



Looking after members' money

— Nest's investment
approach



About this guide

This booklet is intended to help you understand what happens to members' money. It's one of a series of documents that describe our investment process.

- Our Statement of investment principles outlines the policies and principles that guide our decisions when we're managing our members' money.
- Our fund factsheets and Annual report and accounts give more information about how well we've delivered against our investment goals.

This investment approach booklet fills in the details. It provides the information you need to understand how our funds are managed, our goals and objectives and the research that led us to set up our investment approach the way we did.



Contents

Introduction	4
Our investment approach	5
Our ambition for our members	7
Our funds in depth	9
How we invest members' money	14
Managing money day to day	16
Information	16
Decisions	17
Action	18
What next?	22



Introduction

When we're looking after our members' money we have one goal – we want to give them a better income in retirement.

When creating Nest we had the opportunity to build an investment approach from the ground up. We had free rein to create a savings product that focused on what was best for the majority of workers rather than a traditional market of higher earners.

We began with a significant amount of research into our likely membership. We then studied the way other countries had put together mass pensions saving schemes.

We used what we found out as a guide to how we could grow our members' money while addressing their desire to keep it safe. Nest's in-house team took existing and well-understood ways of managing money and combined them in a different way to create a new approach to long-term saving for workers in the UK.

We wanted to build a pensions savings vehicle that's easy for members to use and understand but at the same time gives them access to the latest technology and thinking on portfolio management.

Explaining how we do that is what this booklet is all about.

What is Nest?

Nest is a national workplace pension scheme that any employer can use to meet their new workplace duties. It's the only automatic enrolment scheme in the UK with an obligation to take any employer regardless of the size or value of their business.

Nest is run in the interests of its members by Nest Corporation, which has been appointed as Trustee of Nest. Nest Corporation doesn't have shareholders and doesn't distribute a profit.

It's been designed to be easy to manage online for both employers and members. Our research programme has covered investment, communications and usability with findings in each area directly reflected in the product's features.



Our investment approach

We've created an investment product for all investors. The straightforward experience for the member is built on a sophisticated approach to risk management and asset allocation.

What members see...

- Straightforward enrolment experience.
- Nest Retirement Date Funds offering a tailored approach for every member.
- Clearly labelled fund choices that address the needs of a diverse workforce.
- Clear communications without overwhelming them with information.
- Same low charge across all funds.

What's happening out of sight...

- Multi-phase investment approach that targets different risk and return objectives.
- Dynamic risk management designed to succeed in different economic conditions.
- Delivery system that provides flexibility and efficiency.
- High levels of governance and clear alignment of long-term interests between investment managers and members.

We want to make it easy for our members to save. In fact, one of the best things a saver with Nest can do after they're enrolled is nothing. Doing nothing at this stage means staying enrolled, making contributions and gaining all the advantages of the Nest Retirement Date Fund investment approach.

This is what makes Nest different. We've kept things simple and our charges low without sacrificing any of the high-quality management that the most demanding investors expect.

Nest Retirement Date Funds

We've focused our efforts on creating a robust default option that's right for most people. Our research suggests that a significant majority of the people who'll start saving through automatic enrolment don't want to make decisions about what happens with their money. They just want to know it's being well looked after and will be waiting for them when they're ready to retire.

We've created our default option – the Nest Retirement Date Funds – for them.

At any time there are up to 50 Nest Retirement Date Funds. Each fund aims to have members' money ready to convert into retirement benefits in the year they want to take their money out.

If the member wants to take their money out in 2040 their retirement pot will be held in the Nest 2040 Retirement Fund. If they decide they want to save for longer or take their money out earlier they can change their preferred retirement date at any time. Their retirement pot will be automatically switched to the Nest Retirement Date Fund that matches their new retirement date free of charge.

Our other fund choices

We know that some members have faith or beliefs that mean some types of investment aren't right for them. We also know that some of our members associate putting their money into the stock markets with a high chance of losing it. Others have the opposite view and have an appetite to take more risk than the Nest Retirement Date Funds typically take.

Without suitable options these people may well opt out of automatic enrolment and have no savings for their future.

To make sure that these savers can take part in Nest we've created a range of clearly labelled fund choices. They offer members genuine alternative approaches at the same low charge as our Nest Retirement Date Funds.

Nest Ethical Fund

This fund is designed for members who are concerned about the impact that their investments can have on areas such as human rights, fair labour practices and the environment. Unlike many other ethical funds available, our Nest Ethical Fund choice uses a three-phase investment approach similar to the Nest Retirement Date Funds.

Nest Sharia Fund

This fund is designed for members who want an investment approach based on Islamic law. It invests entirely in global equities judged to meet sharia standards. Because it invests in just one type of asset it carries a higher level of investment risk than our other fund choices.

Nest Higher Risk Fund

This fund is for members who want to take more investment risk to try and make their retirement pot grow more quickly than in a Nest Retirement Date Fund. As members approach their retirement date we'll move their pot into the appropriate Nest Retirement Date Fund. This will help protect any gains they've made and get their retirement pot ready for them to take out of Nest.

Nest Lower Growth Fund

This fund is designed for members who are very cautious about investing. Their retirement pot will be exposed to far less investment risk than a Nest Retirement Date Fund. In the long term however, it will probably grow less than other fund choices and may not keep pace with inflation.

Nest Guided Retirement Fund

This fund is an option for members who are aged between 60 and 70, who have at least £10,000 in their retirement pot, and want to start taking their money out of Nest. Nest members who are in the default strategy (Nest Retirement Date Funds) at their intended retirement date, and who meet the criteria will be automatically moved in this fund.



Our ambition for our members

Nest has been established to help its members save for retirement. We want them to understand how they can improve their future lives and we want to make it easy for them to do so.

Investment has a central role to play in this. By investing internationally and across asset classes we tap into global growth where and when it's available. In this way we can give our members a share in the long-term value they bring to the UK economy and in economic growth around the world.

Understanding what our members want and need

Before we could create a good product for our members we needed to better understand their needs and desires. We conducted a significant amount of research into the likely profile of savers who'll be brought in by automatic enrolment.

We wanted to know what kind of investment will feel right to them. What will feel fair to our members? What are their expectations? What will make them feel that this isn't an obligation but an opportunity to improve their lives?

Our research shows that while they expect to see growth in their savings they're uncomfortable with the idea of extreme volatility and concerned about things like stock market crashes. Many people told us that they would prefer a bit more smoothness in the journey and outcomes that are reasonably predictable. They were less keen on chasing bigger but less likely returns.

We created our Nest Retirement Date Funds for them.

Did you know?



We conduct ongoing research to understand our members and keep our investment strategy up to date. You can find this on our website at nestpensions.org.uk



Nest Retirement Date Fund

What members want

- Growth
- Smooth ride
- Investment decisions made for them

What members need

- Diversified portfolio
- Growth-seeking assets
- Nest lifecycle

Why is managed risk important?

It's impossible to achieve significant returns, such as returns above the risk-free rate, without taking some risk. But risk needs to be taken in a calculated and managed way. Only by doing this can we consistently deliver on our investment objectives.

The goal of our risk management process is to make sure that the risk we take is properly rewarded. We look at the potential return offered by different asset allocations and assess them in relation to the risks they carry. We don't chase the highest returns for our members and we don't aim to expose them to the least risk. We look for the investments that offer the best returns in relation to the level of risk.

We constantly monitor where risk in our funds comes from, how big it is and whether or not it's positively rewarded. We aim to take risks that will be favourably rewarded and minimise exposure to unrewarded risks while delivering the risk/return profile as smoothly as possible.

Why inflation?

Our investment objectives are based on delivering above-inflation growth. We're not interested in delivering market-relative performance. Our members need to grow their money in real terms to build a retirement pot. We want to make sure that our members don't lose out to either the rising cost of living or sudden investment shocks and that they get back the charges they pay through investment growth. It's what our members expect and so we've put it at the heart of what we do.

Communication

Talking to members

We know from our research into people's attitudes to savings and pensions that many are concerned about how safe their money will be in a defined contribution pension scheme. We also know that a lot of people across all levels of education and achievement don't understand what investment is or how it works.

This can stop them from making decisions about their pension out of fear of doing something wrong. But we want our members to have confidence in saving for their retirement. They have a right to know what's happening to their money and many of them want to know.

If members can understand how we look after their money and their likely outcomes, they'll be empowered to make informed decisions about their future. This might include making additional contributions or working for longer to get a better income in retirement.

Our ongoing programme of communications research is focused on finding out how we can bring investment issues alive for our members. We want to connect them with their money. In response to this we've developed new ways to talk about investment using plain language and real-world examples.

For example, we've named our funds to help our members understand their options. We don't have a 'higher growth fund', we have the Nest Higher Risk Fund. This makes savers aware that this fund faces higher volatility than our Nest Retirement Date Funds.

We're continually fine-tuning our communications in response to what our members tell us and developing innovative new ways to help them understand the opportunities that pension saving offers.

Talking to employers and advisers

We also provide information with a more technical focus for those who want more detail. We produce quarterly factsheets aimed at advisers for each of our Nest fund choices and representative Nest Retirement Date Funds. These provide detailed information about asset allocation, risk characteristics and fund performance that outlines how we're going about meeting our objectives.

We also produce documents such as this one to explain our investment strategy and to provide the bigger picture of how our funds work. These include our Statement of investment principles, which are available from our website at nestpensions.org.uk

Our funds in depth

Nest Retirement Date Funds

Each Nest Retirement Date Fund pools the retirement pots of all the members who plan to take their money out of Nest in the same year. So the retirement pots of all our members who plan to take their money out in 2040 are invested in the Nest 2040 Retirement Date Fund. This allows us to efficiently address the common interests of large numbers of savers while still providing a tailored approach for individuals.

We're able to adjust the portfolio of each fund to match our members' place in the saving lifecycle and take account of changing economic and market conditions along the way. This gives our savers a much smoother ride than funds based on a single asset class – such as shares – or those that rely on a mechanical approach that adjusts allocations automatically according to a fixed schedule.

The youngest members who put their money in our Nest Retirement Date Funds will go through three phases. Each phase has a different objective that focuses on the needs of the member at specific times in their savings career.

We have a glide path that sets out the levels of investment risk we expect to take at each stage of the lifecycle. These are designed to balance the member's need to keep their money growing to at least outperform inflation with their desire to avoid the unpredictable returns that they've told us they find alarming.

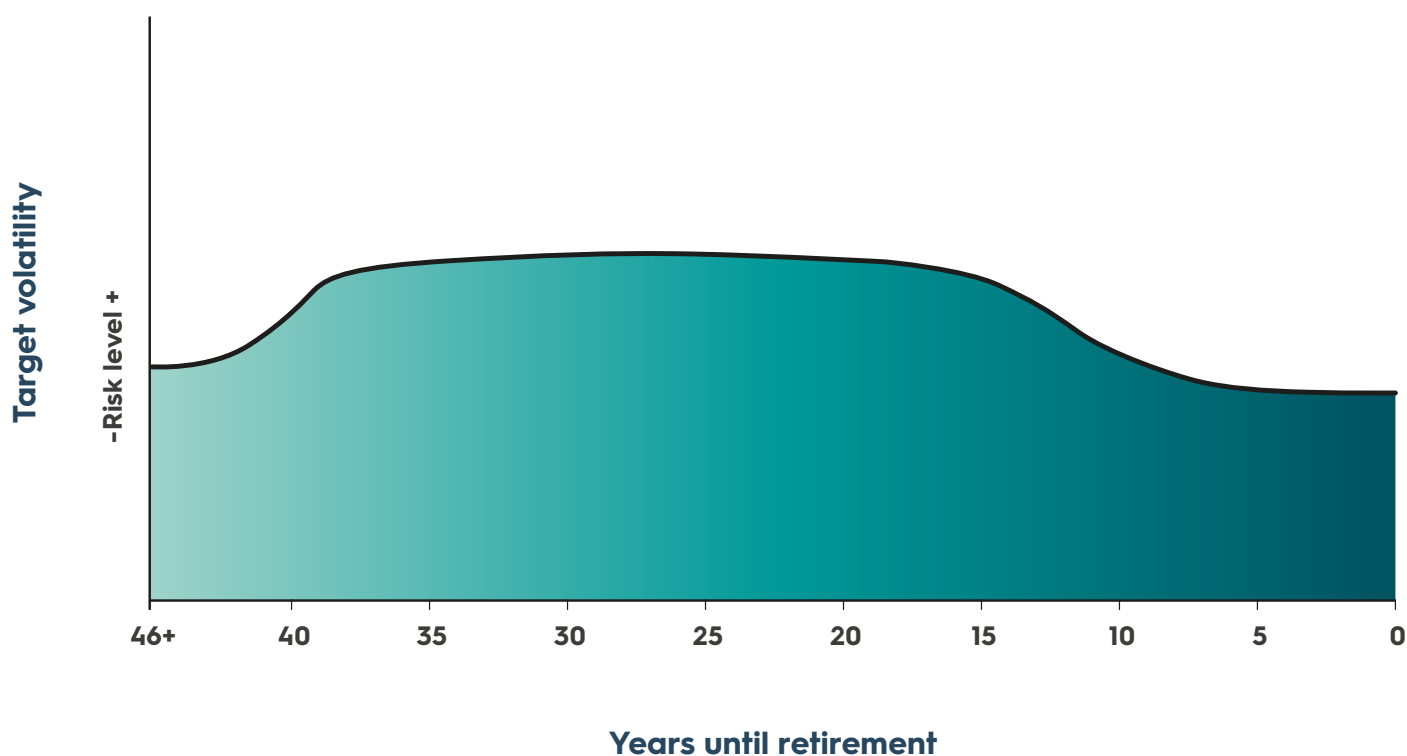
The glide path is defined by the reference portfolio set for each of the phases. The way Nest Retirement Date Funds are structured allows us to vary the amount and type of risk taken according to economic and market conditions.

Moving between phases

Our lifecycle isn't a rigid 'set and forget' regime. We dynamically manage the transition between phases to take account of our view of the financial markets, the economic environment and our latest understanding of our members. This helps us judge the best time to begin reducing or increasing the investment risk.

In this way we can take advantage of the good times on our members' behalf while helping protect them from the bad times.





Foundation phase objectives

- Keep pace with inflation while preserving capital.
- Expect a long-term volatility average of 7 per cent.
- Significantly reduce the likelihood of extreme investment shocks.
- Take appropriate risk at appropriate times, taking account of current economic and market conditions.

Growth phase objectives

- Target investment returns greater than inflation plus 3 per cent and cover all scheme charges.
- Expect a long-term volatility average of 10-12 per cent.
- Maximise diversification.
- Aim for steady growth in real terms over the life of the fund.
- Maximise retirement incomes by taking sufficient investment risk at appropriate times while reducing the likelihood of extreme investment shocks.

Consolidation phase objectives

- Gradually move the portfolio from the return-seeking assets held in the Growth phase to annuity-tracking assets and cash-like investments.
- Gradually reduce volatility and manage the tracking error to annuity prices.
- Continue to grow the portfolio in real terms where this doesn't clash with the above goals.
- Further reduce the likelihood of investment shocks.

The Growth phase is the engine room of the Nest Retirement Date Funds approach where we concentrate on growing the pot quickly. Members could spend up to 30 years in this phase. We've set ourselves a benchmark of 3 per cent above inflation after all charges over an economic cycle so that we – and our members – can judge if we're delivering the growth our members need and expect. In practice, though, we'll try and outperform our objectives in the good times.

The Foundation phase is focused on getting savers into the savings habit. During our research younger savers told us that they may stop saving if they see falls in the value of their retirement pot. This is true even for a very short-term or one-off loss. For this reason members who join in their 20s will typically spend one to five years in the Foundation phase. In this phase we want to encourage members to keep saving by making sure they see a steady increase in their retirement pot as they make contributions. We still aim to beat inflation to protect the real value of their retirement pot but we don't expose them to the risks associated with chasing higher growth. We're prepared to give up a very small amount of potential growth in this phase. Mathematical modelling shows that the impact on final outcomes is negligible for most members, but the impact of stopping saving could be much more harmful.

The Consolidation phase is when we move to lock in any gains that members have made and mitigate the risks that come from converting investment assets into a retirement income and cash. Starting around 10 years before retirement we gradually move member pots into assets that broadly reflect the way we expect them to take their money out of Nest. In the early years of the scheme we expect that most members who enrolled late in their careers will take their relatively small pots as cash. In the long-term though, our members are likely to want to keep benefiting from investment growth while gradually taking money out of their pots to fund their retirement.

We still expect to grow members' money by more than inflation, but in this phase our primary focus is to secure the member's retirement income.

Our other funds

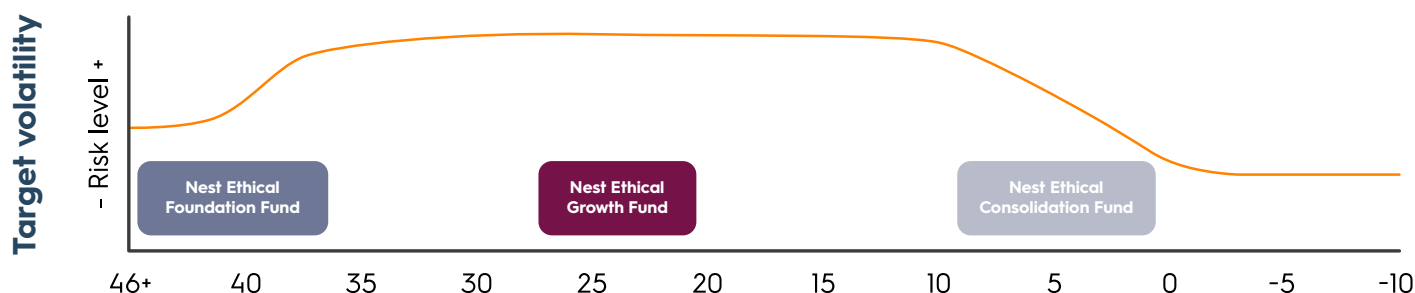
Nest Ethical Fund

- Provide a fund choice for members who want to invest in a portfolio that reflects their ethical investment concerns.
- Aim for steady growth in real terms over a member's time with Nest.
- Maximise incomes in retirement by taking sufficient investment risk at appropriate times while reducing the likelihood of investment shocks.

We know from our research that many savers are suspicious of financial services and the financial services industry. Their concerns are not just over the safety of their money – many also worry about the types of business that their money is supporting.

These members may opt out if they can't be sure that their money isn't being used by companies involved in products or with policies they feel are unethical. People who were interested in ethical investment told us during our research that their main concerns are global issues such as child labour, exploitation and human rights violations.

We believe that members shouldn't be penalised for their views. Our Nest Ethical Fund choice has the same low charges as the default. It offers members a diversified portfolio which includes ethical equities, real estate and UK government bonds. As with the Nest Retirement Date Funds we manage the allocation between these asset types to protect members' retirement pots and take advantage of market growth.



In addition, the Nest Ethical Fund choice follows a similar life cycle to Nest Retirement Date Funds using separate Foundation, Growth and Consolidation funds. This is one of the few ethical pension funds available in the UK that uses a phased investment approach in this way.

At the moment we transition members between these phases using a formula based on their Nest retirement date. However, as our membership expands we'll look at ways we could dynamically manage transitions as we do for the Nest Retirement Date Funds.

Nest Sharia Fund

- Provide a fund with an investment approach based on Islamic law.
- Expect a long-term volatility expectation of 22 per cent.
- Grow a member's pot in real terms over the course of their savings career.

Our member and employer research showed there was sufficient interest in investment that's compatible with Islamic law that some savers would opt out if the option wasn't provided. Although we expect take-up to be limited it's important for us to be able to offer funds for as wide a cross-section of the workforce as possible.

The Nest Sharia Fund invests entirely in the HSBC Life Amanah Pension Fund, which tracks the Dow Jones Islamic Titans 100 index. This index is made up of shares in the 100 largest global companies that have been judged compliant with sharia principles by an independent board of Islamic scholars.

This fund's performance can be volatile because it's invested entirely in equities. Similarly, we're currently unable to change the asset mix over a member's career as we do with Nest Retirement Date Funds as other asset types don't necessarily meet sharia standards.

We'd like to reduce the volatility of this fund and give members a smoother approach. We're looking into ways we can do this efficiently using additional sharia-compliant asset classes.

Nest Lower Growth Fund

- Preserve the nominal value of contributions and grow the fund in line with low-risk money market investments.
- Achieve an investment return that's in line with or better than wholesale money market short-term interest rates before charges.
- We expect a long-term volatility average of 0.5 per cent.
- Provide a fund for members who want to take as little investment risk as possible.

Our research revealed that some of the savers who'll be automatically enrolled in schemes like Nest are very unwilling to trust their money to the financial markets. When given no choice about what happens with their money these savers are very likely to opt out rather than put their money into investments they consider unsafe. This fund has been designed for these members.

Members who choose this fund are very unlikely to see a fall in the nominal value of their fund. However, there's a good chance that at times their retirement pot won't grow as quickly as the cost of living. Remaining in this fund for very long periods may well not be appropriate but it protects savers against an even bigger risk – not saving at all.

Nest Higher Risk Fund

This fund is for members who want to take more investment risk to try and make their retirement pot grow more quickly than in a Nest Retirement Date Fund. When a member chooses to switch into the Higher Risk Fund, they'll have an option to choose which higher risk strategy they'd like to be invested in. The first strategy moves a member's pot out of the higher risk fund into a Nest Retirement Date Fund ten years before their nominated retirement date. This will help protect any gains they've made and get their retirement pot ready for them to take out of Nest. Their pot may though not benefit from the same gains as if they'd left it in the Higher Risk Fund. The second strategy keeps a member's pot in the Higher Risk Fund regardless of their age unless and until they choose to move their money to an alternative fund choice, or transfer or withdraw their funds.

Nest Guided Retirement Fund

This fund is an option for members who are aged between 60 and 70, who have at least £10,000 in their retirement pot, and want to start taking their money out of Nest. Nest members who are in the default strategy (Nest Retirement Date Funds) at their intended retirement date, and who meet the criteria will be automatically moved in this fund.

Nest manages and invests members' pots with the aim of providing them with sustainable withdrawals until age 85. The remaining pot can then be used to purchase a lifetime income from age 85, if the member wishes.

The fund is designed so members can start accessing their retirement savings while continuing to benefit from potential investment returns. Members can also continue to contribute to their pot, but they may be liable to an additional tax charge if contributions exceed £4,000 per year.

Nest does this by splitting the members' pot into parts, each designed and invested differently to meet the different needs of our members throughout their retirement.



How we invest members' money

For much of our portfolio, Nest uses members' money to buy units in pooled funds provided by global fund management companies. Each of these funds has a clear investment objective and generally invests in a single asset class.

We diversify our members' money across different types of investment by buying units in each of these funds in varying proportions. These proportions depend on the Nest Retirement Date Fund or the other fund choices our members have selected.

Using third-party pooled funds in this way helps us manage our members' money efficiently. We're able to give them exposure to a variety of global markets in a way that meets their needs while keeping our charges low.

Fund managers

We continue to evolve our investment strategy and add more fund managers over time where appropriate.

Investment fund manager	Asset class	Investment approach
Allspring previously known as Wells Fargo	Public investment-grade bonds	Active
Amundi	Emerging market debt Private credit	Active Active
BlackRock	Money market securities Private credit Public investment-grade bonds	Active Active Active
BMO	Developed market equities Public investment-grade bonds	Active Active
BNP	Private credit	Active
CBRE Caledon	Infrastructure equity	Active
CoreCommodity	Commodities	Active
GLIL Infrastructure	Infrastructure equity	Active
HSBC	Sharia-compliant developed market equities	Passive
J.P. Morgan	Global high-yield credit	Active
LGIM	Gilts Listed property Direct property	Passive Passive Active
Local Pensions Partnership	Infrastructure equity	Active
Northern Trust	Emerging market equities	Passive
Octopus Investments	Infrastructure equity	Active
Royal London	Public investment-grade bonds	Active
State Street Global Advisors	Gilts	Passive
UBS	Climate-aware developed market equities	Systematic

As at September 2021

Responsible investment and corporate governance

Responsible investment is focused on the ways that returns for investors can be affected by the environmental and social impact of a company, or the way it's governed. These are often abbreviated to 'ESG factors'.

We think that companies with well thought out environmental and social policies and good corporate governance do better in the long run than companies that neglect these issues. It's in the interests of our members for us to consider how companies behave and how it affects members' outcomes in the long term.

Our main goal is to manage the risks that ESG factors can bring to investment. Secondary to this is a desire to improve the way markets operate and encourage sustainable performance from the companies we invest in on behalf of members. Finally, we also need to make sure that Nest is seen to be a responsible investor so that the public – be they members, employers or stakeholders in Nest – can have confidence in the scheme.

Our responsible investment objectives

- Improve the environmental, social and governance performance of our portfolios if we think that it will reduce the amount of downside risk that comes with upside performance.
- Work individually and collaboratively with other investors to improve the way that the markets we invest in operate and are regulated.
- Encourage the companies we invest in on our members' behalf to deliver sustainable and stable performance through longer-term performance horizons rather than a short-term focus.
- Reduce the possibility of reputational damage affecting the value of a company we hold and having any knock-on effect on the reputation of Nest.

Promoting the benefits of responsible investment

We've signed up to several initiatives that promote the benefits of responsible investment.

Nest is a signatory to the United Nations-backed Principles for Responsible Investment (PRI). The PRI are a set of principles that aim to build a framework for global best practice in responsible investment.

We're also signatories to the UK Stewardship Code which includes 12 principles that promote the management and oversight of capital to create long-term value for clients and beneficiaries, leading to sustainable benefits for the economy, environment and society. As part of Nest's commitment to the code we set out how we adhere to the 12 principles in our annual responsible investment report.

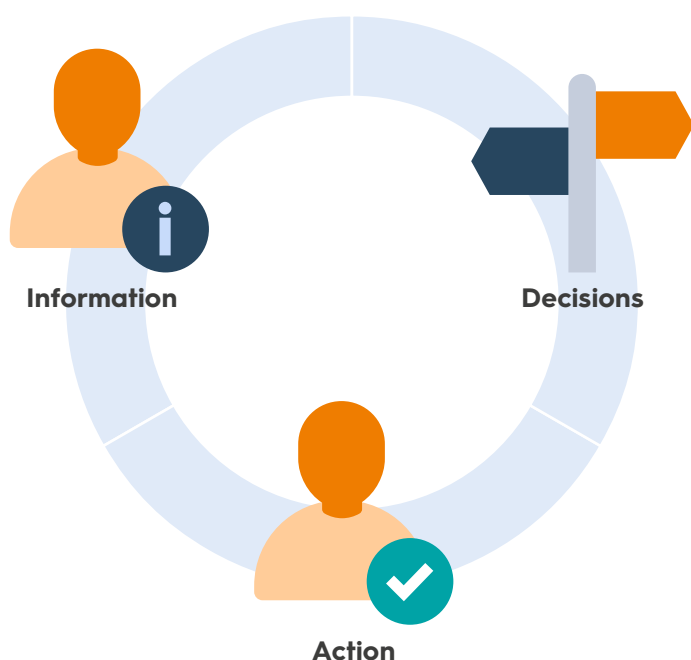
We regularly engage with the Financial Reporting Council (FRC) on issues of UK Corporate Governance and stewardship and are members of the climate and workforce reporting working group.



Managing money day to day

We've put in place a robust, repeatable process to make sure that our members' money is managed responsibly. It combines in-house expertise with leading data providers and fund managers and is subject to checks, balances and monitoring to ensure that sound decisions are made on good information and that these decisions are implemented efficiently.

This process is best understood in three main phases.



Information

At the heart of our process is a comprehensive understanding of what's happening in the economy and the markets. We use this to make appropriate decisions on risk for our members based on how long they have until retirement.

We have two key objectives in mind when managing members' risk.

- **Achieving our growth objective**
Our risk management framework helps us to take the right amount of risk required at any given time to achieve our return objectives.
- **Avoiding extreme losses for our members**
Understanding what's happening to different types of investment in different economic or market regimes helps us reduce exposure to them in periods of crisis and to understand when these assets are undervalued and should be bought.

Decisions

As a trust we have a responsibility to manage money in our members' best interests. All the decisions we make are intended to provide our members with a good return.



In-house investment

The investment function, Nest Invest, manages our members' money from day to day. Nest Invest is regulated by the FCA and authorised to provide advice to the Nest Trustee on investment decisions. They monitor the performance of our fund managers, consider the opportunities available in different asset classes and assess our responsible investment requirements.

We hold an asset allocation meeting every quarter where the investment team reviews all of the information and makes recommendations. This gives us broad weightings for the main asset types we invest in – such as equities and other growth assets, emerging market debt, corporate and other bonds, property, cash and gilts.

The investment committee

All investment decisions are overseen by the Trustee through the investment committee, a group of Trustee Members that meets quarterly to formally review investment operations and decisions. They decide on the recommendations of Nest Invest on:

- investment objectives
- strategic asset allocations
- the parameters of dynamic risk management
- approach to active ownership
- evolution of fund choices
- fund manager selection and monitoring
- investment communications for members and employers
- investment costs.

This committee also monitors fund performance and operation to make sure that the Trustee is fulfilling its legal duties.

Members' Panel and Employers' Panel

The Trustee also gets the views of members and employers using Nest through the Members' Panel and Employers' Panel. These two groups provide member and employer perspectives on investment to the Trustee and have a statutory role in reviewing the Statement of investment principles.

These checks and balances provide Nest with a high level of oversight in its investment operations.

Action

Member

1



Contributions come from employers and members

7



Member's retirement pot held as units in their Nest retirement fund

Tata Consultancy Services (TCS)

2



TCS collects contributions

6



TCS receives unit prices to value retirement pots

Nest/State Street Bank

3

State Street buys units in underlying funds based on Nest's asset allocation decisions

Nest asset allocation



Growth-seeking assets



Income-seeking assets

5



Nest Retirement Date Funds



Other fund choices



State Street Bank calculates AMC and Nest retirement date fund unit prices

Underlying fund managers

4



Amundi
BlackRock
BMO
BNP

CBRE Caledon
CoreCommodity
GLIL
Infrastructure

HSBC
J.P. Morgan
LGIM
Local Pensions Partnership

Northern Trust
Octopus Investments
Royal London

State Street
Global Advisors
UBS

Allspring
previously known as
Wells Fargo

Making the decisions happen

Just as important as getting the right information and making the right decisions is enacting those decisions quickly and efficiently. We're helped in this regard by our scheme administrator Tata Consultancy Services and fund administrator State Street Bank.

Tata Consultancy Services collects contributions for all our members. They pass consolidated trade data on to State Street Bank to invest in Nest funds on behalf of our members.

Our investment operations team is responsible for advising State Street Bank of the changes to the asset allocation and making sure that the changes have been made as directed in a timely way.

Nest Retirement Date Funds structure

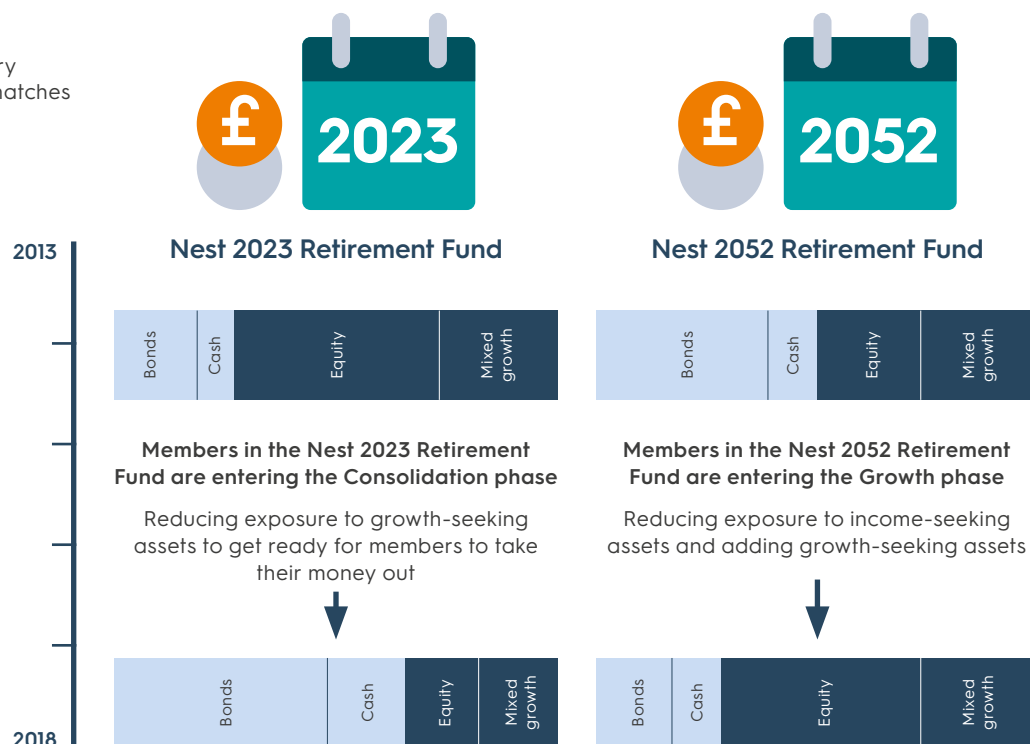
We've structured our default Nest Retirement Date Funds in a way that allows us to minimise our trading costs. They're made up of synthetic sub-funds we call 'tier 2 funds'. Each of these tier 2 funds is a mix of assets designed to focus on growth, income, annuity matching or cash. Tier 2 funds are made up of units in our underlying building block funds provided by our fund managers.



The internal marketplace

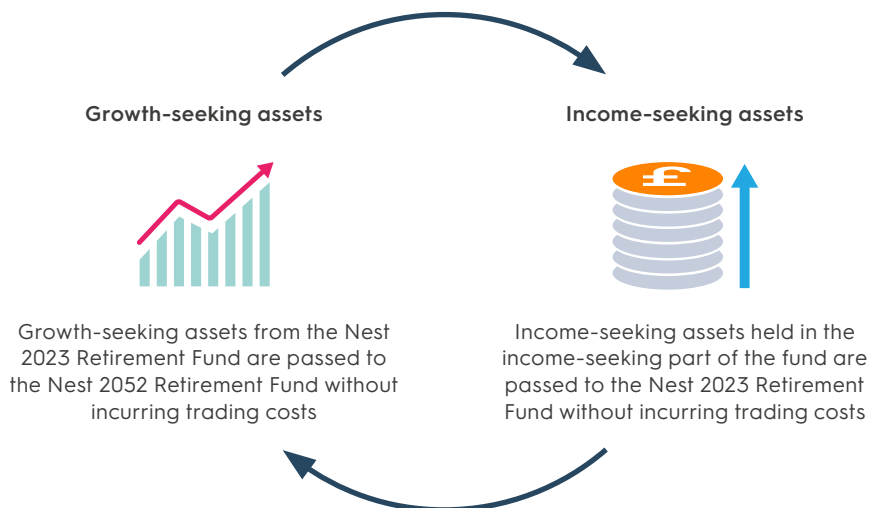
Nest Retirement Date Funds

Our default fund structure gives every member an investment profile that matches their planned retirement date.



The internal market

By creating an internal market between Nest Retirement Date Funds we reduce the drag on performance caused by transactional costs like stamp duty and brokerage fees.



The internal market

The internal market also keeps costs down for members leaving the scheme and those just joining. New member contributions can be used to balance allocations and for payment of cash lump sums for members taking their money out.

Active ownership

It's important to us to make sure that the companies in which we hold shares on our members' behalf are well-run.

The voting rights that come with ordinary shares are an important tool for our responsible ownership objectives. Through voting we can engage with companies and influence how they're run. This helps us make sure they're acting in the best interests of our members who are the ultimate owners of the shares.

Our voting rights are currently exercised on our behalf by our fund managers. We've asked them to make their voting records available to our members. We'll let them know if we have particular concerns about a company or if we believe they're voting in a way that's not in our members' interests.

As a large investor we'll be able to make sure the companies held in our funds understand the importance we place on environmental, social and governance factors.

The risks associated with environmental, social and governance factors may not be front of mind for directors. Our influence as active investors can help make sure that the companies held in our funds understand the importance we place on them. We'll also work with other investors to engage with companies on issues where we have a shared interest. Coordinating our efforts in this way makes it more likely that we can positively influence the companies we invest in.

We expect our fund managers to keep us informed about contact they have with the companies they invest in on our members' behalf and their efforts to promote high standards.

Our fund managers exercise the voting rights with regards to the shares Nest owns on behalf of our members. Our fund managers vote in line with their respective voting policies, but we also have a voting and engagement policy of our own. Of course, there will be times when we think our fund managers could do more, or where we recognise that their views aren't necessarily aligned with ours and our members' needs. We work closely with our fund managers and offer constructive challenge if our views differ.

Keeping track

The investment operations team monitors the activity of our suppliers to make sure they're providing the level of service we expect. Every day they check that the asset allocations implemented by State Street Bank match our strategy and make sure that unit prices and member accounts are correctly valued. We also monitor the activity of our underlying fund managers to check that they continue to provide the right mix of assets and a high level of service.

We recognise, however, that pricing errors can happen so we have a process to assess and correct them quickly. All pricing errors of more than 10 basis points are recorded, reviewed and reported to our investment reporting and compliance committee. As well as correcting the error they investigate how it happened to make sure there are no problems with our systems or processes.

We'll pay members compensation where the pricing error has affected the value of their retirement pot by more than 50 basis points, subject to a minimum loss in terms of monetary amounts. We'll also correct any over-valuations of units so that all our members are treated fairly and in line with industry best practice.

Did you know?



You can find out more about our voting policies on our website at nestpensions.org.uk/investmentapproach

What next?

As Nest grows we'll have many more members making contributions and the amount of money we manage will increase dramatically. This will give us the opportunity to explore other ways of helping our members. Some possible areas of further development include:

- Exposure to new asset classes – when we have a larger pool of members we'll be able to expand the range of building block funds we use.
- Bringing some outsourced functions in-house – as our member funds under management increase we'll be able to provide some of the services we currently outsource.



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