asset allocation of Nest's 2040 Retirement Date Fund as of 31 March 2024. The proportion of the foreign currency exposure is hedged in our developed market credit funds, global developed equity fund and our private market funds.

[2] Nest's Sharia Fund comprises of one fund manager (HSBC) managing one mandate (Islamic Global Equity Index fund). We are currently reviewing this arrangement to consider whether further diversification is needed.

Equities
- 47.0% Climate aware global developed equities
- 5.0% Climate aware global emerging market equities
- 2.6% Private equity

Growth Credit
- 4.3% Emerging market debt
- 4.1% Global high yield bonds
- 4.0% Private credit

Real assets
- 0.9% Property income
- 6.5% Hybrid property (UK direct & REITs)
- 3.1% Infrastructure equity
- 2.7% Infrastructure equity – renewables

Investment grade bonds
- 4.3% Sterling corporate bonds
- 3.1% Short durations UK investment grade bonds
- 7.4% Global investment grade bonds
- 1.0% Short duration investment grade bonds
- 0.4% Short duration GILTs

Alternatives
- 1.2% Commodities

Cash
- 2.4% Low risk sterling liquidity
- 0.0%* Derivatives

**Derivative fund at 0.006%*

Over the last few years, Nest has further diversified the way we invest for members by increasing the Scheme's investment in private markets. This allows members to benefit from the additional expected returns available to investors in illiquid assets.

› Even though public markets surged towards the end of last year, the overall percentage that private markets represented in Nest's portfolio rose slightly to 17**%** as of 31 March 2024 (the allocation the previous year was around 16%). We expect to increase our allocation to private markets up towards 30% over the coming years.

Liquidity

It is important Nest has access to enough liquid assets to fulfil requests from members who want to withdraw from their pension pots, either because they're retiring, transferring to another scheme, or choosing a different Nest fund. This part of the SIP aims to ensure there is sufficient management of the liquidity of the Scheme's assets.

Nest is proactively checking liquidity across its portfolio, setting liquidity parameters for each of the five building blocks which are carefully monitored. This is coordinated by the newly created illiquidity committee, an executive sub-committee which makes key decisions on liquidity management across Nest's portfolio.

The committee generally meets on a monthly basis to review investment pipelines and cashflow positions, and on a quarterly basis for a full agenda of actions. Meetings are chaired by the Director of Public and Private Markets and regular attendees include the CEO of Nest Invest, CIO, and key personnel from across the investment and Corporation finance teams. The sub-committee is a key part of Nest Invest's internal investment governance framework.

› The illiquidity committee met in March 2024 and discussed issues with manager deal pipelines and cash flows. No significant issues were identified.

As Nest continues to increase its investment into private (more illiquid) markets to benefit from the typically strong, long-term performance these can provide, this will be balanced against the need for sufficient liquidity.

› Nest has good liquidity through a consistently strong cashflow, receiving around £500 million a month in member and employer contributions. The Trustee is confident there is sufficient liquidity to manage any member requests to take money out of the Scheme.

Realisation of investments

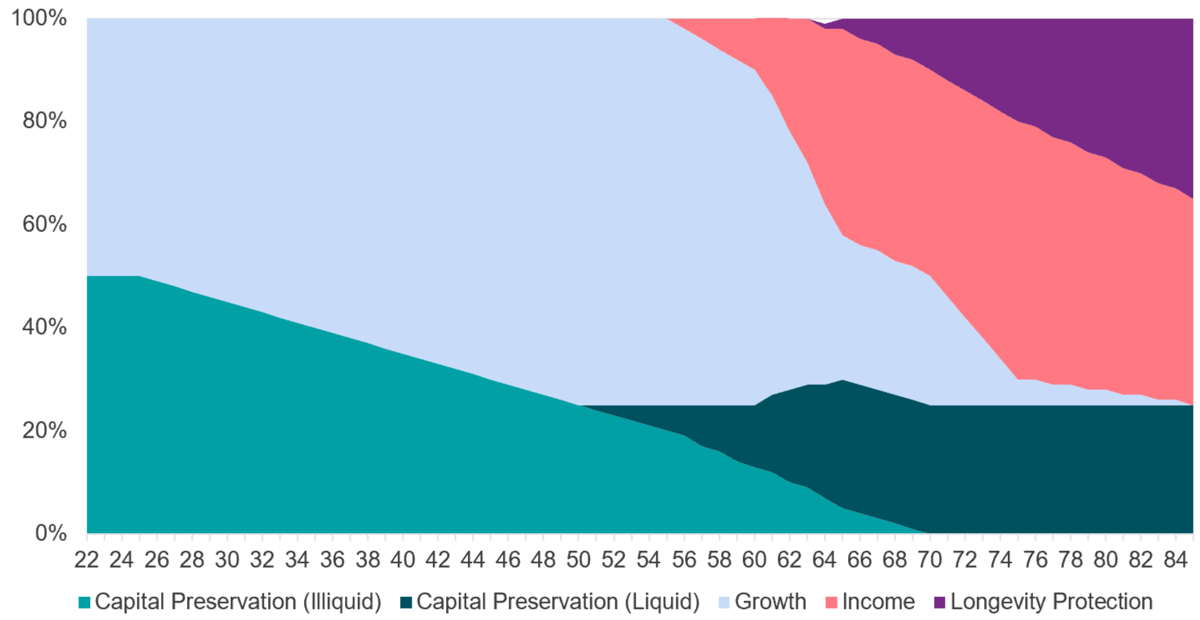
This part of the SIP aims to ensure the Trustee has considered members' long-term needs for later life.

The Trustee is comfortable Scheme funds are positioned appropriately for the level of demand from Nest members approaching retirement who are likely to withdraw their money from the Scheme.

› The number of members taking their money at retirement remains very low. This is to be expected given the relatively young age profile of the Scheme's membership.
› There was little member transfer activity in proportion to the Scheme's membership over the last year. Requests for transfers both in and out of the Scheme are being managed effectively.

Nest believes it has a fiduciary duty to help ensure members achieve good outcomes in retirement. There is research to show automatically defaulting members into cash or very low volatility assets is not the most suitable approach, given the changing nature of retirement and the desire for members to have flexibility into their later years.

To this end, Nest is in the process of updating the retirement journey for members in our retirement date funds – see the graph below for the eventual target member journey, bottom axis is the age of the Nest member.



As Nest members pass their designated retirement date, those in the default funds with less than £10,000 in their Nest pot are moved into the Post Retirement Date Fund which aims to grow members' savings in line with increases in the cost of living over the long term, after all scheme charges.

Since 2020, eligible members with more than £10,000 enter the Nest Guided Retirement Fund (NGRF) to meet members' income needs throughout retirement. NGRF is designed for members to make regular and sustainable income withdrawals up to the age of 85, leaving a separate pot that can be used by members at age 85 to purchase a guaranteed income for life in the form of an annuity (that income is designed to be consistent with the income they were previously drawing, to provide confidence to members throughout their retirement that their money won't run out). It also provides members access to emergency cash. NGRF offers flexibility as members can withdraw their pot in full, or choose a different retirement option, at any time if their circumstances change.

NGRF is market leading in that it continues to grow members' money in retirement and provides members with a sustainable and regular income managed by Nest. This gives members assurance that the income they are drawing is sustainable. However, NGRF has two notable limitations; it does not provide an in-scheme approach to income in later life as members are required to purchase an annuity on the open market; and it does not include any provision for members to share longevity risk. The absence of this means that members' incomes are likely to be materially lower than if the retirement income solution included longevity risk sharing.

Over the last 18 months, work has been undertaken to explore how the Scheme can further enhance its retirement proposition, focusing on the different ways Nest could implement longevity protection to deliver a lifelong retirement income to members. Nest has commissioned support from pension consultants with specialist expertise in longevity to support the next phase of this work.

Risk

This part of the SIP identifies the investment risks the Scheme faces. The Trustee reviews these risks annually and sets out how comfortable we are to take different types of investment risk on behalf of our members.

Nest manages many risks across its investment strategy through diversification, ensuring members' money isn't too concentrated in one asset class, sector, or region. This ability has been enhanced by the integration of the Aladdin risk management system early this year, allowing Nest to undertake greater and more sophisticated risk analysis.

The annual review of the investment performance principal risks has been completed and Nest is satisfied the Scheme is managing these risks appropriately. The Trustee is confident risks are being monitored and managed appropriately in accordance with the Scheme's stated risk appetites.

Overall structure

Every year, the Nest Corporation's Enterprise Risk team undertakes a deep-dive review of each of Nest's principal risks to ensure they remain relevant and appropriate to Nest. The annual deep dive of the Investment principal risk is reviewed by the investment committee before onward submission to the Board Risk sub-committee, as per the oversight arrangements set out in the Committee's terms of reference.

In addition, there is a newly created executive committee within Nest Invest, called the executive investment committee, with the primary purpose of considering new investment ideas, opportunities and proposals in the context of Nest's overall investment beliefs, investment strategy, risk and return objectives and cost budget. Members of the committee include CEO of Nest Invest, CIO, Nest Invest Directors and representative from the Market Risk and Asset Allocation team. The Committee meets on a monthly basis and is an advisory committee, created to support the existing governance framework.

- The executive investment committee this year discussed topics such as the attractiveness of US mid-market loans, how to introduce more diversification in the Sharia fund choice and the timberland procurement.

Environmental, social and governance risk

Responsible investment and stewardship are built into the core of our investment strategy. Every year we produce a **Responsible Investment report** showing how our investment beliefs and policies translate into the decisions we make, our engagement with companies and other organisations, and how this affects our members' money.

Our investment team has identified seven priority areas that guide our current work. These are derived using our prioritisation framework and are based on thorough research and analysis.

- climate change
- natural capital
- human capital

- human rights
- big tech
- diversity
- food

Nest sees climate change as a key risk facing all aspects of the Scheme's approach to investing for members. The **climate change risk policy** was first implemented in 2020/21 with the aim to align the Scheme's entire investment portfolio with the goals of the Paris Agreement. The policy has since been updated to reflect Nest setting short-term climate change targets, and climate change scenario projections impacting Nest's asset allocation. Both the policy's implementation and ongoing suitability is reviewed annually by Nest and progress is reported twice a year to the investment committee.

Nest Invest meets every quarter to review how the Scheme's portfolios in different asset classes are performing, how the markets are performing, and what investment risks and opportunities exist or could emerge, including those we monitor through our asset class dashboard. As part of this, we monitor the net zero alignment of the asset classes we invest in, as well as how our portfolios might be impacted by other ESG factors and what we might do to mitigate them.

- In March this year, a workshop was held for Nest's investment committee to discuss and hear the views on how the Trustee's climate change policy and implementation plan (the roadmap) should evolve and develop. The workshop considered new areas for inclusion in the policy, such as physical climate risks, nature and biodiversity and ways to strengthen existing approaches for climate opportunities and the Just Transition. This work will help shape Nest's evolving climate change policy, which will be updated in 2024.

The climate change roadmap outlines the progress in reducing the carbon footprint of the Scheme's investment portfolio. The roadmap also sets out future targets and activities to help Nest become net-zero by 2050 or sooner.

- 62% of Nest's total investments are now in climate-aware mandates.

In 2021, statutory regulation came into force relating to reporting in line with the Task Force on Climate-related Financial Disclosures (TCFD) recommendations to improve both the quality of governance and action taken by trustees to identify, assess and manage climate risk. Nest's latest **TCFD report** is on our website.

- Reflecting best practice highlighted by the Pensions Regulator (TPR) in its review of the first tranche of disclosures, we added to the data tables in the Annual TCFD report 2022/23 the percentage change in the financed emissions metrics from last year, and added more narrative around the direction of travel. An executive summary has also been added to help make the report more accessible to a range of potential readers.

The Scheme is part of various initiatives as part of our stewardship and active ownership practices, which help Nest review and monitor other ESG risks facing our portfolio, which can affect long-term investment performance. These initiatives cover issues including human rights, deforestation, diversity and inclusion, and responsible technology innovation and implementation.

- In 2023, Nest escalated our engagement with Barclays by co-filing a shareholder resolution for its 2024 annual general meeting. The resolution asked the company to issue a report describing how it is responding to the risk of stranded assets of planned new oil and gas infrastructure and assets. In response to this, Barclays highlighted that it was in the process of updating its energy policy and offered the opportunity for Nest and other investors to review the policy on a confidential basis, providing feedback ahead of publication. We reviewed several versions of the policy and recommended amends, which resulted in the policy being updated to include a commitment to stop financing new oil & gas expansion projects. Further information on this stewardship example, and others, can be found in the latest Responsible Investment report.

The Scheme also has specific and limited purposes screens in place. These include:

- Nest applies a controversial weapons screen to its portfolio, meaning we do not invest in companies directly involved in the production or sale of cluster weapons, anti-personnel landmines or chemical and biological weapons.

   - A triennial review of Nest's policy on controversial weapons was undertaken during the year and discussed with the investment committee in April 2024. The review showed the exclusions working as expected and there were no proposed major changes to the policy.
- Nest divested from companies that derive more than 20% of their revenues from thermal coal production and/or power generation, oil sands and arctic drilling. Nest has stepped up this level of divestment to include all companies with more than 10% of revenues from these activities. We believe these activities are not compatible with a transition to 1.5C, and that companies deriving significant revenues from these activities will struggle to transition quickly enough to the low carbon economy. In total, 133 companies that make more than 10% of their revenues from thermal coal production and power generation, arctic exploration and oil sands were removed from our portfolio by the end of 2023.
- A portfolio-wide exclusion on companies deriving more than 10% of their sales from the sale of tobacco. The annual review of our **tobacco position** and the letters of assurance from relevant fund managers ensure Nest is confident the Scheme's tobacco exposure remains at zero weight. Nest recently reviewed the implementation of its approach to tobacco free portfolios and are satisfied that the portfolio continues to remain tobacco free.
- To mitigate our exposure to ESG risks in some of our investments, Nest implemented a United Nations Global Compact (UNGC) screen within our emerging market equities fund in 2014. The UNGC aims to mobilise the global business community to contribute to sustainable development the principles cover key areas such as human rights, labour standards, environmental protection, and anti-corruption measures. Companies that breach these principles may face legal, reputational, and operational risks. As a result of the screen, we divested from several companies found to have severe direct involvement in forced labour in the Uyghur region.
- This year Nest developed a portfolio wide policy requiring our segregated fund managers to screen our portfolio, using a third-party data provider of their choice, to identify companies that have been assessed as violating or having potentially violated one or more of the UNGC principles. Where violations do occur, we set expectations for our segregated mandate public market fund managers to engage with said companies to get further insights into the breaches and encourage corrective action. By having a screen in place, Nest can assess the ESG risks associated with the investment and work with fund managers to make informed decisions when breaches occur.

Expected returns on investments

The Trustee sets the investment strategy and objectives for the default Nest Retirement Date Funds and the Scheme's other fund choices for members. This part of the SIP describes how the investment strategy is monitored and assessed against longer and shorter-term time horizons.

On a triennial basis, the Board reviews scheme member characteristics, circumstances and attitudes. This is then used to set the overarching investment objectives and design the member journey.

The SIP was updated in July 2023 to set out the new overarching investment objective for the default strategy: **Delivering the best retirement income for as many as possible**.

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

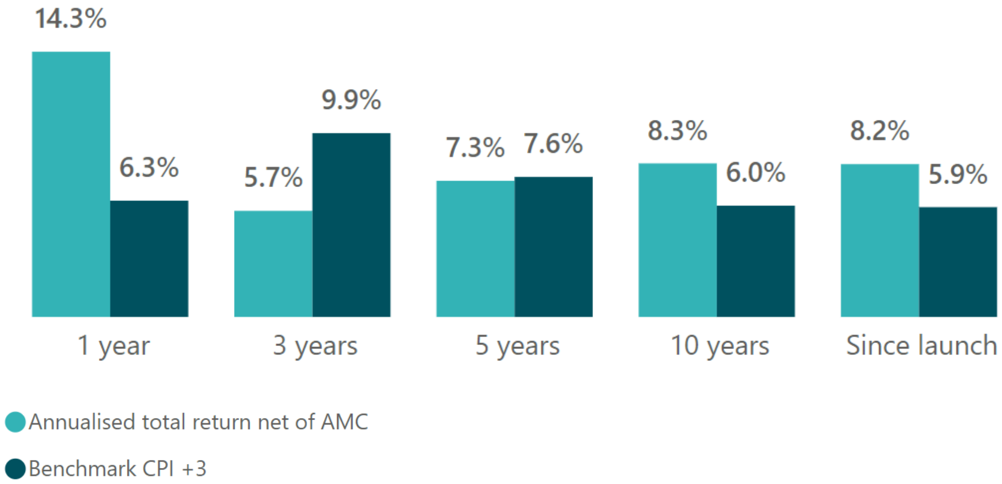
- Grow member savings faster than inflation (CPI) after all charges during a member's working life.
- As a member approaches retirement invest to deliver a predictable retirement income.
- Provide members with a smooth transition between their working and retirement years.
- Deliver similar outcomes for cohorts with similar contribution histories and similar ages.

These new investment objective and sub-objectives guide Nest's approach to its default investment approach, to ensure that members who do not wish to take an active role in how their contributions are invested, can do so in confidence.

- In addition to setting new objectives, the investment committee approved a new approach to strategic asset allocation, drawing on member research, to provide a more bespoke approach to asset allocation throughout a members' time saving with Nest. This is currently being finalised and will take some time to fully implement but the key aspects are now in place and operating effectively.

On an annual basis using the new approach to asset allocation Nest reviews the strategic asset allocation to assess the probability of different portfolios meeting the overall investment objective and specific targets for the five building blocks and overall member outcomes in different stages of their savings career with Nest.

- The graph below outlines the investment performance of Nest's 2040 Retirement Fund (default strategy, growth phase), featuring data as of 31 March 2024.



- Further information on the performance of Nest's alternative member funds can be found in the quarterly **fund factsheets** we produce.

The Trustee is satisfied the Scheme's funds have been invested in a way that has a reasonable expectation of meeting the Scheme's objectives over the long-term.

Responsible investing and stewardship

This part of the SIP sets out the Trustee's beliefs and policies with regards to managing ESG risks and seeking opportunities. It also sets out where we seek to incorporate Scheme members' views, and how we act as a responsible and watchful asset owner on behalf of our members.

Included in the recently updated SIP are investment beliefs that were revised in 2023, as part of our triennial review to check our investment beliefs remain relevant. Two of the revised beliefs specifically cover the importance of responsible investing and stewardship.

Incorporating and acting upon climate risk and other environmental, social and governance (ESG) factors is a significant driver of investment outcomes.

- Integrating sustainability factors into our investment process, from asset allocation and benchmark construction to manager selection and risk management, supports the identification and ultimately the pricing of ESG risk and opportunity.
- Capital allocation by investors and corporations can make a difference in how ESG risks play out and is particularly effective when aligned with policy and regulation.

Acting as responsible long term stewards has a positive and broad impact on member outcomes.

- Where portfolios are well diversified, performance is broadly determined by the global economic systems in which investees operate – engaging with companies, fund managers, and policy makers to improve financial markets and influence the long-term health of these systems is in our members' best interests and part of our fiduciary duty.
- We consider the impact of our investments as an economic actor in our own right and as part of a wider investor community. We believe we can deliver on our investment objectives and have a net positive impact on externalities that affect members' investments and retirement outcomes.

The Trustee is satisfied relevant ESG issues were taken into account in 2023/24. Four people within the investment team have the direct responsibility for researching and managing Nest's responsible investment activities, but increasingly all Nest investment team members are integrating ESG factors and responsible investing principles within their day-to-day activities.

A full breakdown of how the Trustee manages ESG risks in the portfolio, including how the Scheme implements our voting and engagement policy and acts as an active steward of members' money, can be found in the latest annual **Responsible Investment report**. A selection of this wide-ranging activity is outlined below.

Voting

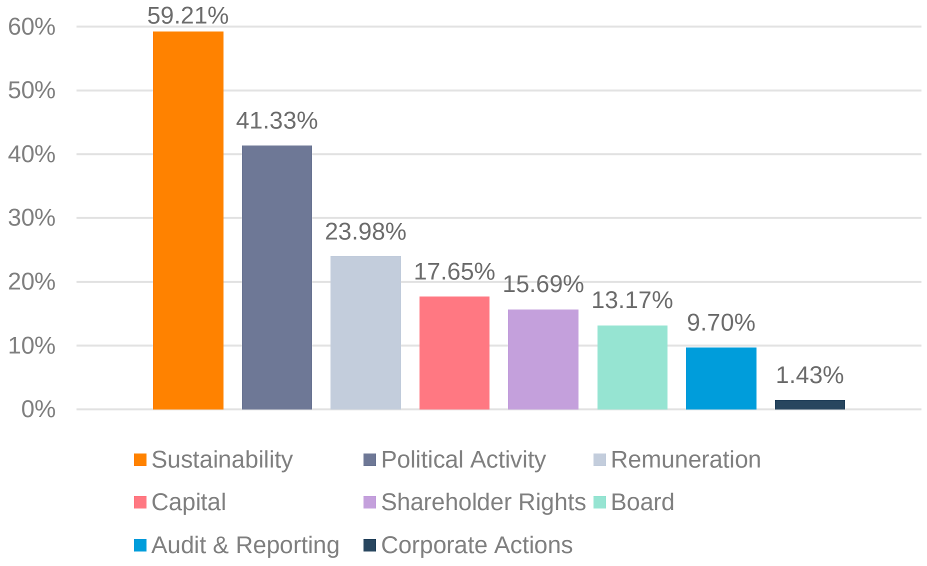
Buying shares gives Nest's membership part ownership of that company and usually gives us the right to vote at their annual general meeting (AGM), where key issues on how the company is run are discussed. Nest continues to employ the proxy voting service, Minerva Analytics, to best utilise the voting rights available to the Nest Scheme. Its vote management tools allow the Scheme to efficiently identify shareholder and management resolutions of concern or interest and allow us to vote electronically on them.

Minerva Analytics also helps us monitor the voting intentions of our fund managers so we can check they are voting in line with our views (or to prompt a discussion if they are planning to vote in a different way), as set out in our voting and engagement policy. The exercise of these votes is published quarterly on our website and annually in our Responsible Investment report.

- Every year, Minerva Analytics Ltd carries out a review of Nest's shareholder voting. The last report was published in August 2023 and covered the 2022 shareholder voting season. A report covering the 2023 voting period will be published in 2024.

Given the short period in which AGMs occur, it's not possible to provide detailed analysis for every vote where our fund managers' voting intentions differ from our own policy. We therefore focus on our largest holdings to scrutinise how our fund managers are exercising votes on issues that are most significant to us. UBS Asset Management (UBS) also leads on engagement with the poorest-performing companies in our climate-aware world equity fund, based on carbon emissions, or a lack of clear plans or strategy to manage the transition to net zero. This helps us maximise the effectiveness of our involvement to help reduce the carbon risk our members face, which is likely to translate into poorer performance and negatively impact member incomes in retirement.

- Over the last year, 41,517 votes were cast on our behalf, primarily at company AGMs, with 18% being against management. The graph below shows the Scheme's votes against management by category.



- During the last voting season (2023), Nest overrode our fund managers' voting intentions 156 times to better align our votes with our policy and beliefs. If we override our fund managers to vote against management recommendations, we engage with the company directly. In the last year, we wrote letters to several companies to explain our voting decisions and areas of concern, seeking resolution or ongoing dialogue. Notable examples of our voting overrises include:

  <u>Antimicrobial resistance (AMR) at McDonald's</u>

  McDonald's had not achieved its goal announced in 2018 and 2020 to prohibit routine preventive use of antibiotics by meat suppliers and reduction targets for medically important antibiotics across 80% of its global beef supply. As a result, Nest supported two shareholder resolutions at its 2023 AGM requesting that McDonald's board reports to shareholders on the adoption of an antibiotics policy, and that the board instate a policy that complies with World Health Organization (WHO) standards on the use of medically important antimicrobials in animals throughout McDonald's supply chain.

  <u>Remuneration and workforce pay at Walmart</u>

  We overrode our fund manager's voting decisions on a shareholder resolution requesting that Walmart enhance its processes for setting targets on chief executive officer (CEO) compensation, by taking into consideration the pay levels of Walmart employees across all levels. We voted in support of this shareholder proposal as we believe that executive remuneration should be determined within the context of broader workforce pay, and take into account pay levels of equivalent sectors, and wider public concerns.

Examples of Nest's voting activity can be found in the latest Responsible Investment report. Notable high-profile votes cast by Nest include:

- During the 2023 AGM season, Nest challenged BP's decision to scale back their oil and gas production and emission reduction targets. Nest voted against the reappointment of BP's chair Helge Lund as a protest against the poor corporate governance not to give shareholders a chance to vote on the revised climate targets, and against the targets themselves.
- Following engagement with Shell last year, we were disappointed to see the company announce changes to its production targets - it had previously suggested that oil production would fall by 1-2% per year until 2030, but it would now be kept stable. We therefore decided to escalate our engagement by co-filing a shareholder resolution with Follow This and 27 other institutional investors. The resolution asked Shell to align its medium-term emissions reduction targets covering the use of its energy products (scope 3) with the goal of the Paris Climate Agreement of limiting warming to well-below 2C and pursuing efforts to limit warming to 1.5C. At the annual general meeting in May 2024, 19% of investors voted in favour of the shareholder resolution, while 22% of investors voted against Shell's new energy transition targets.

Stewardship

- Over the past year, Nest engaged directly, through correspondence and/or attending meetings with management, with 36 companies. In particularly, Nest and our external fund managers have engaged with 110 companies on climate change.

The Scheme participates in wider initiatives to help fulfil our stewardship responsibilities, including being a member of, or signatory to, ShareAction's Good Work Coalition, the Asset Owner Diversity Charter, 30% Club UK Investor Group, Workforce Disclosure Initiative and Global Canopy's deforestation-free pensions guidance working group. Additional initiatives to be added based on Nest's responsible investment report.

- In the last year, the Scheme has also joined the Financing a Just Transition Alliance (FJTA), an investor group on the Just Transition that is led by the LSE Grantham Research Institute. Our association will help the Scheme benefit from the resources FJTA have available, helping us further develop our policies on the Just Transition. A full list of new initiatives Nest has joined can be found in the latest Responsible Investment report.

The Scheme was among the first signatories of the Financial Reporting Council's new UK Stewardship Code 2020. The Code comprises 12 principles on reporting stewardship activities and outcomes that asset owners like Nest must demonstrably meet.

- In February 2024, the Scheme maintained our status as a signatory to the Stewardship Code.

Nest is willing to escalate engagement with companies we feel are not managing specific risks to their business and are not suitably engaging with us, or our fund managers, on how they're managing the issue. Examples of Nest's stewardship engagement can be found in the latest Responsible Investment report.

- Working closely with ShareAction, and building on Nest's stewardship activity last year, the Scheme continued to exert pressure on Barclays in developing a robust climate policy. A shareholder resolution was filed with a number of conditions for withdrawal, including that Barclay's energy policy reflects the feedback provided to the bank on the policy itself and that there's an annual meeting between Barclay's CEO and the investor co-filing group. In February 2024, these conditions were met and the resolution was withdrawn. There is more Nest would like from Barclays, particularly in setting Scope 3 emission targets, and engagement with the bank will continue.

Other activities

Nest has prepared responses to a number of regulatory investment consultations over the past year. A list of the times Nest has responded to consultations and advocating for better standards can be found in Nest's Responsible Investment report. Notable examples include:

- The Scheme submitted in January 2024 a response to guidance on the FCA's anti-greenwashing rule (GC 23/3). Nest used this opportunity to express our support for a general anti-greenwashing rule, and welcomed the opportunity to respond to this additional consultation on guidance for FCA-authorised firms that make claims about the sustainability of a product or service.
- The Taskforce for Social Factors convened by DWP released a guide for consultation with the UK pensions industry, which includes recommendations about how social factors can be better incorporated into investment decisions. Nest submitted a response to this consultation in support of the taskforce and advocating for a greater amount of detail in relation to certain social factors.

Additional information

Investment fund choices

This part of the SIP makes provision for the establishment and oversight of other fund choices within the Scheme.

Nest is continuing work to review the overall fund choice available to members, with a view to ensuring our additional fund choices (outside of the Scheme's default offering) meet our member needs. Nest recognises some Scheme members will want to prioritise ethical and religious beliefs or want to take a different level of investment risk in how their pension is invested. Alternative funds offered by the Scheme are the Ethical Fund, Sharia Fund, Higher Risk Fund, and Lower Growth Fund. Any member can switch between these funds, free of charge.

Nest consults with its members to gather their views on a range of topics, including how they feel about being invested in certain types of industry. In 2023, we gathered feedback from members in the Ethical Fund, Higher Growth Fund and Sharia Fund about their perceptions of fund choice at Nest, their reasons for switching funds and their views on the fund they have chosen.

- Our research identified that members who have made a fund choice are more engaged with Nest and hold stronger perceptions of Nest as a pensions provider compared to those in the default fund.
- Higher Risk Fund members are largely driven by the search for better returns. Members of this fund are more likely to be male and have a higher income than members in Nest’s default fund or other fund choices.
- Ethical Fund members want to invest according to their values and in a way that benefits the environment and society. Younger members in particular seek information about climate change before choosing the Ethical Fund.

Our member research is taken into account when we consider how to improve and evolve our fund choices. Over the next year we intend to add an additional diversifying asset class to our Sharia Fund accompanied by suitable member communications. This aligns with our investment objective to ensure our funds are sufficiently diversified as far as is practicable.

Governance

The Pensions Act 2008 required Nest to establish an Employers’ Panel and a Members’ Panel. The purpose of these panels is to allow employers and members to tell Nest what they think about Nest and what’s important to them, to make sure that their voices are heard.

- The Panels are a sounding board for ideas and suggestions proposed by Nest. They provide challenge and recommendations on key issues to make sure that specific member and employer concerns are raised at Board level. They are also consulted when Nest reviews the Statement of investment principles (SIP) - the Panels were regularly consulted when we reviewed the member demographic and attitudes evidence.
- The input from both Panels was sought when we proposed new investment objectives and member investment journey paths. When this work was incorporated into changes made to the SIP in 2023, both Panels were further consulted and their feedback was presented to the Board when discussing the changes to the SIP.

Glossary

Asset

Something of economic value that an individual, an organisation, a corporation or a government owns, for example, a piece of property, a share in a company or a building or machinery.

Annual general meeting (AGM)

Most shares in publicly traded companies give their owners a right to vote on some company decisions, including on issues like whether to take over another company or to approve the amount senior executives are paid.

Voting usually takes place at each company’s AGM, the yearly gathering of a company's interested shareholders where directors of the company present the company's financial performance and shareholders vote on issues at hand.

(the) Board

The Board members of Nest Corporation are collectively referred to as the Board of Nest Corporation, or simply the Board. They’re supported by an executive team and a range of specialists who aim to make sure Nest works in the way it should. Board members are currently chosen by the Secretary of State for Work and Pensions in line with public appointments guidance that promotes selection on the basis of merit, fairness, and openness.

Climate risk

The potential negative impacts of climate change on an organisation. It includes the potential for adverse effects on lives, livelihoods, health status, economic, social and cultural assets, services (including environmental), and infrastructure due to climate change.

Controversial weapons

The production or sale of cluster weapons, anti-personnel landmines or chemical and biological weapons.

Custodian

This is a financial institution that holds customers' investments for safekeeping. Nest’s custodian, State Street, works closely with us to allocate the right savings to the right fund, ensuring all information on what has been invested is accurate.

Default fund

A pension fund into which members are automatically enrolled.

Our default funds, the Nest Retirement Date Funds, are target-date funds where the investment objectives follow a glide path based on how far away the member is from their expected retirement date, year by year.

Diversification

The spreading of investments across different asset classes, markets, sectors, countries, etc. This is done to minimise investment risk. This is an investment application of the everyday term ‘don’t put all your eggs in one basket’.

Engagement

The process by which investors leverage their position to influence corporate decision-making. An individual or organisation with shareholder ownership has more opportunities for engagement, particularly through voting at company AGMs.

Outside of voting, investors can take a more informal approach by having a dialogue with senior management behind closed doors or making public declarations with open letters, press releases, and collaboration with other investors in industry or issue-specific working groups, like ShareAction.

Environmental, social and governance factors (ESG)

ESG factors are a set of standards used to evaluate a company’s behaviour, typically used to screen potential investments.

Environmental factors consider how a company treats the environment, such as their policies on a transition to a low carbon economy. Social factors examine how the company manages relationships with the people it works with, including employees, suppliers, customers, and the communities where it operates. Governance deals with a company's leadership, executive pay, audits, internal controls, and shareholder rights.

We believe that well-run organisations with sound environmental, social practices and good governance have a better chance of long-term success and profitability.

FCA

The Financial Conduct Authority is a financial regulatory body in the United Kingdom. It works to ensure financial markets are honest, fair and effective.

Fund manager

A third party that is responsible for implementing an investment strategy in an asset class or classes and for managing the portfolio of assets in which members' money is invested on their behalf.

Global high yield bonds

A category of bonds based on their credit rating. These bonds generally pay higher interest rates because they have lower credit ratings than investment-grade bonds. They are also known, somewhat disconcertingly, as junk bonds.

Illiquid assets

An illiquid asset is one that can't be quickly resold without a significant loss in value, for example property or infrastructure projects. Conversely, a liquid asset can be quickly sold without a significant loss in value, like stocks and shares.

Investment management agreement (IMA)

This agreement gives fund managers the authority to invest capital on behalf of investors, and detail a set of investment beliefs that are to be used to guide day-to-day investment decisions and the manager's investment strategy.

Nest's investment beliefs are set out in our **Statement of investment principles.**

Investment committee

A group that oversees the overall investment strategy and approach of an organisation as well as the investment team.

The Board delegates these powers to Nest's investment committee, whose membership includes members of the Board and independent investment specialists.

Investment return

The amount gained or lost on money invested in assets, usually expressed as a percentage. Annualised investment returns over several years help to demonstrate the longer-term performance of an investment.

Investment risk

Investment risk is the possibility of losing the money you invest. There's a risk than you might not get back what you put in or that you might not earn what you expect to.

Investment risk committee

Nest's investment risk committee meets quarterly to oversee investment risk management activities across the investment process. The committee makes decisions on risk mitigation measures or resolutions, proposals for changes to existing risk limits/targets and the risk management process.

The committee aims to support a holistic investment risk management approach. It therefore monitors investment risk management activities across the different teams within our investment risk governance structure and ensures adequate checks and balances are embedded consistently within those activities. Its remit includes reviewing key ESG issues including climate-related risks for Nest portfolios first identified by the responsible investment team, and recent developments in the responsible investment space which could have negative impacts on Nest portfolios.

Investment strategy
The guidelines that lay out future investment goals and the rules and procedures to be used when making investment decisions. Investment strategy evolves in response to changes in the economy and investors' needs. We also prioritise members' needs when evolving our investment strategy.

Leveraging

Leveraging refers to the use of borrowed funds, usually through derivative contracts, to increase the amount of money invested in the performance of an asset. It can help increase investment returns but also raises the level of risk taken by the investor, since the borrowed money will need to be repaid and there is no guarantee the underlying investment will be profitable.

Liquidity
The ability to move cash into and out of other assets. The liquidity of an asset refers to how easily and how often it can be traded or exchanged. It also means the ability to trade an asset in exchange for cash.

Minerva Analytics
Our proxy voting advisor. They help us monitor the voting intentions of our fund managers and to vote in line with our views set out in our voting and engagement policy. We take investment considerations, research and analysis, and our engagement history into account to inform our voting decisions. We have no hesitation in overriding our fund managers' votes if we disagree with their views.

Nest Ethical Fund
A pension fund for Nest members who have specific concerns about the impact that organisations have on the environment and society, for example in areas such as human rights and fair trade.

Nest Invest
Nest Invest Limited, referred to as Nest Invest, is the name of Nest's investment subsidiary, which was authorised by the FCA as an occupational pension scheme firm in January 2020. It can act on behalf of its client, Nest Corporation, to provide regulated advice, arrange deals and provide instructions to fund managers with regards to the investments in the Scheme's portfolio. The investment team at Nest Invest manages the investment of our members' money. They monitor the performance of our fund managers, consider the opportunities available in different asset classes and assess and implement our responsible investment requirements.

Occupational pension scheme
Occupational pension schemes are regulated by The Pensions Regulator. They're set up to provide retirement benefits for employees.

Pooled funds
A set of money from many individual investors that has been combined for investment purposes. The collective, or 'pooled', investment account lets the investors be treated as a single account holder, enabling them to buy more shares collectively than they could individually. They will often benefit from economies of scale, leading to better prices.

Private equity
Not all companies are listed on the stock market. These are known as privately held companies, with household names like Aldi, IKEA and Mars, the chocolate manufacturers, all falling under this banner, as well as many innovative and growing businesses.

Private equity is a way of investing in these companies, and helps them to raise money for new technology, to acquire other businesses, or just to boost their balance sheet. Privately held companies use this injection of cash to grow and develop without the quarterly scrutiny of the stock markets, which can put pressure on senior management to achieve short term results. Money is typically invested for medium to long periods of time, with private equity managers working closely alongside company management to make the business more profitable in the long-term. As they're not listed publicly, they're less easy to invest in than ordinary stocks and shares.

Responsible investment
A strategy and practice to incorporate ESG factors in investment decisions.

Securities Class Action (SCAs)
A securities class action, or securities fraud class action, is a lawsuit filed by investors who bought or sold a company's publicly traded securities within a specific period and suffered economic damage because of violations of securities laws.

Securities lending
A mature, well-regulated practice that can be a source of revenue for institutional investors. Investors temporarily lend their securities to borrowers in return for a fee. The 'lender' receives pre-agreed collateral, typically with an additional margin, in the form of other securities or cash before transferring the title of the securities to the borrower. A legal agreement protects the lender's entitlement to all the economic benefits of the lent securities (such as dividends) and, in the unlikely event of the borrower defaulting, the collateral is used to fund the replacement of the securities borrowed.

Segregated mandate
A fund run exclusively for a client, as opposed to a pooled fund.

Statement of investment principles (SIP)
Nest's policies and principles that guide all decisions when managing members' money.

Stewardship
This is the responsible allocation, management and oversight of assets to create long-term value, which also helps bring about sustainable benefits for the economy, the environment and society. Asset owners, like Nest, can sign up to The UK Stewardship Code which sets a certain expectation on how organisations will look after money invested on behalf of their members.

Task Force on Climate-related Financial Disclosures (TCFD)
An organisation that provides a framework on the types of information that companies should disclose to support investors and other stakeholders to allow them to appropriately assess climate risks.

Target-date funds (TDFs)
An age-based fund, where the members invested in each fund are expected to retire in the same year. This approach allows investors to effectively implement an investment strategy that matches the different life stages members go through.

Trustee
A person, group of people or a company that acts in a specific interest. Nest Corporation is a Trustee of the Nest Scheme and acts in a sole interest of the Scheme's members.

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