Statement of Investment Principles

Coats UK Pension Scheme

September2023

Introduction

This document contains the Statement of Investment Principles ('the SIP') required under Section 35 of the Pensions Act 1995, as amended by the Pensions Act 2004 (the "Act"), for the Coats UK Pension Scheme ('the Scheme'). It describes the investment policy being pursued by the Trustee of the Scheme and is in compliance with the Government's voluntary code of conduct for Institutional Investment in the UK ("the Myners Principles"). This SIP also reflects the requirements of Occupational Pension Schemes (Investment) Regulations 2005.

The Trustee is responsible for the investment of the Scheme's assets and arranges administration of the Scheme. Where it is required to make an investment decision, the Trustee always receives advice from the relevant advisers first and it believes that this ensures that it is appropriately familiar with the issues concerned.

Declaration

The Trustee confirms that this SIP reflects the principles governing how decisions about investments are made for the Scheme. The Trustee acknowledges that it is responsible, with guidance from the advisers, for ensuring the assets of the Scheme are invested in accordance with these principles.

Signed *Chris Martin* **Date** 5 October 2023

For and on behalf of the Trustee of the Coats UK Pension Scheme

Scheme Governance

The Trustee is responsible for the governance and investment of the Scheme's assets. The Trustee considers that the governance structure set out in this SIP is appropriate for the Scheme as it allows the Trustee to make the important decisions on investment policy, while delegating the day-to-day aspects to the Asset Managers as appropriate.

The Trustee has also established an Investment and Funding Committee ("IFC"), and has delegated the following authorities to it:

- Review of investment strategy.
- Recommendations of long-term strategic asset allocations, including consideration of alternative asset classes.
- Monitor cash management procedures.
- Recommendations of suitable investment management styles, including consideration of their respective costs.
- Advise on the choice of appropriate benchmarks.
- Recommendations of long-term funding targets and overall funding strategy.
- Monitor Scheme funding position and report issues to Trustee Board.
- Monitor Scheme performance against any agreed flight plan and make recommendations to act in accordance with any agreed de-risking protocol.
- Negotiate deficit recovery plan and triennial valuation with the Company.
- Monitor the appropriateness of risk controls.
- Make decisions on the appointment and removal of Asset Managers and custodians and the associated terms. For the avoidance of doubt these like for like changes should be within the same asset class, with similar approaches (e.g. active or passive) and should not meaningfully change the broad risk exposures that come from the mandate.
- Review and monitor Investment Consultant and managers.
- Understand and monitor the level of transaction costs incurred by the managers.
- Draft an updated Statement of Investment Principles when appropriate.
- Recommendations regarding corporate governance, responsible investment, stewardship and other such investment issues.
- Monitor the investment aspects of the AVC and legacy, closed DC arrangements.
- Recommendations on appropriate investment training.
- Where appropriate, make short-term decisions due to rapidly changing market conditions or similar urgent circumstances.

- Monitor the Trustee Risk Register in relation to investment, funding and covenant matters to ensure this is kept up-to-date.

Investment Objectives

- The principal objective of the Trustee is to invest the assets of the Scheme to meet its liabilities when they fall due.
- The investment strategy of the Scheme is managed and monitored using a Pensions Risk Management Framework (PRMF), which outlines the funding objectives and risk constraints set by the Trustee. The PRMF is reviewed and monitored by the Trustee on at least a quarterly basis including the expected return on assets as provided by the Investment Consultant.
- The Trustee has agreed a primary funding objective for the Scheme to reach full funding by 2028 using a liability discount rate of Gilts + 0.40%. This prudent liability discount rate will help to reduce the Scheme's dependence on the Sponsor.
- The Trustee has set a risk budget of 7% for the Funding Ratio-at-Risk (FRaR), therefore the investment strategy should not risk the funding level decreasing more than 7% with 95% confidence on a Gilts + 0.40% basis. Within this risk budget, the Trustee seeks to diversify risks across a range of exposures, and to focus on risks that they view as well-positioned to outperform the liabilities.
- In setting the investment strategy, the Trustee aims to:
  - Target an expected return that includes a buffer above the required return to meet the funding objective.
  - Manage the investment risk including that arising due to mismatch between assets and liabilities and maintain the total risk on the Scheme below the risk budget set in the PRMF.
  - Maintain suitable liquidity of assets such that the Scheme is not forced to buy and sell investments at certain times to pay member benefits or meet potential collateral calls.
- The Scheme holds investments as permitted by its Trust Deed and Rules.
- As the DC section is closed to future contributions, the Trustee's main investment objective is to ensure the investment option(s) remain suitable for the relevant members.

Investment Strategy

Having considered advice from its advisers, and having due regard for the objectives, the liabilities of the Scheme, the risks of and to the Scheme and the covenant of Coats Group Plc., the Trustee has adopted an appropriate investment strategy.

This investment strategy is designed to ensure the following criteria are met:

- **Diversification**

The choice of investments is designed to ensure that the Scheme's investments are adequately diversified given the Scheme's circumstances. The Trustee will monitor the strategy regularly to ensure that they are comfortable with the level of diversification.

- **Suitability**

The Trustee has taken advice from the advisers to ensure that the asset allocation strategy is suitable for the Scheme, given its liability profile, any legal requirements, regulatory guidance and specifications in the Trust Deed.

Risk management

The Trustee will look to reduce overall risk by hedging the impact of interest rate and inflation movements on the underlying liabilities. By reducing the impact of interest rate and inflation movements on the funding ratio, the Scheme is able to spend its risk budget on return-seeking assets.

In addition to the hedging strategy, the Scheme has purchased a bulk annuity insurance policy. The policy reduces overall risk by providing a match to investment and non-investment risks for the liabilities of the Scheme to which the policy relates (i.e. interest rate, inflation and longevity risks).

Monitoring

Asset Manager Policy

The Trustee delegates the day-to-day management of the assets to multiple Asset Managers.

Asset Managers are carefully selected by the Trustee to manage each of the underlying mandates, following guidance and written advice from its Investment Consultant. Details of the investment objectives and mandates for each Asset Manager are set out in the Investment Implementation Policy document.

Due to the cost benefits and ease of implementation, the Trustee predominantly invests in pooled investment vehicles. The Trustee recognises that due to the collective nature of these investments, there is less scope to directly influence how the asset manager invests. However, the Scheme's Investment Consultants ensure the investment objectives and guidelines of the manager are consistent with that of the Trustee. Where the Trustee does invest via segregated investment vehicles, the terms of the long-term relationship between the Trustee and the manager are set out in a separate Investment Management Agreement (IMA). These document the Trustee's expectations of their managers; alongside the investment guidelines they are required to operate under.

Where relevant, the Trustee requires its Asset Managers to invest with a medium to long-term time horizon, and to use any rights associated with the investment to drive better long-term outcomes. For some asset classes, the Trustee does not expect the respective Asset Managers to make decisions based on long-term performance. These may include investments that provide risk reduction through hedging, consistent with the Trustee's strategic asset allocation.

The Trustee appoints its Asset Managers with an expectation of a long-term partnership, which encourages active ownership of the Scheme's assets. When assessing a manager's performance, the focus is on longer-term outcomes, and the manager is assessed over a medium to longer-term timeframe, subject to a minimum of three years.

The Trustee would not expect to terminate a manager's appointment based purely on short-term performance. However, a manager's appointment could be terminated within a shorter timeframe than three years due to other factors, such as a significant change in business structure, the investment team, or changes in the strategic needs of the Scheme.

Managers are paid a fee for a defined set of services based on the size of assets managed on behalf of the Scheme (as well as additional performance fees, where these have been previously agreed with a manager in repayment for performance above a specified benchmark). The Trustee reviews the fees periodically to confirm they are in line with market practices.

The Asset Managers should provide a written performance report each quarter to the Trustee through the Investment Consultant. The Investment Consultant will produce a manager report for the Trustee based on this information. The Trustee will meet the managers on an ad hoc basis to review the managers' actions and investment performance. The Investment Consultant will assist the Trustee in fulfilling their responsibility for monitoring the Asset Managers. The Trustee's policy towards monitoring non-financial performance is set out in the Social, Environmental and Ethical Issues Policy.

The Trustee reviews the portfolio transaction costs and portfolio turnover range of managers periodically where the data is disclosed and available. The Trustee will then determine whether the costs incurred were within reasonable expectations, with assistance from the Investment Consultant.

SIP

The Trustee aims to review this SIP annually, or, without delay, following any changes to the investment strategy, and modify it with consultation from their advisers and the Sponsor. There will be no obligation to change this SIP, any Asset Manager or its Investment Consultant as part of such a review.

Risks

The Trustee recognises there are numerous risks involved in investing the assets of the Scheme. These include (but are not limited to) deficit risk, manager risk, liquidity risk, currency risk, interest rate and inflation risk, political risk, sponsor risk and counterparty risk. The Trustee monitors and manages these risks through measures specific to each risk.

In respect of the Defined Contribution section, the Trustee recognises there is the risk that past contributions and ongoing investment returns fail to provide an adequate level of benefits for the members of this section. The Trustee acknowledges the difficulties in directly addressing some of these risks as the DC section is closed to future contributions and members are only invested in with profits policies.

The Trustee will keep these risks and how they are measured and managed under regular review.

Other Issues

Statutory Funding Objective

The Trustee will obtain and consider proper advice on the question of whether the investments are satisfactory having regard to both the investment objectives and the requirement to meet statutory funding requirements.

The funding position is reviewed periodically by the Scheme Actuary, with a full actuarial valuation at least every three years.

The Trustee will consider, with their advisers, whether the results of these actuarial Valuations suggest that any change to investment strategy is necessary to ensure continued compliance with the statutory funding objective.

Corporate Governance

The Trustee policy on the exercise of rights attaching to investments, including voting rights, is that these rights should be exercised by the Asset Managers on behalf of the Trustee having regard to the best financial interests of the beneficiaries. The Trustee has been made aware of each Asset Manager's corporate governance policy where appropriate and has delegated the exercise of such rights to the Asset Managers.

Social, Environmental and Governance Issues

The Trustee incorporates all financially material considerations into decisions on the selection, retention and realisation of investments through strategic asset allocation decisions and the appointment of Asset Managers, so far as possible. The Trustee believes the investment time horizon to fund all future benefits is a long-term one and that it must therefore invest responsibly, targeting sustainable outcomes to ensure it is able to pay its members on time, and in full. Non-financial matters are not taken into account in the selection, retention and realisation of investments.

The Trustee believes that environmental, social and governance ("ESG") factors (including but not limited to climate risk) will be financially material over the time horizon of the Scheme, but will have varying levels of importance for different types of assets invested by the Scheme. As such, it will consider ESG-related factors when making decisions in relation to the Scheme's asset allocation and manager selections, including any future buy-in/out transactions.

The Trustee believes ESG considerations are one of a number of important inputs into decision making when setting the strategic asset allocation of the fund. The Trustee considers how the exposure to risk is managed when selecting asset classes, sub-sectors, and specific Asset Managers or strategies. The Trustee believes that there may be investment opportunities that can contribute towards solving sustainability challenges and provide compelling risk-adjusted returns. It will consider such opportunities as appropriate and when consistent with its wider risk and return objectives. The Trustee is also mindful of the societal impact of its investment decisions and is committed to a responsible investment approach which is at once responsive to this and consistent with its overarching fiduciary obligations.

When selecting new Asset Managers, the Trustee must make itself comfortable that they can adequately manage ESG-related risks on its behalf and invest in line with its beliefs (where possible). Whilst the Trustee expects its Investment Consultant to monitor the ESG capabilities of its managers, it seeks to review all existing managers periodically to ensure they are held to account. If the Trustee is not satisfied that its managers are investing responsibly, it will express its concerns, retaining the ability to divest if adequate improvements are not made.

The Trustee expects the provider of the insurance agreement, Aviva, to operate similar standards in respect of managing ESG-related risks and stewardship as set out for the Scheme's asset managers above.

The Trustee understands climate change as a systemic, long-term financial risk to the value of its investments and will explicitly consider the risk it poses when making investment decisions.

The Trustee recognises that best practices will continue to evolve and adapt in this area, and therefore it requires its Investment Consultant to keep it updated on the most pertinent developments. The Trustee is committed to periodically reviewing its approach to responsible investment to ensure it remains appropriate.

Stewardship and Engagement Policy

The Trustee understands good stewardship to be the responsible allocation, management, and oversight of capital - with the aim of creating long-term value for members and sustainable benefits for the economy, environment, and society. The Trustee aims to use their influence as an owner of assets to ensure that good practices are reflected in terms of ESG factors and will hold investment managers to account for the effective use of their influence as owners of assets.

Resourcing stewardship

The Trustee's approach to stewardship reflects its broader investment approach: to hire investment managers and hold them to account for delivery, rather than to invest directly. In a similar way the Trustee undertakes stewardship through oversight and challenge its investment managers rather than operating as active stewards directly of the underlying assets in which it invests.

The role of the IFC – acting under delegated authority of the Trustee – is to provide oversight of the investment managers. The IFC hire appropriately skilled investment managers, set clear expectations, assess the quality of their performance, and will hold them to account where they identify deficiencies or areas for further improvement.

Key area of focus

To best channel its stewardship efforts, the Trustee believes it should focus on a key theme. The key theme has been chosen by assessing its relevance to the Scheme and its members, the financially material risks it poses, and the maturity and development of thinking within the industry that allows for ease of integration into the Trustee's approach. The Trustee's chosen theme is 'climate change'.

Significance of stewardship in appointment and monitoring of investment managers

It is the responsibility of the IFC to lead the Trustee's engagements with investment managers. The Trustee will not appoint investment managers that cannot demonstrate the standards to which it holds existing investment managers. These expectations can be summarised as:

- Effective processes for and delivery of stewardship activity, alignment with leading standards, and evidence of engagement related to our key themes, with the aim of positive change;

- Provision of tailored reporting on stewardship activities and outcomes; and
- Participation as appropriate in public policy debates and the development of best practices.

The Trustee expects its investment managers to provide specific evidence they have acted in accordance with these expectations which should provide the Trustee with enough insight to ascertain whether its investment managers are practicing effective stewardship that is best aligned with the Trustee's long-term interests. Where the IFC identify deficiencies they will be escalated accordingly, with the ultimate response being the removal of mandates where the Trustee believes it is in the interests of members to do so. The Trustee view incremental improvements by its investment managers as the key success measure of its own stewardship activities.

Engagement: expectations and process

The Trustee expects investment managers to engage with issues to maintain or enhance the long-term value of the Scheme's investments and limit negative externalities on the planet and society. This includes performance, strategy, risks, capital structure, conflicts of interest, and environmental, social or governance considerations.

The Trustee recognises that there is no 'one-size-fits-all' stewardship approach and instead encourages its investment managers to prioritise stewardship opportunities and apply the most suitable/influential engagement strategies based on their in-depth knowledge of a given asset class, sector, geography and/or specific company or other asset.

Investment managers are expected to have robust ESG, climate change, and stewardship policies and processes in place. These are used to define how underlying companies are monitored and engaged with, how progress is measured, and when escalation is required. The Trustee expects manager engagement with companies to be underpinned by engagement on public policy matters where relevant. The Trustee expects that these assessments and progress in stewardship activities are tracked over time, to maintain continuity of activity and to assess the effectiveness of stewardship delivery. The Trustee will challenge its investment managers when their engagements are deemed to be of deficient quality.

In order to drive corporate change, and where initial engagement has made little progress, the Trustee expects its investment managers to escalate engagement accordingly. The Trustee allows investment managers discretion over the appropriate tools to deploy; however, expects these to be communicated with issuers' management teams. Should there still be little progress made after escalation, the Trustee expects investment managers to consider disinvestment as a final course of action.

Voting: expectations and process

The exercise of voting rights for equity holdings within pooled funds has been delegated to the Trustee's investment managers. The Trustee therefore does not direct how votes are exercised within these mandates and does not have its own proxy voting provider. Nonetheless, the Trustee fully recognise and appreciate the value of voting as a signal or ultimate sanction in influencing company behaviour. As active owners, it is the Trustee's responsibility to hold investment managers to account for their voting activities to ensure they are exercising voting rights in the Scheme's best interests. As such, the Trustee considers investment managers' voting policies and records, and requires its investment managers to report significant votes to us as relevant.

Investment managers are expected to have their own voting policies, informed by leading global standards, and that fully integrate ESG considerations. Investment managers are expected to be informed by the views of proxy voting service providers, but retain ultimate ownership of the decision and are expected to apply judgement as to whether they follow the recommendation of their advisor. The exercise of voting rights should form part of a wider engagement dialogue and if investment managers wish to vote contrary to management recommendations, the Trustee expects this is communicated and its investment managers' views expressed to the company.

Whereas voting responsibilities are outsourced to investment managers, the Trustee recognises its fiduciary and regulatory responsibility to retain agency in the process. Investment manager oversight is the key mechanism for this, and the Trustee will therefore hold its investment managers accountable not only for voting activity as a whole, but also how they have voted in significant votes. Under DWP Guidance, it is the Trustee's responsibility to define the significance of votes placed on the Scheme's behalf, and to be transparent with stakeholders and beneficiaries regarding outcomes.

Significant votes have been defined as votes which meet one or more of the following criteria. Please note the more of these criteria a vote meets, then the more significant the vote is likely to be deemed, with the most significant votes to be disclosed in the Implementation Statement (rather than all significant votes):

- Votes relating to the Trustee's key stewardship theme;
- Votes relating to an issuer to which the Scheme has a large £ exposure;
- Votes identified due to potential controversy, driven by the size and public significance of a company, the nature of the resolution, and the weight of shareholder vote against management recommendation.

Buy-in Policy

In November 2022, the Trustee entered into a bulk annuity insurance policy with Aviva PLC, which provides monthly payments to the Scheme covering member benefit payments to the insured population, c.30% pensioner members at outset.

The Scheme has counterparty risk in relation to Aviva i.e. the risk the insurance company defaults on agreed payments to the Scheme. The Trustee, upon receiving advice from specialist advisors prior to the transaction, is satisfied with the financial strength of Aviva and is additionally protected by regulation in the form of supervision and intervention by the Prudential Regulatory Authority, and takes further comfort from the existence of Financial Services Compensation Scheme ("FSCS") protection.

Additional Voluntary Contributions (AVCs)

Under the Scheme's Trust Deed and Rules, members are unable to invest Additional Voluntary Contributions ('AVCs'), however, they are able to move existing AVCs.

The Trustee has selected a range of investment funds for the AVCs to be invested in, which are reviewed regularly having regard to their performance, the objectives and the views of the advisers.

Corah Defined Contribution Section

The Scheme also has a legacy Defined Contribution (DC) Section for some members of Corah (a company acquired by the Sponsor group in the past). The members of the DC section within the Corah benefits structure are all invested in with profits policies provided by Prudential. Members have access to the With-Profits Cash Accumulation Fund managed by Prudential. The fund is typically invested in a broad conventional mix of assets (equity, fixed interest and property).

The Trustee regularly reviews the fund with regard to its performance, fees and objectives.