First Hydro Company Group of the Electricity Supply Pension Scheme
Statement of Investment Principles ("SIP")

1. Introduction

This edition of the Statement has been prepared by the Group Trustees of the First Hydro Company Group of the Electricity Supply Pension Scheme (the "Scheme") in accordance with the requirements of Section 35 of the Pensions Act 1995 (as amended), and Regulation 2 of the Occupational Pension Schemes (Investment) Regulations 2005 (as amended), and any subsequent additional regulations.

This SIP replaces the previous SIP dated February 2020. In preparing this edition the Group Trustees have taken appropriate written advice from Lane Clark & Peacock LLP, Investment Adviser to the Scheme, whom we believe to be suitably qualified and experienced to provide such advice. The advice considered the suitability of investments including the need for diversification given the circumstances of the Scheme and the principles contained in this SIP. The Group Trustees have also consulted with the sponsoring employer, First Hydro Company. This Statement is consistent with the Scheme's governing documents.

The Scheme is registered with HM Revenue and Customs. The Scheme provides final-salary related benefits. No employer-related investment is intended by the Group Trustees. The sponsoring employer intends to remit all relevant contributions to the Group Trustees within the relevant timescales.

2. Investment Objectives

The primary objective for the Scheme is to ensure that the benefit payments are met as they fall due. In addition to this primary objective, the Group Trustees also aim for the expected return on the Scheme assets to be maximised, whilst managing and maintaining risk at an appropriate level.

3. Investment Strategy

With input from our advisers and in consultation with the employer, we reviewed the investment strategy for the Scheme in August 2021, considering the objectives described in Section 2.

The investment strategy is shown in the following table.

Asset class	**Strategic allocation**
Global equities	10%
Diversified growth	16%
Forestry	6%
Long lease property	5%
High yield bonds	8%
Corporate bonds	13%
Liability driven investment & cash	42%
Total	**100%**

The Group Trustees' target is to hedge 85% of interest rate and inflation risk on the Technical Provisions basis.

Our policy is to target the maximum expected return level subject to ensuring the level of investment risk is appropriate to reflect the Scheme's circumstances. We believe that the strategy above meets this objective.

There is no formal rebalancing policy. We monitor the asset allocation from time to time. If material deviations from the strategic allocation occur, we will consider with our advisers whether it is appropriate to rebalance the assets.

4. Expected Return on Investments

The LDI mandate can invest in long- and short-dated, inflation-linked and fixed versions of pooled leveraged bond funds. Each fund aims to match a generic cashflow profile and the use of multiple funds by the Group Trustees results in a closer match with the Scheme's cashflow profile.

The passive Global Equity product is expected to track its composite index, the relevant Solactive Low Carbon Transition Index.

Specific outperformance targets for the actively managed products used are included in the appendix.

5. Risk Management & Risk Measurement

The Group Trustees are satisfied that their investment managers are prudent and professional in their general approach to investment. The investment products used involve holding units in pooled funds that maintain diversified portfolios of underlying assets (e.g. shares, bonds, units in property funds, and other financial instruments). This reduces the risk to the Scheme and members of investing in any specific individual asset. The use of passive funds also removes some of the risk involved in a purely active investment strategy.

The use of separate investment managers, in particular within the Diversified Growth element, reduces the manager risk faced by the Scheme on its active mandates. The Group Trustees will keep the asset allocation under review, and risk measurement forms part of the performance monitoring process.

6. Implementation of the investment arrangements

Before investing in any manner, we obtain and consider proper written advice from our investment adviser as to whether the investment is satisfactory, having regard to the need for suitable and appropriately diversified investments.

We have signed agreements with the investment managers setting out the terms on which the portfolios are to be managed.

We have limited influence over managers' investment practices because all the Scheme's assets are held in pooled funds, but we encourage our managers to improve their practices within the parameters of the fund they are managing.

Our view is that the fees paid to the investment managers, and the possibility of their mandate being terminated, ensure they are incentivised to provide a high quality service that meets the stated objectives, guidelines, and restrictions of their fund. However, in practice managers cannot fully align their strategy and decisions to the (potentially conflicting) policies of all their pooled fund investors in relation to strategy, long-term performance of debt/equity issuers, engagement, and portfolio turnover.

It is our responsibility to ensure that the managers' investment approaches are consistent with our policies before any new appointment, and to monitor and to consider terminating any arrangements that appear to be investing contrary to those policies. We expect investment managers to make decisions based on assessments of the longer term performance of debt/equity issuers, and to engage with issuers to improve their performance (or where this is not appropriate to explain why). We assess this when selecting and monitoring managers.

We evaluate investment manager performance over both shorter and longer term periods as available. Except in closed-ended funds where the duration of the investment is determined by the fund's terms, the duration of a manager's appointment will depend on strategic considerations and the outlook for future performance. If a manager is not meeting its performance objectives, we will consider alternative arrangements.

Our policy is to evaluate each of our investment managers by considering performance, the role it plays in helping to meet our overall long-term objectives, taking account of risk, the need for diversification and liquidity. Each manager's remuneration, and the value for money it provides, is assessed in light of these considerations.

We recognise that portfolio turnover and associated transaction costs are a necessary part of investment management. Since the impact of these costs is reflected in performance figures used in our assessment of the investment managers, we do not explicitly monitor portfolio turnover. We expect our investment consultant to incorporate portfolio turnover and resulting transaction costs as appropriate in its advice on the Scheme's investment mandates.

7. Realisation of Investments

The Group Trustees' policy is to ensure that the assets invested are sufficiently realisable to enable the Group Trustees to meet their obligation to provide benefits as they fall due. The Group Trustees are satisfied that the arrangements in place conform to this policy. The Group Trustees monitor their net cashflow position, the likely need to realise capital, and hence any effect on asset allocation and the choice of investment funds.

8. Additional Voluntary Contributions

The Scheme has available facilities for members who wish to contribute to enhance their retirement benefits. The Group Trustees believe these to be appropriate facilities for this purpose, but they note that the decisions on the level of contributions paid and the funds used rest entirely with the members.

9. Environmental, Social and Governance (ESG) Considerations including Voting and Engagement

In endeavouring to invest in the best financial interests of the beneficiaries, the Group Trustees have elected to invest in pooled funds and cannot therefore directly influence the environmental, social, and governance policies and practices of the companies in which the pooled funds invest.

Given the objectives of the Scheme, the Group Trustees exclude non-financial matters (ie matters relating to the ethical and other views of members and beneficiaries, rather than considerations of financial risk and return) in the selection, retention and realisation of investments.

The Group Trustees have delegated to their investment managers the exercise of rights attaching to investments, including voting rights, and engagement with relevant persons such as issuers of debt and equity, stakeholders and other investors about relevant matters such as performance, strategy, capital structure, management of actual or potential conflicts of interest, risks and ESG factors. The investment managers will from time to time report on their current and future actions in these areas.

We do not monitor or engage directly with issuers or other holders of debt or equity, but we do engage with current and prospective investment managers on matters including ESG and stewardship. We expect the investment managers to exercise ownership rights and undertake monitoring and engagement in line with their policies on stewardship, considering the long-term financial interests of the beneficiaries

The Group Trustees will consider a manager's ESG credentials during their selection, retention, and realisation of investments, given the time horizon of the Scheme and its members.

The Group Trustees have invested the Scheme's equity portfolio in a "low carbon transition" fund, which has been designed to reduce exposure to the financial risks arising from climate change.

10. Compliance

Performance monitoring, manager remuneration and duration of manager appointments are covered elsewhere in this Statement, or in the Group Trustees' Annual Report.

The Group Trustees publish their SIP online for general public access.

The Group Trustees will publish annually online an Implementation Statement that outlines how the various requirements (set out above) have been followed during the year, and describes the voting behaviours of the asset managers on their behalf.

The Group Trustees will formally review this statement as and when required, without delay after any significant change in investment policy and/or regulatory requirement and at least every three years, with the assistance of their advisers. A copy of this statement is available for inspection by Scheme members.

This statement has been agreed by the Group Trustees on 22 December 2021.

Appendix

This table provides background to the table used in section 3 of the SIP.

This appendix may be revised from time to time without triggering the need for a wholesale review of the SIP.

Manager targets

Asset Class	Manager	Actively Managed Fund Target
Diversified growth	L&G	Outperform Base Rate by 4.5% per annum
	Ruffer	Outperform twice the bank base rate
Forestry	Bidwells	To generate income and capital growth by investing in UK commercial forestry and renewables.
Long lease property	L&G	To provide an income stream that rises annually in line with LPI (RPI between 0% and 5%).
High Yield bonds	L&G	Outperform the ICE BofA Global High Yield BB-B Rated (excluding financials) 2% constrained Currency Hedged Index by 1% p.a. (before fees) over a rolling three-year period.
Corporate bonds	L&G	To achieve growth of capital within a globally diversified portfolio of predominantly investment grade credit and to preserve value by avoiding defaults and securities experiencing significant deterioration in credit quality.

Manager weightings

A more detailed version of the table used in section 3 of the SIP is as follows:

Asset Class	Weight (%)
Low Carbon Global Equity – L&G	10.0
Diversified growth	16.0
L&G	***8.0***
Ruffer	***8.0***
Forestry – Bidwells	6.0
Long lease property – L&G	5.0
High Yield – L&G	8.0
Corporate bonds – L&G	13.0
LDI and cash – L&G	42.0
Total	**100.0**

Internal rebalancing

Legal & General are not currently applying rebalancing on behalf of the Group Trustees.

In the Global Equity portfolio, a 60/40 distribution between UK and overseas assets has been targeted at the outset of the investment.

The Global Equity portfolio may be held on a Currency hedged or unhedged basis, and can move between these without triggering a full review of the SIP.

The L&G absolute return fund can switch between Diversified and Dynamic Diversified without triggering a full review of the SIP.

Legal & General provide the LDI funds used within the Group Trustees' LDI portfolio.