The Co-operative Pension Scheme (Pace) – Co-op Section ("the Section")

Statement of Investment Principles – January 2024

1. Introduction

Pace Trustees Limited ("the Trustee") has drawn up this Statement of Investment Principles (the "Statement") to comply with the requirements of the Pensions Act 1995 ("the Act") and subsequent legislation. The Statement seeks to take into account the principles underlying the (Myners) Code of Best Practice for pension scheme investment, which has been endorsed by the Government and the Pensions and Lifetime Savings Association. The Statement also seeks to take into account the Investment Governance Group ("IGG") principles for defined benefit and defined contribution schemes.

Since August 2018, the Co-operative Pension Scheme (Pace)'s assets and liabilities have been sub-divided into two sections, relating to the Co-operative Group Limited ("the Co-op") and the Co-operative Bank ("the Bank") respectively. Investment policy is determined separately for each section.

The remainder of this Statement refers primarily to the section of Pace of which the sponsoring employer is the Co-op, namely the Co-op Section ("the Section"). The Co-op has been consulted in preparing this Statement and will be further consulted regarding any proposed changes to the Statement. However, the ultimate power and responsibility for deciding investment policy lies solely with the Trustee.

The Statement is intended to affirm the investment principles that govern decisions about the Section's investments.

The Section provides two types of benefit; a defined contribution section (the "Defined Contribution" section) and a defined benefit arrangement (the "Defined Benefit" section). These are covered separately in Sections 2 and 3 respectively. The Defined Benefit section is closed to new entrants.

The investment responsibilities of the Trustee are governed by the Scheme Rules (which are available on the Pace website) and relevant legislation.

2 Defined Contribution section

2.1 Process for Choosing Investments

The process for choosing investments is as follows:

- Identify appropriate investment objectives
- Consider the risks faced by members of the Defined Contribution section
- Identify a range of investment options for members suitable to cover the range of likely investment objectives and risk tolerances over a member's working life and, where appropriate, ethical or religious beliefs members may hold.

The Trustee also considers any other factors which it believes to be financially material including environmental, social and corporate governance factors, particularly when setting the default strategy for the Defined Contribution section.

In considering the appropriate investments for the Defined Contribution section the Trustee has obtained and considered the written advice of the Investment Adviser, whom the Trustee believes to be suitably qualified to provide such advice.

2.2 Investment Objective

The Trustee's objective is to make available to members a programme of investment, via pooled funds, which seeks to generate income and capital growth and which, together with new contributions from members, the Co-op and Participating Employers, will provide a fund at retirement with which to provide an income in retirement.

The Trustee recognises that members have differing investment needs and that these may change during the course of members' working lives. The Trustee also recognises that members have differing attitudes to risk and retirement objectives. The Trustee believes that members should be provided with a range of options to tailor their pension investments to their individual circumstances.

The default arrangement aims to grow member contributions ahead of inflation over the members working life, reducing absolute fund volatility as the member approaches retirement. It is designed to be appropriate for members who want to take all of their account as a lump sum on retirement. During the early years, it will be invested in the "Pace - Build Your Pot" Fund with the objective of achieving growth over the long term. As members approach their selected retirement age, the default arrangement automatically switches holdings fully into the "Pace – Consolidate Your Pot" Fund, and over the 10 years prior to a member's selected retirement date switches into the "Pace – Take Your Pot – As Cash" Fund to provide capital protection.

2.3 Risk Management and Measurement

The Trustee recognises specific investment risks which can be managed by the range of investment options provided to members. These are:

- **Shortfall or 'opportunity cost' risk** - the risk that members end up with insufficient funds at retirement with which to secure a reasonable income.
- **Capital risk** - the risk of a fall in the value of the members' funds.
- **Custody risk** - the safe custody of the defined contribution assets is delegated to professional custodians appointed by the Fund provider.
- **Purchasing power risk** - the purchasing power risk to members is that the investment return over members' working lives does not keep pace with inflation and does not therefore secure an adequate retirement income. This risk is mitigated through the design of the Target Funds, which aim to provide sufficient investment returns over a member's working life. In addition, the Trustee has made available three Growth Funds, should members wish to select their own investment options.
- **Conversion risk** - the risk that relative market movements in the years just prior to retirement lead to substantial reduction in the retirement income and cash lump sum secured. This risk is mitigated through the design of the three Target Funds, which aim to protect members from relative market movements in the years just prior to retirement. In addition, the Trustee has made available two Pre-retirement Funds and a Cash Fund, should members wish to select their own investment options.
- **Manager risk** - the risk that the chosen investment manager underperforms the benchmark against which the investment manager is assessed. This risk is mitigated through the regular review of investment performance by the Trustee.
- **Lack of diversification risk** – the Trustee recognises the risks that may arise from a lack of diversification within the investments. The Trustee therefore invests in pooled fund vehicles, to ensure an adequately diversified portfolio for each fund option.

In formulating the investment options to make available to members the Trustee has considered the willingness and ability of Pace's defined contribution membership to take investment risk. As part of this, the Trustee considered the capacity of members to respond to an adverse event.

The funds offered through the Defined Contribution section of Pace have been chosen, in part, to help members mitigate these risks.

2.4 Investment Strategy

The Defined Contribution section of Pace offers three lifestyle strategies plus a range of self-select funds to members with growth or protection objectives.

The lifestyle strategies have been designed to target the three retirement objectives; lump sum, secure income and flexible income. All of the lifestyles invest in equities, bonds and alternative growth assets during the 'growth phase'. The lump sum lifestyle strategy is designed for members targeting a lump sum at retirement and has a high exposure to cash at retirement. The flexible income targeting lifestyle de-risks to a much smaller allocation to cash and the secure income targeting lifestyle de-risks into bonds and cash, as members approach retirement.

The lump sum lifestyle strategy acts as the "default" investment option for those members who do not wish to select their own funds.

The Trustee believes that the investment strategy options are currently appropriate for meeting the Pace objective set out in 2.2 and controlling the risks identified in 2.3 for the membership as a whole.

The default investment strategy includes an allocation to a multi-asset fund, via the Pace Growth (Mixed) Fund, that may include an allocation to illiquid assets if the fund manager chooses to do so. As at 30 June 2023, there was an allocation to alternative assets (including Real Estate, Infrastructure and Private Equity) within the fund. These alternative investments are currently accessed via REITS (Real Estate Investment Trusts) and Investment Trusts which are liquid investments and do not impact the liquidity profile of the fund.

We believe that long-term net risk-adjusted investment returns may be improved by investing in illiquid assets. However, illiquid assets in DC pension schemes is a relatively new and developing area and the most efficient way to access this is through a multi-asset structure. Therefore, at this time, it is our policy not to invest the DC default in standalone funds of illiquid assets. However, with the support of our investment advisers, we intend to consider investment in illiquid assets when we next review the default strategy.

2.5 Expected Return

The funds available are expected to provide an investment return relative to the level of risk associated with it. The Trustee believes that the range of funds offered should provide a range of returns suitable for the membership as a whole.

3. Defined Benefit section

3.1 Process for Choosing Investments

The process for choosing investments is as follows:

- Identify appropriate investment objectives, covering both risk tolerance and target return
- Construct a portfolio of investments that is expected to meet the investment objectives

The Trustee is committed to achieving these investment objectives in a way that takes into account broader environmental, social and corporate governance concerns where possible. Investing responsibly is an important consideration for the Trustee and is covered in more detail in Section 8.

In 2020, the Trustee entered into bulk annuity policies with Aviva Life & Pensions UK Limited ("Aviva") and Pension Insurance Corporation ("PIC") in respect of a portion of the Defined Benefit section's pensioner liabilities. In

November 2023, the Trustee entered into an additional bulk annuity policy with Rothesay Life in respect of the vast majority of the remainder of the Defined Benefit section's pensioner and deferred liabilities. These bulk annuity policies will provide all benefits due from the Section to members. The only remaining defined benefit assets consist of cash held by the Section to meet future expenses and some small residual liabilities.

In considering the appropriate investments for the Section, the Trustee has obtained and considered the written advice of the Investment Adviser, whom the Trustee believes to be suitably qualified to provide such advice. Where matters described in this Statement may affect the Section's funding policy, input has also been obtained from the Scheme Actuary. The advice received, and arrangements implemented are, in the Trustee's opinion, consistent with the requirements of Section 36 of the Pensions Act 1995 (as amended).

3.2 Investment Objectives

The Trustee has a duty to invest the defined benefit assets of the Section in a manner which, over the life of the Defined Benefit section, should enable the Trustee to provide the promised benefits under the rules.

The Trustee considers that its broad objective is to invest the Section's assets in such a manner that members' entitlements can be paid when they fall due. As a key step to achieving this, the Trustee, following consultation with the Co-op, has entered into three bulk annuity contracts issued by Aviva, PIC and Rothesay Life respectively. Aviva, PIC and Rothesay are authorised by the Prudential Regulation Authority to write contracts of long term life insurance of this nature in the UK.

The Trustee would ultimately like to insure or discharge any insured liabilities and progress towards an insurer buy-out of the Section's known liabilities, with the aim of achieving an appropriate discharge of liability in respect of known obligations in accordance with the Section's governing documentation and relevant legislation.

In due course, in order to complete the buy-out transaction, the known members' benefits would be secured by means of individual annuity policies issued by Aviva, PIC and Rothesay Life directly to the members, in accordance with the terms of the bulk annuity policies. The Section could then be wound up.

The Section's principal assets are the bulk annuity policies held with Aviva, PIC and Rothesay Life. As a result, all of the Section's assets are represented by these policies with the exception of residual assets held in the Trustees' bank account and in pooled cash funds.

3.3 Risk Management and Measurement

The Trustee recognises a number of risks involved in the investment of the defined benefit assets of the Section. Following the decision to purchase bulk annuity insurance policies covering the Section's liabilities, the Trustee has identified the following risks:

- **Counterparty credit risk** – investment in a bulk annuity policy represents a concentrated risk of the annuity provider(s) not making the required payments. The policies in place are governed by insurance market solvency requirements and the protections provided by the Financial Services Compensation Scheme, and the Trustee has further mitigated this risk through careful choice of insurance providers and negotiation of contract terms.

- **Liquidity risk** – while the buy-in policies held by the Section can only be liquidated by the Trustee in specific and limited pre-defined circumstances, they are designed to match the liquidity requirements of the relevant liabilities as exactly as possible, and so the requirement to hold liquid assets to meet these liabilities as they are due falls away.

  The residual assets invested in cash funds are daily dealing and the underlying instruments are liquid in nature.

- **Longevity risk** – the impact of potential increases in life expectancy of the Section's pensioners was mitigated with the purchase of the buy-in annuity policies held with Aviva, PIC and Rothesay Life.

- **Environmental, social and governance risk (including climate change)** – the Trustee recognises that environmental, social and corporate governance concerns, including climate change, can have a financially material impact on the Section. With the purchase of insurance policies, the Trustee's responsibility for the management of these risks is limited and passed on to PIC, Aviva and Rothesay Life (and the insurers' management of these risks was considered as part of their selection).

- Residual assets of the Defined Benefit Section are held as cash in a liquid pooled fund. Given the size and nature of these investments the Trustee also believes it has minimal direct exposure to risks arising from long-term sustainability issues, including climate change as a result of these investments. To the extent that the residual assets are exposed to ESG risks, this is addressed through the use of BlackRock's Liquidity Environmentally Aware Fund ('LEAF')

3.4 Investment Strategy and Expected Return

The nature of the buy-in policies is such that their expected return is equal to the change in value of the member benefits covered. Due to the buy-in policies, the Section's investment strategy does not have a return target and instead the target is to maintain liquidity and security to support any future buy-out of the Section's liabilities.

The residual assets are invested in a way that is designed to preserve the capital value, through pooled cash funds and the Trustee Bank Account. They are expected to return in line with SONIA interest rates.

4. Day–to-Day Management of the Assets

The Trustee has appointed Aviva, PIC and Rothesay Life as its annuity providers having obtained and considered written advice from its advisors, who the Trustee consider to be suitably qualified to provide such advice.

In this context, relevant investment advice relates to that provided in accordance with the requirements of Section 36 of the Pensions Act 1995 (as amended).

The Trustee will also hold cash within the Trustee Bank Account and pooled cash funds for ongoing expenses.

For the Defined Contribution section, the Trustee has selected a number of suitable pooled funds for members to invest in.

5. Investment Manager Appointment, Engagement and Monitoring

Defined Contribution section

Investment managers are appointed based on their capabilities and, therefore, the perceived likelihood of achieving the stated expected return and risk characteristics required for the asset class they are selected to manage.

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

The Trustee receives, and considers, performance reports produced on a quarterly basis, which present performance information and commentary on the funds they invest in over various time periods. The Trustee reviews the absolute performance and where relevant, will also consider relative performance against a suitable index used as the benchmark and/or against the manager’s stated target performance (over the relevant time period) on a net of fees basis. In terms of reporting, the Trustee’s focus is primarily on long term performance, but short-term performance is also reviewed.

The Trustee may review a manager’s appointment if:

- There are sustained periods of underperformance;
- There is a change in the underlying objectives of the investment manager, or a change in the portfolio manager;
- There is a significant change to the Investment Adviser’s rating of the manager; or
- There is a change to the Trustee’s overall strategy that no longer requires exposure to that asset class or manager.

The investment managers are remunerated by way of a fee calculated as a percentage of assets under management.

The investment managers are aware that their continued appointment is based on their success in delivering the mandate for which they have been appointed. If the Trustee is dissatisfied, then it may look to replace the manager or in some circumstances ask the manager to review the Annual Management Charge.

Investment manager performance is generally reported net of transaction costs (where possible), and therefore managers are incentivised in this way to keep portfolio turnover costs to the minimum required to meet or exceed their objectives.

Transaction costs are collated and reported annually through the Trustee Report and Accounts.

The Trustee will continue to monitor industry improvements concerning the monitoring and reporting of portfolio turnover costs.

The Trustee is a long-term investor and is not looking to change the investment arrangements on a frequent basis. There is therefore no set duration for manager appointments. The Trustee typically expects to retain an investment manager unless:

- There is a change to the overall investment strategy that no longer requires exposure to that asset class or manager.

- The manager appointed has been reviewed and the Trustee has decided to terminate the mandate.

Defined Benefit section

For the buy-in policies, the Trustee invests in annuity contracts that match the liabilities of the Section.

The annuity contracts held with Aviva, PIC and Rothesay Life will be monitored to ensure that they continue to deliver what is expected under the contract, which is to provide cashflows aligned with the benefits due to the members covered by the policy.

The Trustee has appointed the insurers providing the annuity contracts with the expectation of a long-term partnership with both the Trustee and eventually the member, following the potential novation of the annuity contracts into the name of the member at the point of winding up the Section. As annuity contracts cannot be traded on the open market, and by definition will perform as expected, the Trustee would not expect to review the insurers' appointments.

Since the Section is invested solely through the purchase of the bulk annuity policies held with Aviva, PIC and Rothesay Life, the Trustees are unable to incentivise the insurer, remunerate or monitor portfolio turnover costs as these are not applicable to a bulk annuity.

The Trustee paid premiums to Aviva and PIC in 2020 and to Rothesay Life in 2023 when it entered into buy-in policies with the three insurers. There are no ongoing fees in respect of the policies.

For the residual assets, the Fund invests in BlackRock's pooled cash fund ('LEAF'). The Trustee has taken steps to satisfy themselves that BlackRock have the appropriate knowledge and expertise for managing the Defined Benefit section's cash investments.

6. Realisation of Investments

The Defined Benefit section's principal assets are the bulk annuity policies with Aviva, PIC and Rothesay Life. As a result, all of the Defined Benefit section's assets are represented by these policies, with the exception of residual cash held in the Trustees' bank account or in pooled cash funds.

The residual cash is to be held in order to help the Trustees meet imminent cash outgo in connection with ongoing expenses arising that are to be met from the Section. Assets underlying BlackRock LEAF are considered to be predominantly traded on regulated markets. BlackRock LEAF trades daily.

Future benefits payable from the Section prior to any future buy-out will be funded by the bulk annuity policies.

For the Defined Contribution section, the investment managers have discretion in the timing of realisation of investments and in considerations relating to the liquidity of those investments, within parameters stipulated in the relevant appointment documentation.

7. Additional Assets

The Trustee is responsible for the investment of Additional Voluntary Contributions ("AVCs") paid by members and various immediate annuity contracts. The Trustee reviews the investment performance of the chosen AVC providers on a regular basis and takes advice as to the providers' continued suitability.

8. Socially Responsible Investment and Corporate Governance

The Trustee has a Responsible Investment ("RI") Policy which it reviews at least annually. This document details the policy for considering Environmental, Social and Governance ("ESG") factors, including climate change, in the strategic investment process and investment decision-making process, assessing Pace's investment managers' performance on ESG issues, engagement with investee companies, consideration of and participation in third party ESG initiatives and public disclosure of Pace's ESG policy in practice.

Given the bulk annuity policies purchased for the Defined Benefit section in 2020 and 2023, the Trustee's expectation is that the scope for meaningful implementation of these policies is very limited, although ESG factors including the investment policies in relation to climate risk of the insurers were considered as part of their selection. The remainder of section 8 applies to the Defined Contribution section.

Defined Contribution section

In accordance with its fiduciary responsibilities, the Trustee takes account of financially material factors when making investment decisions, i.e. those factors which are expected to have an impact on investment returns and risk over the Section's anticipated lifetime (including the long-term sustainability of investee companies' performance – in particular the impact of climate change).

The Trustee also recognises that it may take non-financial factors into consideration (i.e. those motivated by other concerns, such as social impact) where the Trustee has good reason to expect that Scheme members would share these concerns, and where the decision is not expected to have material financial detriment.

The Trustee will apply these considerations in setting Pace's RI Policy, with the Trustee assessing members' likely concerns (as far as this is practically possible) through engagement with members and through engagement with the Co-op when developing the Policy.

At the time of writing, the RI policy reflects three broad RI issues which the Trustee believes represent particular risk to the Scheme and which the Trustee believes can be addressed. As the Policy is kept under regular review, the issues identified may change over time. These issues are:

- Protection of the environment (including climate change, and deforestation)
- Labour conditions and equal pay.
- Corporate governance.

The Trustee seeks to address these issues through Pace's engagement with its investment managers and the selection of the funds available through Pace DC.

The Trustee gives its investment managers full discretion to evaluate ESG factors and engage with companies. The Trustee also encourages its investment managers to adopt best practices in these areas and to act in the best interests of Pace members. The Trustee recognises that where investments are held in pooled funds, it may not be possible to instruct the manager to follow a separate voting policy or to exercise votes. The Trustee may, from time to time, raise specific ESG issues with investment managers and seek a response.

As part of the appointment of new investment managers and its ongoing monitoring process, the Trustee will consider the Investment Adviser's assessment (in terms of the Investment Adviser's own system of ESG ratings) of how each investment manager embeds ESG and stewardship factors into its investment process and how the manager's responsible investment philosophy aligns with Pace's Responsible Investment policy. This includes the investment managers' policy on voting and engagement.

In addition, the Trustee carries out regular reviews of the managers' ESG policies and actively engages with managers to better understand their processes.

The Trustee offers funds with ESG tilts in the Pace Growth (Mixed) Fund and the Pace Growth (Shares) 2021 Fund (both of which form part of the default strategy). The Trustee also considers ESG factors as part of the Scheme's process for selecting and retaining investment options. In addition, the Trustee recognises that some members may wish to take more explicit account of ethical issues or their personal religious beliefs in their investments, and so it offers an ethical equity fund, the Pace Growth (Ethical Shares) Fund, and an Islamic equity fund, the Pace Growth (Shariah) Fund.

As a responsible investor, the Trustee exercises rights, including any voting rights attaching to Pace's investments, in the best interests of Pace's members. Specifically, the Trustee has instructed the investment managers to exercise voting rights accordingly, where applicable and wherever it is practicable to do so, and to report to the Trustee.

9. Professional Investment Advice

The Trustee has appointed Lane Clark & Peacock LLP to provide advice in relation to the principles and fund choice set out in this document relating to the Defined Contribution section. The Trustee has appointed Mercer Limited to provide advice on all aspects of investment relating to the Defined Benefit section of the Section (with the exception of investment related advice on the suitability of the buy-in policies, which was provided by a 3rd party professional adviser).

10. Review of this Statement

The Trustee will review this Statement annually and without delay after any significant change in investment policy or demographic profile of the membership. The Investment Advisers will provide the advice needed to allow the Trustee to review and update this Statement as required. In addition, no change will be made to the Statement unless the proposed changes to investment policy have been approved by the Trustee and recorded in the minutes of a Trustee meeting.

Approved by Pace Trustees Limited on 15 January 2024

Appendix: Division of Duties and Responsibilities

Duties and Responsibilities	Executed By
▪ Overall responsibility for the Section's investments. ▪ Appoint and monitor the Investment Adviser. ▪ Review of the Responsible Investment Policy. ▪ Define the terms of appointment of the Defined Contribution Committee. ▪ Appoint the members of Defined Contribution Committee.	The Trustee
▪ Make day-to-day decisions relevant to the operation of the Defined Contribution section's investment strategy.	The Defined Contribution Committee
▪ Monitor appointed Investment Managers and other service providers	The Trustee and Defined Contribution Committee
▪ Perform asset liability modelling exercises, as required. ▪ Advise on the strategic framework. ▪ Advise on the selection of the Investment Managers. ▪ Monitor the Investment Managers, providing both qualitative and quantitative input to the Trustee and Manager Monitoring and Implementation Committee as appropriate. ▪ Advise on the implementation of mandates. ▪ Advise on the Statement of Investment Principles.	The respective Investment Advisers to the Section (both defined contribution and defined benefit)
▪ Operate within the conditions set down by the Investment Management Agreement (or equivalent documentation) ▪ Select individual investments with regard to their suitability and diversification. ▪ Supply the Trustee with sufficient information to allow the review of activity.	The Investment Managers and insurance providers