Statement of Investment Principles

This is the Statement of Investment Principles made by International Power Group Trustee Limited, Trustee of the International Power Group of the Electricity Supply Pension Scheme (ESPS) (the 'Scheme'), in accordance with the Pensions Act 1995 (as amended). This Statement, which was approved by the Trustee on 11 August 2020 is subject to periodic review at least every three years and without delay after any significant change in investment policy and/or regulatory requirement.

In preparing this Statement, the Trustee has consulted with the principal employer to the Scheme (International Power Ltd.) and has taken written advice from Hymans Robertson LLP, who has been appointed as the Investment Adviser to the Scheme.

In relation to the Myners Code of Conduct for Investment Decision Making, the extent of the Trustee's adoption of the Code is provided in a separate document named Myners Code Adherence Document. The document, which is available to Scheme members on request, includes details of the Scheme's investment strategy and structure.

Scheme Objectives

The primary objective of the Scheme is to provide pension and lump sum benefits for members on their retirement or other entitlement trigger and/or benefits on death before or after retirement, for their dependants, on a defined benefits basis.

One of the Trustee's overriding funding principles for the Scheme is to agree a set of employer contributions at a level which is sufficient:

- to build up assets to provide for new benefits of active members as they are earned;
- to recover any shortfall in assets relative to the value placed on accrued liabilities over the longer term; and
- to ensure that there are always sufficient assets of the Scheme (at their realisable value) to meet 100% of benefits as they fall due for payment to members.

For employee members, benefits are based on service completed but take account of expected future salary increases. The value of liabilities is calculated on the basis agreed by the Trustee and the Employer; the Trustee also considers the Scheme's funding position on a more stringent low risk basis. These funding positions are monitored regularly by the Trustee and formally reviewed at each triennial actuarial valuation, or more frequently as required by the Pensions Act 2004.

The Trustee expects to de-risk assets over time, and the Technical Provisions basis agreed with the Employer makes an allowance for de-risking of the investment strategy with a long-term objective to achieve fully funded status on a gilts + 0.5% p.a. basis by 2033. At that point, the Trustee expects that the Scheme can thenceforth be administered on a low risk basis with:

- an asset allocation which is expected to achieve gilts + 0.75% p.a. in order to maintain a prudence buffer against adverse liability experience;
- interest rate and inflation hedging close to 100%; and
- an allowance for a prudent view on mortality risk.

While the Technical Provisions basis assumes de-risking will happen on a straight-line basis over time, the Trustee has agreed with the Employer that actual de-risking decisions will be made with reference to various relevant matters, including Asset Liability Modelling. It has been agreed that de-risking will be considered when modelling indicates that risk can be reduced while maintaining an acceptable probability of achieving full funding on a gilts + 0.5% p.a. basis by 2033 ('the long-term target'). Within this objective, the Trustee is seeking to achieve self-sufficiency whereby the assets are used over time to pay all future benefits whilst taking limited investment risk. In addition, there may be opportunities to facilitate one or more partial buy-ins if pricing is sufficiently attractive, and the Trustee monitors general buy-in market pricing on a quarterly basis for this purpose.

Investment Strategy

Based on advice received from the Investment Adviser the Trustee has translated its objectives into a suitable strategic asset allocation benchmark for the Scheme, namely 21.5% in equity assets, 31.5% in alternative growth assets and 47% in matching assets. In setting this benchmark the Trustee has considered the Scheme's liquidity and Employer covenant strength, along with an assessment of the Trustee's risk appetite based on Asset Liability Modelling ("ALM") carried out by the Investment Adviser. The aim is to maintain at least a 70% probability of success against the long-term target.

This has been translated into benchmarks for the managers, which are consistent with the Scheme's overall strategy. These investment managers' benchmarks are consistent with the Trustee's views on the appropriate balance between maximising the long-term return on investments and minimising volatility and risk. All day to day investment decisions have been delegated to authorised investment managers.

The investment strategy takes due account of the maturity profile of the Scheme (in terms of the relative proportions of liabilities in respect of pensioners and active members), together with the level of disclosed surplus or deficit (relative to the funding bases used). It is intended that the Trustee reviews the investment strategy at least every three years following actuarial valuations of the Scheme. The Trustee also monitors fund performance relative to the investment managers' benchmarks on a quarterly basis. In reviewing strategy and performance, the Trustee takes written advice, as appropriate.

To achieve the Scheme's objectives the Trustee has decided the following:

Choosing Investments: The Trustee will appoint managers who are appropriately authorised to undertake investment business. The Trustee has given the managers specific directions as to the asset allocation and benchmark, but investment choice has been delegated to the managers.

The Trustee has appointed each of its managers to deliver a specific benchmark or performance target, which in the aggregate are expected to deliver the Scheme investment strategy.

For segregated mandates, the terms on which the manager is engaged will be defined specifically for the Scheme. Where the Trustee invests in pooled funds the objectives of the fund and the policies of the manager will be evaluated by the Trustee to ensure that they are appropriate.

Remuneration for each mandate is determined at the inception of the mandate based on commercial considerations and typically set on an ad valorem basis but may include performance related fees. The Trustee periodically reviews the fees against industry standards.

The Trustee reviews the nature of Scheme investments on a regular basis. The Trustee seeks and considers written advice from the Investment Adviser when determining the appropriateness of each manager and mandate for the Scheme, particularly in relation to diversification, risk, expected return and liquidity. The Trustee recognises the long-term nature of its liability profile and appoints its managers to invest in such a way that generates long-term sustainable returns for the growth assets. The Trustee will carry out necessary due diligence on the underlying investment decision making process to ensure the manager makes investment decisions over an appropriate time horizon aligned with the Scheme's objective.

For open-ended investments, the Trustee engages managers at outset and on an ongoing basis with no pre-determined term of appointment, although the Trustee expects the minimum duration of the appointment will be three years. The Trustee monitors its managers' performance against their respective benchmarks or targets on a regular basis over short medium and long-term time horizons against several metrics. Material deviation from performance or risk targets is likely to result in the mandate being formally reviewed.

Kinds of investment to be held: The Scheme may invest in quoted and unquoted securities of UK and overseas markets including equities and fixed interest and index linked bonds, property, commodities and cash either directly or through pooled funds. The Scheme may also make use of derivatives and contracts for difference. The Trustee considers all of these asset classes to be suitable to the circumstances of the Scheme.

Balance between different kinds of investments: The Scheme's managers will hold a mix of investments which reflects their views relative to their respective benchmarks. The managers will maintain a diversified portfolio of assets through direct investment or via pooled funds.

Risk: The Scheme is exposed to several risks which pose a threat to the Scheme meeting its objectives. The principal risks affecting the Scheme are:

Funding risks

- Financial mismatch – The risk that Scheme assets fail to grow in line with the developing cost of meeting the liabilities.
- Changing demographics –The risk that longevity improves, and other demographic factors change, increasing the cost of the Scheme benefits.
- Systemic risk - The possibility of an interlinked and simultaneous failure of several asset classes and/or investment managers.

Risk is assessed by monitoring the Scheme's asset allocation and investment returns relative to the benchmark. The Trustee also assesses risk relative to liabilities by monitoring the funding level of the Scheme, the delivery of benchmark returns relative to liabilities and by regularly updating the ALM to monitor the probability of success against the long- term target.

The Trustee keeps mortality and other demographic assumptions under review and these are considered formally at triennial valuations. The Trustee may enter into insurance contracts to reduce these demographic risks, if appropriate.

The Trustee seeks to mitigate systemic risks through a diversified portfolio, but it is not possible to make specific provision for all possible eventualities.

Asset risks

- **Concentration** - The risk that a significant allocation to any single asset category and its underperformance relative to expectation would result in difficulties in achieving funding objectives.
- **Illiquidity** - The risk that the Scheme cannot meet its immediate liabilities because it has insufficient liquid assets or insufficient cash flow income from assets.
- **Currency risk** – The risk that the currency of the Scheme's assets underperforms relative to Sterling.
- **Manager underperformance** - The failure by the fund managers to achieve the rate of investment return assumed in setting their mandates.
- **Environmental, Social and Governance (ESG) risks** – the extent to which ESG issues are not reflected in asset prices and/or not considered in investment decision making leading to underperformance relative to expectations.
- **Climate risk** - The extent to which climate change causes a material deterioration in asset values as a consequence of factors including but not limited to policy change, physical impacts and the expected transition to a low-carbon economy.

The Trustee manages asset risks as follows:

- By investing across a range of assets, including quoted equities and bonds, the Trustee recognises the potential need to access funds in the short term to pay benefits. For pooled funds, the Scheme holds less than 10% of the total value of each.
- The risk of manager underperformance is mitigated by the inclusion of passive investment mandates. Also, in appointing several investment managers, the Trustee has considered the risk of underperformance by any single investment manager.

The Trustee does not expect managers to take excess short-term risk. The Trustee's approach to the consideration of ESG risks and climate risk is set out in further detail below.

Other provider risk

- **Transition risk** - The risk of incurring unexpected costs in relation to the transition of assets.
- **Custody risk** - The risk of loss of Scheme assets when held in custody or when being traded.
- **Credit default** - The possibility of default of a counterparty in meeting its obligations.

The Trustee monitors and manages risks in these areas through a process of regular scrutiny of its providers, and audit of the operations it conducts for the Scheme or has delegated this role to the appointed investment managers. When carrying out transitions, the Trustee seeks professional advice.

De-risking: The Trustee uses ALM analysis at Trustee meetings to assess the funding level, appropriate risk and hedge levels with the aim of maintaining an acceptable probability of success against the long-term target.

Expected return on investments: Over the long-term, investment returns are expected to exceed the rate of return assumed by the Actuary.

Realisation of investments: Most of the Scheme's investments may be realised quickly if required, although the property funds (which represent less than 10% of the Scheme's assets) may be difficult to realise quickly in certain circumstances.

Portfolio turnover: The Trustee has expectations of the level of turnover within each mandate which is determined at the inception of the mandate. The Trustee expects managers to report on at least an annual basis on the underlying assets held within the portfolio and any material changes in holdings over the period. The Trustee will challenge its managers if there is a sudden change in portfolio turnover or if it seems excessive. The Trustee will request turnover costs over the Scheme reporting year. Where possible, the Trustee will compare the costs to a theoretical portfolio turnover and cost for an appropriate index.

Custody: The Scheme uses custody services provided through the central Trustee of the ESPS, Electricity Pensions Trustee Limited. Most of the the Scheme's investments are in pooled funds and as a result the custody of the Scheme's investments is arranged by the appointed investment managers. The pooled fund units and segregated assets are held by the custodian of the Electricity Pensions Trustee Limited on behalf of the Scheme.

Employer Covenant

The Trustee has a standing agenda item for its meeting each quarter to consider the strength of the Employer covenant and receives regular information from the Employer to facilitate this, including semi-annual presentations on the Employer's strategic plans, quarterly management accounts and more detailed full year data. Any material change in the strength of the Employer covenant may trigger a reassessment of the strategic asset allocation benchmark and the de-risking plan (discussed below)

As part of the agreement on the 2016 Triennial valuation the Trustee and the Employer agreed that additional contributions will be payable if a formal estimate of the buyout deficit reveals that the Employer's net assets have fallen below either of two prescribed triggers (ten times the Group's estimated buy-out deficit and five times the Group's estimated buy-out deficit). In the event of a payment being made to the Trustee as a result of a Trigger

Event arising, a reassessment of the strategic asset allocation benchmark and the de-risking plan will also take place.

Financially material factors

The Trustee recognises that the consideration of financially material factors over the appropriate time horizon of the investments, including ESG factors, is relevant at different stages of the investment process. The Trustee further recognises that the financial materiality of any factor, including ESG factors, is context specific and that whilst some factors may be relevant to certain stocks/assets, they may not be relevant to others.

The Trustee will consider such factors in determining the selection, retention and realisation of investments, where there is sufficient data or evidence to allow it to do so systematically. Where there is not sufficient data or evidence, the Trustee will require that its managers take such considerations into account within their decision making. The Trustee has explicitly acknowledged the relevance of climate change and ESG factors in framing its investment beliefs and these beliefs are reflected in the principles set out below and the broader implementation of strategy.

Strategic and structural considerations

The strategic asset allocation benchmark has been determined using appropriate long-term economic and financial assumptions from which expected risk/return profiles for different asset classes have been derived. These assumptions apply at a broad market level and are considered to reflect implicitly all financially material factors.

Given the inherent uncertainty, the Trustee has not made explicit allowance for the risks of climate change in setting the strategic asset allocation benchmark. The Trustee periodically discusses climate change with its investment adviser/managers to consider the potential implications for the Scheme's investments.

Given the discretion afforded to the active investment managers, the Trustee expects that its managers will take account of all financially material factors including the potential impact of ESG factors in the implementation of their mandate.

Selecting investment managers

Within active mandates, the Trustee has delegated responsibility for the consideration of stock specific issues to the individual investment managers. The Trustee is satisfied that the managers are following an approach which takes account of all financially material factors.

In passive mandates, the choice of benchmark dictates the assets held by the manager and the manager has minimal freedom to take account of factors that may be deemed to be financially material. The Trustee accepts that the passive manager will deliver returns in line with the benchmark and believes the choice of benchmarks will deliver appropriate risk adjusted returns. The Trustee will review the index benchmarks employed for the Scheme on at least a triennial basis.

In selecting new investment managers, the Trustee explicitly considers potential managers' approach to responsible investment and the extent to which managers integrate ESG issues in the investment process.

The Trustee expects the Investment Adviser to provide input and analysis to assist the Trustee in assessing the investment managers' performance. The Trustee will highlight any areas of concern identified during such reviews to the manager as part of its engagement process and request that the manager takes appropriate action. This may include concerns over performance, risk management, stewardship practices, investment process and operational issues and, where such concerns are raised, the Trustee will require the manager to demonstrate levels of improvement. Failure to achieve the desired improvements may result in the mandate being reduced or terminated.

Non-financially material factors

Given the objectives of the Scheme, the Trustee has considered including non-financially material factors in the Scheme's investment strategy but has decided not to impose any restrictions or exclusions.

Voting and engagement

The Trustee is supportive of the UK Stewardship Code and expects the managers to comply and produce a commitment statement. The Trustee also requires the managers to be committed to the United Nations' Principles for Responsible Investment.

The Trustee delegates voting decisions on stocks to its managers on the basis that voting power will be exercised by them with the objective of preserving and enhancing long-term shareholder value. The managers are expected to use engagement with company management for positive influence as opposed to divestment from companies unaligned with the Scheme's objectives.

Where relevant, the Trustee has reviewed the voting policies of its managers and determined that these policies are appropriate. Where appropriate, the Trustee will seek further information from its managers on how portfolios may be affected by a particular issue.

The Trustee does not engage directly but believes it is sometimes appropriate for its managers to engage with key stakeholders in order to consider the management of conflicts of interest and improve corporate behaviors. Managers are expected to notify the Trustee of any issue on which they believe it may be beneficial for the Trustee to undertake further engagement. The Trustee will review engagement activity undertaken by the managers as part of its broader monitoring activity.

Responsibility for investment decisions has been delegated to the managers which includes consideration of the capital structure of investments and the appropriateness of any investment made and where managers are responsible for investing in new issuance, the Trustee expects the manager to engage with the issuer about the terms on which capital is issued and the potential impact on the rights of new and existing investors.

The Trustee considers any conflicts of interest arising in the management of the Scheme and ensures the managers have appropriate conflicts of interest policy in place. The managers are required to disclose any potential or actual conflict of interest in writing to the Trustee.

Monitoring

The Trustee will review manager engagement and voting activity on a periodic basis in conjunction with its Investment Adviser and uses this information as a basis for discussion with the investment managers. Where the Trustee deems it appropriate, any issues of concern will be raised with the manager for further explanation. The Trustee aims to meet with all its managers on a periodic basis. The Trustee provides the managers with an agenda for discussion, including issues relating to individual holdings and, where appropriate, ESG or other issues. Managers are challenged both directly by the Trustee and by its Investment Adviser on the impact of any significant issues including, where appropriate, ESG issues that may affect the prospects for return from the portfolio.

Additional Voluntary Contributions (AVCs)

The Trustee gives members who joined prior to 6 April 2006 the opportunity to invest in a range of vehicles at the members' discretion.

Signed by the Chair on behalf of International Power Group Trustee Limited

Chair …Approved by the Trustee………………… Date …23 September 2020…………………………