Scottish Milk Limited Retirement Benefits Plan

Statement of Investment Principles

1. Background

This Statement sets down the principles governing decisions about investments for the Scottish Milk Limited Retirement Benefits Plan (the "Plan") to meet the requirements of the Pensions Act 1995 as amended by the Pensions Act 2004, the Occupational Pension Schemes (Investment) Regulations 2005 and subsequent Regulations. Before preparing it we have consulted First Milk Limited (the "Company") and obtained and considered written professional advice from our investment consultant. We will review this Statement every three years.

Our investment responsibilities are governed by the Plan's trust deed: a copy of the relevant clause, of which this Statement takes full regard, is available on request.

2. Investment Policy

Our main aims are:

- To make sure that we can meet our obligations to the beneficiaries of the Plan;

- To pay due regard to the Company's interests on the size and incidence of employers' contribution payments.

In order to ensure that an appropriate investment strategy is in place, an analysis of the assets and liabilities of the Plan was undertaken during 2014 and a subsequent review to further de-risk in 2016. The investment allocation was further reviewed in 2019. The following investment objectives were agreed as part of these reviews:

- To minimise the risk (or volatility) of the portfolio relative to the liabilities as far as practical.
- To restructure the bond portfolio so that it better reflects the characteristics of the Plan's liabilities by hedging against interest rate and inflation movements to help minimise the risk of an increase in the required deficit reduction contributions (above RPI) in the future.
- To ensure that the investment portfolio is consistent with the long term assumptions used in determining the funding requirements of the Plan.

As a result, the growth portfolio represents 5% of total Plan assets and the remaining assets are invested to fully hedge the interest rate and inflation sensitivities of the liabilities on a Technical Provisions basis, after making an allowance for the sensitivities of the agreed shortfall-correction contributions. As at 2022, this corresponded to an interest rate hedging ratio of 98% and an inflation hedging ratio of 94% of the liabilities on a Technical Provisions basis, before adjusting for the shortfall-correction contributions. The Trustees believe that the resulting asset mix is currently appropriate in meeting the aims and objectives described above.

3. Day to Day Management of the Assets

The Trustees invest the main assets of the Plan in pooled fund arrangements with BlackRock Investment Management ("BlackRock").

The overall Plan's target allocation is detailed below:

Asset Class	Benchmark %	Index
World Equity	5.0	FTSE All World Developed
TOTAL GROWTH	**5.0**	
Liability Driven Investment ("LDI")	71.0	Liability Cashflows
Corporate Bonds	24.0	iBoxx Sterling Non-Gilts Index
TOTAL MATCHING	**95.0**	
TOTAL	**100**	

Details of the range of funds used by the manager plus the fees are included in the Appendix.

The Investment Manager is regulated by the Financial Conduct Authority (FCA). As required by the Financial Services Act, we have entered into a signed Agreement with them. The Agreement provides important protections for the Plan itself, and for the Trustees. It also sets out the terms on which the assets are managed; the investment brief; guidelines and restrictions under which the Investment Manager operates.

The Trustees also operate a bank account and invest additional voluntary contributions on behalf of members in separate insurance policies.

4. The Trustees' Risk Management Methodology

The Trustees' investment policy is derived from a formal analysis of the Plan's assets and liabilities. The analysis enables the Trustees to evaluate the available investments for the Plan and implement the most appropriate strategy which balances the need to meet the investment objectives and the risks taken by the Plan.

On consideration of the results of this analysis, and based on advice from their investment consultants, the Trustees determined a target mix of asset types, which the investment manager may operate and these are set out in Section 3.

The revised investment strategy in place has reduced significantly the equity risk within the Scheme as well as significantly reducing the interest rate and inflation mismatch by investing in bond (and bond like) assets with similar characteristics to the liabilities. The Trustees appreciate that there does remain an element of risk but believe that the asset allocation policy in place manages risk as far as practical. There are other risks such as:

- The liability benchmark used to assess the assets against is an approximate picture of the liabilities of the Plan (due to the assumptions required to model the liabilities) and the pooled funds used to hedge the liabilities are an approximate match to the liability benchmark. However, the Trustees believe that the funds used provide an efficient way of hedging the Plan's liabilities.

- There are also operational risks involved in the use of leveraged pooled funds, including counterparty credit risk and leverage management. BlackRock, the Plan's investment manager, monitor and manage these risks on behalf of the Trustees.

The agreement with the investment manager includes a number of guidelines which, among other things, are designed to ensure that only suitable investments are held by the Plan.

The terms of the agreement do not allow the investment manager to do anything that could be considered to be speculative or "trading" by the Financial Conduct and Tax Authorities.

5. Buying and Selling Investments

We have delegated the responsibility for buying and selling the underlying investments to the investment manager. As already mentioned, the day-to-day activities which the investment manager carries out for us are governed by the agreement between us, which is reviewed from time to time to ensure that the operating instructions, guidelines and restrictions remain appropriate.

6. Rebalancing and Cashflow Policy

The Trustees will monitor the asset split between the growth and matching assets as set out in section 3 on a six monthly basis with input from Mercer.

Mercer will assess the level of cashflow expected over the next six months to pay forthcoming known benefits and expenditure. The funds required will be sourced where possible from income payments from the pooled funds that provide that facility. Any excess monies required will be sourced in order to bring the growth and matching split closer to the target allocation. In addition, the LDI portfolio may also be realigned if it has drifted materially from its target interest rate and inflation hedging ratios.

However, if the actual asset allocation has drifted materially from its target allocation and the cashflow requirements are not believed to rectify the situation, then the Trustees may issue instructions to the manager to rebalance the assets. In doing so consideration will be given to the costs of the rebalancing exercise

7. Environmental, Social and Governance Issues

ESG, Governance and Climate Change

The Trustees believe that good stewardship and environmental, social and governance ("ESG") issues may have a material impact on investment returns, and that good stewardship can create and preserve value for companies and markets as a whole. The Trustees also recognise that long-term sustainability issues, particularly climate change, present risks and opportunities that increasingly may require explicit consideration.

The Trustees have given the appointed investment manager full discretion in evaluating ESG factors, including climate change consideration, and exercising voting rights and stewardship obligations attached to the investments, in accordance with their own corporate governance policies and current best practice, including the UK Corporate Governance Code and the UK Stewardship Code.

The Trustees consider how ESG, climate change and stewardship is integrated within investment processes in appointing new investment managers and monitoring existing investment managers. Monitoring is undertaken on a regular basis and is documented periodically.

Investment restrictions

The Trustees have not set any investment restrictions on the appointed investment manager in relation to particular products or activities but may consider this in future.

Member views

The Trustees do not explicitly consult members when making investment decisions but regularly update members via newsletters and by making a copy of the Statement of Investment Principles available on request.

Stewardship
The Trustees' policy on the exercise of rights attaching to investments, including voting rights, and in undertaking engagement activities in respect of the investments is that these rights should be exercised by the investment manager on the Trustees' behalf. In doing so, the Trustees expect that the investment manager will use their influence as major institutional investors to exercise the Trustees' rights and duties as shareholders, including where appropriate engaging with underlying investee companies to promote good corporate governance, accountability and to understand how those companies take account of ESG issues in their businesses.

The Trustees will monitor and engage with the investment manager about relevant matters (including performance, strategy, capital structure, management of actual or potential conflicts of interest, risks, social and environmental impact and corporate governance matters), through the Plan's investment consultant and at any adhoc meetings.

The investment manager will be asked to provide details of their stewardship policy and engagement activities on at least an annual basis. The Trustees will, with input from their investment consultant, monitor and review the information provided by the investment managers. Where possible and appropriate, the Trustees will, through the Plan's investment consultant, engage with their investment manager for more information and ask them to confirm that their policies comply with the principles set out in the Financial Reporting Council's UK Stewardship Code.

8. Engagement with Investment Managers

The policy in relation to the Trustees' arrangements with their investment managers are set out below.

<u>8.1 Incentivising investment managers to align their investment strategy and decisions with the Trustees' policies:</u>

The investment manager is appointed based on their capabilities and, therefore, their perceived likelihood of achieving the expected return and risk characteristics required for the asset class being selected for.

The Trustees look to its investment consultant for their forward looking assessment of a manager's ability to outperform over a full market cycle. This view will be based on the consultant's assessment of the manager's idea generation, portfolio construction, implementation and business management, in relation to the particular investment fund that the Plan invests in. The consultant's manager research ratings assist with due diligence and questioning managers during presentations to the Trustees and are used in decisions around selection, retention and realisation of manager appointments.

If the investment objective for a particular manager's fund changes, the Trustees will review the fund appointment to ensure it remains appropriate and consistent with the Trustees' wider investment objectives.

As the Trustees invest in pooled investment vehicles they accept that they have no ability to specify the risk profile and return targets of the manager, but appropriate mandates can be selected to align with the overall investment strategy.

The corporate bond fund mandate is actively managed and the manager is incentivised through higher relative remuneration relative to an equivalent passive mandate. An actively managed appointment will be reviewed following periods of sustained underperformance. The Trustees will review the appropriateness of using actively managed funds (on an asset class basis) on an ad-hoc basis.

<u>8.2 Incentivising the investment managers to make decisions based on assessments about medium to long-term financial and non-financial performance of an issuer, and to engage with issuers in order to improve their performance in the medium to long-term</u>:

The Trustees will consider the investment consultant's assessment of how the investment manager embeds ESG into its investment process and how the manager's responsible investment philosophy aligns with the Trustees' responsible investment policy regarding financial and non-financial performance. This includes the investment managers' policy on voting and engagement. In addition, performance in the medium to long term can be improved where the investment manager (i) makes decisions based on assessments about medium to long-term financial and non-financial performance of an issuer of debt or equity; and (ii) engages with issuers of debt or equity. The Trustees will use this assessment in decisions around selection, retention and realisation of manager appointments.

The Trustees meet with the investment manager on an adhoc basis and can review the decisions made by their managers, including voting history (in respect of equities) and engagement activity. The Trustees can challenge such decisions to try to ensure the best long term performance over the medium to long term.

The Trustees delegate all voting and engagement activities to the investment manager. When required, the Trustees will question managers' voting decisions if they deem them out of line with the investment fund's objectives or the objectives / policies of the Plan.

The investment manager is aware that their continued appointment is based on their success in delivering the mandate for which they have been appointed to manage. If the Trustees are dissatisfied, then they will look to replace the manager.

<u>8.3 Aligning the evaluation of the investment manager's performance and the remuneration for investment management services with the Trustee policies:</u>

The Trustees receive 6 monthly investment performance reports from their investment consultant, which presents performance information over 3 months, 1 year, 3 years and since inception periods. The Trustees review the absolute performance, relative performance against a suitable index used as the benchmark, and against the manager's stated target performance (over the relevant time period) on a net of fees basis. The Trustees' focus is on long term performance but will put a manager 'on watch' if there are short term performance concerns.

If a manager is not meeting performance objectives, or their investment objectives for the mandate have changed, the Trustees may ask the manager to review their fees – either the Annual Management Charge or the performance related fee element.

The investment manager is remunerated by way of a fee calculated as a percentage of assets under management. The Trustees ensure that remuneration of the investment manager is consistent with their investment policies and the statement of investment principles and will look to for reduced remuneration or termination of the mandate if there are any concerns.

8.4 Monitoring portfolio turnover costs incurred by the investment manager:

The Trustees receive MiFID II reporting from their investment manager and investment consultant (where applicable) but do not analyse the information. The Trustees do not currently monitor portfolio turnover costs but may look to do this in the future.

However, the Trustees will continue to monitor industry improvements concerning the reporting of portfolio turnover (and associated costs). In future, the Trustees may ask the manager to report on portfolio turnover cost. They may assess this by comparing portfolio turnover across the same asset class, on a year-on-year basis for the same manager fund, or relative to the manager's specific portfolio turnover range in the investment guidelines or prospectus.

The Trustees do not currently set a portfolio turnover target - being the frequency with which the assets are expected to be bought/sold - because the investment manager does not provide the Plan with sufficient information to monitor and compare. As noted above, the Trustees will continue to monitor industry improvements and may look to set a target in the future.

8.5 Duration of the arrangement with the asset manager:

The Trustees are long-term investors and are not looking to change the investment arrangements on a frequent basis.

As the funds in which the Plan invests are open-ended, there is no set duration for the manager appointments. The Trustees will retain an investment manager unless:

- There is a strategic change to the overall strategy that no longer requires exposure to that asset class or manager;
- The manager appointment has been reviewed and the Trustees have decided to terminate.

9. Additional Voluntary Contributions

The Scheme provided a facility for members to pay AVCS that are invested in a range of options through Clerical Medical and the Standard Life Assurance Company. The AVC facility was closed many years ago and the assets invested now make up a very small proportion of the Plan's total assets. The Trustees monitor the AVC arrangements on an annual basis and seek expert advice (when required) to ensure the charges and performance remain competitive.

10. Compliance with this Statement

We, the Trustees, BlackRock, our appointed investment manager, and Mercer, our consultants, each have duties to perform to ensure compliance with this Statement. These are:

The Trustees will review this Statement regularly (or following any changes to the investment arrangements) on the advice of Mercer.

BlackRock, the investment manager, will prepare quarterly reports to the Trustees, including:

- Valuation of all investments held for the Plan;
- Records of all transactions, together with a cash reconciliation;
- A review of recent actions undertaken on behalf of the Plan, together with a summary of their current stated policy.

The investment manager will notify us in advance of any new investment categories in which they are proposing to invest.

Mercer, our consultants, will provide the advice needed to allow us to review and update this Statement regularly.

Signed .... Date ....

For and on behalf of the Trustees of the Scottish Milk Limited Retirement Benefits Plan

Date of Amendments

First Amendment:	June 2000	Ninth Amendment:	May 2009
Second Amendment:	September 2000	Tenth Amendment:	February 2012
Third Amendment:	April 2002	Eleventh Amendment:	May 2015
Fourth Amendment:	October 2002	Twelfth Amendment:	October 2016
Fifth Amendment:	December 2003	Thirteenth Amendment:	May 2019
Sixth Amendment:	July 2005	Fourteenth Amendment:	September 2020
Seventh Amendment:	January 2006	Fifteenth Amendment:	October 2022
Eighth Amendment:	June 2008		

Appendix

BlackRock Investment Management

BlackRock Investment Management manages the Plan's assets and has an objective to match the benchmark of the various underlying funds with the exception of the corporate bond fund, which has an objective to outperform its benchmark by 0.75% p.a. net of fees over rolling three year period:

Asset Class	Benchmark %	Index	Fees (p.a.)
World Equity	5.0	FTSE All World Developed	0.15% on the first £15 million 0.08% on the next £85 million 0.05% thereafter
Corporate Bonds	24.0	iBoxx Sterling Non-Gilts Bonds Index	0.35%
LDI Funds	71.0	Liability cashflows	
Gilt Funds			0.08% p.a. on the first £15m 0.04% p.a. on the next £85m
Leveraged single stock gilt funds and LMF Profile Funds.			0.15% p.a. on the first £50m
Sterling Liquidity fund			0.125% p.a.
Total	**100.0**		

Fees:

BlackRock will charge a minimum quarterly fee of £2,500.