Statement of Investment Principles

Yorkshire Building Society Pension Scheme (November 2024)

Introduction

1 This document is the Statement of Investment Principles (the "SIP") made by the Trustee of the Yorkshire Building Society Pension Scheme (the "Scheme") in accordance with the requirements of Section 35 of the Pensions Act 1995 (as amended by the Pensions Act 2004 and regulations made under it).

2 The Trustee will review this SIP at least every three years and without delay after any significant change in investment policy. Before finalising this SIP, the Trustee took written advice from the Scheme's Investment Consultant (Towers Watson Limited) and consulted the Principal Employer, Yorkshire Building Society (the "Society"). The ultimate power and responsibility for deciding investment policy, however, lies solely with the Trustee.

3 The Scheme operates for the exclusive purpose of providing retirement and death benefits to eligible participants and beneficiaries. The Scheme provides both a Defined Benefit ("DB") and Defined Contribution ("DC") pension arrangement. These two arrangements are considered both separately and together in different areas of this Statement.

Scheme objectives – DB Section objectives

4 The Trustee's policy is to seek to achieve the objectives through investing in a suitable mixture of real and monetary assets. It recognises that the returns on return seeking assets, while expected to be greater over the long term than those on liability matching assets, are likely to be more volatile. A mixture across asset classes should nevertheless provide the level of returns required by the DB Section of the Scheme to meet its liabilities at an acceptable level of risk for the Trustee and an acceptable level of cost to the Society.

5 A full triennial valuation of the Scheme was carried out as at 31 December 2022, using asset return assumptions developed by the Scheme Actuary, and considering many diversified asset classes for possible investment. The Trustee reconsidered the asset allocation of the Scheme in light of this valuation, and will continue to do so at other times where it is deemed necessary.

6 The principal duty of the Trustee is to act in the best interests of the members of the Scheme. In light of this duty, the Trustee's objectives for the DB Section are:

a. To achieve a return on the Scheme's assets that is consistent with the long-term assumptions of the Scheme Actuary in determining the funding of the Scheme, whilst also balancing risk.

b. To aim for the assets to exceed the liabilities as determined in the event of the Scheme winding up on the basis of cash equivalent transfer values.

c. To minimise the requirement for the Society to make further deficit recovery plan contributions.

Investment strategy – DB Section

7 The Trustee's investment strategy (excluding the buy-in) seeks to generate returns between 0.90% pa and 1.20% pa above liability growth (measured on a gilts basis) in the long term (i.e. gilts + 0.90%-1.20% pa).

8 The investment strategy makes use of three key types of investments:

- a range of instruments that provide a better match both to changes in liability values and expected liability cashflows, including (but not limited to) gilts, corporate bonds and derivatives.
- a diversified range of return-seeking assets, including (but not limited to) equities (implemented physically and/or through equity futures), corporate bonds, and secure income assets.
- passively and actively managed portfolios as appropriate, following consideration of efficiency, liquidity and level of transaction costs likely to prevail within each market as well as the impact of the investment managers' fees on future expected returns.

9 The balance within and between these investments will be determined from time to time with regard to maximising the chance of achieving the Scheme's investment objectives.

10 The Scheme will hold assets in cash and other money market instruments from time to time as deemed appropriate.

11 The Scheme holds a legacy reinsurance asset that is in the process of being redeemed.

12 The Trustee will monitor the liability profile of the Scheme and will regularly review, in conjunction with the Investment Consultant and the Scheme Actuary, the appropriateness of its investment strategy.

13 The expected return of an investment will be monitored regularly and will be directly related to the Scheme's investment objectives.

14 A buy-in policy to the value of c.£250.4m has been implemented, as at 19 November 2018, and excluded in the context of the Scheme's investment objective.

15 The Trustee's policy is that there will be sufficient investments in liquid or readily realisable assets to meet cashflow requirements in foreseeable circumstances so that the realisation of assets will not disrupt the Scheme's overall investments, where possible. The Trustee, together with the Scheme's administrators, will hold sufficient cash to meet benefit and other payment obligations.

Risks & Regulations – DB Section

16 The Trustee recognise a number of risks involved in the investment of the Scheme's assets. These risks include but are not limited to:

a. Solvency risk and mismatching risk is a qualitative and quantitative assessment of the expected development of the liabilities relative to the prevailing investment policies. It is managed through assessing the progress of the actual growth of the assets relative to liabilities under the current investment policy.

b. Manager risk is the expected deviation of the prospective risk and return, as set out in the managers' objectives, relative to the investment policy. It is managed through diversification across investment managers and by the ongoing monitoring of the performance of the investment managers as well as a number of qualitative factors supporting the managers' investment process.

c. Liquidity risk is measured by the ability to achieve the level of cash flow required by the Scheme over a specified period. It is managed by regular communication between the Trustee and the Administrator through estimates of the monthly benefit outflow, ensuring sufficient cash balances are available.

d. Political risk is the level of concentration of any one market leading to the risk of an adverse influence on investment values arising from political intervention. It is managed by regular reviews of the actual investments relative to policy and through regular assessment of the levels of diversification within the existing policy.

e. Sponsor risk is the risk that the level of ability and willingness of the Sponsor to support the continuation of the Scheme and to make good any current or future deficit deteriorates. It is managed by assessing the interaction between the Scheme and the Sponsor's business, as measured by a number of factors, including the creditworthiness of the Sponsor and the size of the pension liability relative to a number of metrics reflecting the financial strength of the Sponsor.

f. Credit risk is the risk that the issuer of a bond will default in repayment of principal and/or interest. It is managed by investing in UK Government bonds where the credit risk is significantly lower, and by investment mandates requiring limits around the amount of non-investment grade credit held. Credit risk also applies to the buy-in policy referring to the risk that the insurer could fall insolvent. This is mitigated by industry protections (FSCS) and the due diligence carried out by the Trustee in selecting an appropriate insurer.

g. Currency risk is the level of concentration in the currency of any one country/region leading to an adverse influence on investment values arising from unfavourable currency movements. A proportion of the currency risk is managed by currency hedging programmes operated by the investment managers within their mandates. The Scheme leaves a proportion of the currency exposure unhedged and the level of unhedged exposure is monitored through time. .

h. Market risk is the risk that the investment vehicles in which monies are invested underperform expectations. It is managed by constructing a diverse portfolio of investments across various markets.

i. Operational risk is the risk associated with the safe-keeping of the Scheme's assets and is managed through a custody arrangement with a third party custodian for the segregated assets.

j. Custodian risk is the risk that the creditworthiness of the custodian bank and the ability of the organisation to settle trades on time and provide secure safe-keeping of the Scheme's segregated assets under custody.

k. Derivative risk refers to counterparty risk, basis risk, liability risk, and legal and operational risk. Counterparty risk is managed through collateral management, diversifying exposure across counterparties, and the use of robust ISDA or other relevant documentation. Basis risk is addressed through the investment policy adopted by the Trustee for the backing assets and the investment managers' asset management capabilities. Liability risk is managed by updating the liability hedging benchmark at appropriate regular intervals. Legal and operational risk is managed by the Trustee taking appropriate advice when putting in place legal documents, reviewing legal documents already in place and appointing and monitoring providers capable of carrying out the required operational tasks.

17 The agreements with the investment managers include a number of guidelines which, among other things, are designed to ensure that only suitable investments are held by the DB Section.

Scheme objectives – DC Section

18 The Trustee policy is to seek to provide lifestyle strategies and self-select funds to support individual preferences and their retirement planning. The Trustee recognises that members' needs may have changed following the introduction of pension freedoms in 2015 and the Trustee have considered the range of options available as the market has developed. In addition, they recognise that the returns on equities, while expected to be greater over the long-term than those on bonds, cash and other investment classes are likely to be more volatile. For those members who are willing to accept a greater level of volatility in pursuit of achieving a higher value of their investment account, a limited number of all-equity funds are available.

19 For the DC Section, the objectives are:

a. To offer a suitable range of options, including a default lifestyle strategy, three additional lifestyle strategies and a range of self-select funds.

b. To recognise and limit the risk of a member's account failing to satisfy the member's reasonable expectations over the long term.

c. To optimise the long-term benefits from the Scheme by allowing members to benefit from good long-term growth on their assets whilst having regard to the objectives shown under the previous paragraph.

d. The Trustee monitors the value for money received by members of the DC section from their membership of the Scheme and commission WTW to undertake an annual review and make recommendations for improvements. The Trustee aim to ensure that the members receive good value for money but recognise that this does not necessarily equate to paying lower fees or costs for services.

Investment strategy – DC Section

20 The Trustee invests in a range of index-tracking funds, selected by the members and managed by a range of investment managers, subject to due diligence. They are satisfied that the requirement for diversification can be achieved through the range of funds made available to the members. The following types of funds are available for members to select:

- Global and emerging market equity funds
- Diversified growth fund
- Bond funds
- Cash fund
- Shariah Fund

21 The Trustee believes that, with these funds, the members can minimise the risks identified in Section 32. The Trustee offers members the option to invest in the range of funds entirely at their discretion. If a member does not specify a choice, the default lifestyle strategy will apply.

22 The Trustee reviewed its DC fund range in October 2023 and currently offers the following approaches for members to invest their DC benefits:

a. **Default: the "Flexible Lifestyle" strategy** - this strategy has been made available for those members who wish to have a less active role in managing their investments. Under this approach, members' investments are automatically switched from equities into a broader mix of assets, and part of the members' investments are then switched into bonds and cash as they near normal retirement age. The default option is aimed at members who haven't yet decided how they will take their retirement benefits, or who may wish to retain a greater degree of flexibility in how their savings are invested.

b. **Lump Sum Lifestyle Strategy** – this strategy is targeted at those members specifically aiming to take their benefits from the Scheme as a single cash lump sum, or a small number of lumps sums over a short period of time. It includes a higher weighting to cash investments at a member's normal retirement age.

c. **Annuity Lifestyle Strategy** – this strategy is targeted at those members who intend to use the majority (or all) of their retirement savings to purchase an annuity – that is a guaranteed income for life. It includes a higher weighting to bond investments at a member's normal retirement age.

d. **Drawdown Lifestyle Strategy** - this strategy is targeted at those members wishing to utilise income drawdown in retirement. Under this approach members' benefits are automatically switched from equities to a broader mix of assets including cash as they near normal retirement age.

e. **Self-select** - this strategy has been made available for those members who would like to manage the investment of their account.

23 In addition to the default lifestyle strategy described above, for the purposes of regulation 2A of the Investment Regulations, due to their history and development, the following funds are classified as “default arrangements”:

- International Equity Investment Fund
- Diversified Investment Fund
- Pre-Retirement Fund
- Cash Fund
- Lump Sum Lifestyle Strategy

24 Members are able to make changes to their investment choices at any time and at no fee (although the DC administrator reserves the right to limit the number of free switches allowed).

25 The Trustee has taken into regard the historical rates of return earned on the various classes of asset available for investment of the DC Section’s assets in assessing the choices offered to members.

26 The Trustee believes that the range of funds offers adequate diversification and is appropriate for the DC Section. The Trustee monitors the range of options regularly and at least every 3 years to ensure that the investment options are sufficiently diverse and consistent with the risk profile of DC members.

27 The members' accounts are held in funds are sufficiently liquid to be realised to provide pension benefits on retirement, or earlier on transfer to another pension arrangement.

Risks & Regulations – DC Section

28 The Trustee recognises that, in a defined contribution arrangement, members assume the investment risks. The Trustee further recognises that members are exposed to different types of risk at different stages of their working lifetimes. Investment risks inherent within the DC Section include:

a. Inflation risk is the risk that the investment return over members’ working lives will not keep pace with inflation and does not, therefore, secure an adequate pension. It is managed by providing investment options that are expected to provide a long-term rate of return that exceeds inflation, such as equity funds and diversified growth funds.

b. Conversion risk is the risk that investment market movements in the period immediately prior to retirement lead to a substantial reduction in the anticipated level of pension or cash lump sum benefit. It is managed by providing a range of investment options that allow members sufficient flexibility to meet their varying objectives.

c. Liquidity risk is the risk that members may experience a delay when moving or redeeming their investments. It is managed by investing in liquid assets.

d. Market risk is the risk that the investment vehicles in which monies are invested underperform expectations. It is managed by investing in a range of diversified assets and in different countries/regions.

e. Manager risk is the expected deviation of the prospective risk and return, as set out in the managers’ objectives, relative to the investment policy. It is managed by the ongoing monitoring of the performance of the investment managers.

f. Political risk is the level of concentration of any one market leading to the risk of an adverse influence on investment values arising from political intervention. It is managed by making available investment options which are diversified across many countries.

g. Credit risk is in relation to Fidelity and the third-party fund managers through its holding in unit-linked funds. In the event of default by Fidelity the Scheme is protected by the Financial Services Compensation Scheme (FSCS). In the event of the default of the third-party managers, the Scheme may not be covered by the FSCS and may not be able to recover all assets, however mitigations are in place to minimise this risk.

h. Currency risk is the level of concentration in any one country/region leading to an adverse influence on investment values arising from unfavourable currency movements. The Trustee periodically reviews the appropriateness of the level of currency exposure in the default strategy.

29 The Trustee considers the same regulatory aspects for the DC Section, as for the DB Section.

Investment managers – DB and DC Sections

30 The Trustee has taken advice from the investment consultant to ensure the investment strategy and investments are suitable for the Scheme and will review the suitability of the investments from time to time. In addition, all investment managers are subject to due diligence prior to appointment and subject to any concerns about the investment manager or change to the fund structure.

31 In accordance with the Financial Services and Markets Act 2000, the Trustee will set general investment policy, but will delegate the responsibility for selection of specific investments to appointed investment managers. The investment managers shall provide the skill and expertise necessary to manage the investments of the Scheme competently.

32 The Trustee is not involved in the investment managers' day-to-day method of operation and does not directly seek to influence attainment of their performance targets. The Trustee will maintain processes to ensure that performance is assessed on a regular basis against a measurable objective for each manager, consistent with the achievement of the Scheme's long-term objectives, and an acceptable level of risk.

33 The Trustee has delegated responsibility for the selection, retention and realisation of investments to the investment managers (within certain guidelines and restrictions). The Trustee will review the policies of each of their managers from time to time.

34 When considering its policy in relation to stewardship including engagement and voting, the Trustee expects investment managers to address broad Environmental, Social and Governance (“ESG”) considerations. The Trustee assesses that ESG risks, including a wide range of big picture themes such as climate change, pose a financial risk to the Scheme and that focussing on these issues is ultimately consistent with the Trustee’s fiduciary duties and the financial security of its members. The Trustee incorporates an assessment of how well the investment managers exercise these responsibilities as part of its overall assessment of their performance.

Investment monitoring – DB and DC Sections

35 The Trustee will monitor both Schemes’ investment performance, adherence to respective mandates and review the nature of the investments held periodically. In doing so the Trustee will consider all relevant factors in determining whether this Statement remains appropriate with any updates made on a timely basis, with a full review of this statement at least every three years and after any significant change to the investment policy, or demographic profile of relevant members in the DC Section.

36 While the Trustee is not involved in each investment managers’ day to day operation, they will regularly assess individual manager performance and adherence to their respective mandates. In particular, the Trustee will review the extent to which the return on investments relating to the default arrangement is consistent with the aims and objectives of the Trustee in respect of the default arrangement.

37 Trustee appoints its investment 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 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 due to other factors such as a significant change in business structure or the investment team.

38 The Scheme uses many different managers and mandates to implement its investment policies. The Trustee ensures that, in aggregate, its portfolio is consistent with the policies set out in this Statement, in particular those required under regulation 2(3)(b) of the Occupational Pension Schemes (Investment) Regulations (2005). The Trustee will also ensure that the investment objectives and guidelines of any particular pooled vehicle are consistent with its policies, where relevant to the mandate in question. Where segregated mandates are used, the Trustee will use its discretion, where appropriate, to set explicit guidelines within the Investment Management Agreement to ensure consistency with the Trustee's policies, where relevant to the mandate.

39 To maintain alignment, managers are provided with the most recent version of the Scheme's Statement of Investment Principles on a regular basis and are required to confirm that the management of the assets is consistent with those policies relevant to the mandate in question. For pooled funds, managers are asked to confirm whether they believe there is any misalignment between the objectives and guidelines of the fund(s) they manage on behalf of the Scheme, or the manager's approach to sustainable investment, and the Trustee's policies.

40 Should the Trustee's monitoring process reveal that a manager's portfolio is not aligned with the Trustee's policies, the Trustee will engage with the manager further to encourage alignment. For pooled funds, if a fund's objectives and guidelines, or an investment manager's approach to sustainable investment, do not appear to be sufficiently aligned with the Trustee's policies, the Trustee will engage with the investment manager to ascertain the reasons for this and whether closer alignment can be achieved. This monitoring process includes specific consideration of the sustainable investment/ESG characteristics of the portfolio and managers' engagement activities. If, following engagement, it is the view of the Trustee that the degree of alignment remains unsatisfactory, the manager (or pooled fund) will be terminated and replaced.

Fee structures – DB and DC Sections

41 Managers are paid an ad valorem fee, in line with normal market practice, for a given scope of services which includes consideration of long-term factors and engagement.

42 The Trustee reviews the costs incurred in managing the Scheme's assets regularly, which includes the costs associated with portfolio turnover. In assessing the appropriateness of the portfolio turnover costs at an individual manager level, the Trustee will have regard to the actual portfolio turnover and how this compares with the expected turnover range for that mandate.

Other matters

43 The Scheme is a Registered Pension Scheme for the purposes of the Finance Act 2004.

44 DB assets in respect of members' AVCs are invested with a range of asset managers. No additional contributions can be made into these AVC arrangements.

45 The Scheme also holds annuity policies with Aviva (formerly Commercial Union), with the income supporting pensions in payment.

46 DC assets in respect of members' AVCs are invested in the same way as normal contributions.

Environmental, Social and Governance ("ESG") considerations

47 The Trustee recognises that long-term sustainability issues have a material impact on risk and outcomes, both financial and non-financial, though the Trustee's fundamental mission is to meet its financial obligations and act in the best financial interests of the Scheme and its members.

48 The Trustee believes that ESG factors, including climate change, affect risk and return in the medium to long-term, and as such should be taken into account throughout the investment process when reviewing current and new investment opportunities.

49 The Trustee actively reflects ESG factors in both the DB Section, through investments held in the Scheme's Secure Income Assets, and the DC section, through investing in an Adaptive capped weighted passive equity fund with an ESG overlay as part of the international equity fund which is a component part of the default investment option.

50 To the extent possible, the Trustee will delegate the responsibility to take ESG principles into account to its investment managers, and will periodically review these policies with the assistance of its investment adviser through reporting or direct engagement with its investment managers as appropriate. The managers have produced statements setting out their policy in this regard. The Trustee acknowledges that it acts on behalf of the Scheme's members in relation to ESG principles, and whilst they may not specifically ask for member views, they may re-visit this statement from time-to-time as deemed appropriate.

51 The Trustee holds a set of specific sustainable investment beliefs which are considered alongside the Trustee's investment policies. These beliefs are reviewed periodically.

Exercise of Voting Rights

52 The Trustee has delegated the exercise of voting rights attached to the Scheme's investments to its investment managers on the basis that voting power will be exercised by them with the objective of preserving and enhancing long-term shareholder value. Accordingly, the managers have produced written guidelines of their process and practice in this regard. The managers are encouraged to vote in line with their guidelines in respect of all resolutions at annual and extraordinary general meetings of companies. The Trustee expects managers to report regularly on votes cast and other relevant matters including capital structure of investee companies, actual and potential conflicts, other stakeholders and the ESG impact of underlying holdings.

53 For most of the Scheme's investments, the Trustee expects the investment managers to invest with a medium to long time horizon, and to use their engagement activity to drive improved performance over these periods. The Trustee invests in certain strategies where such engagement is not deemed appropriate, due to the nature of the strategy and/or the investment time horizon underlying decision making. The appropriateness of the Scheme's allocation to such mandates is determined in the context of the Scheme's overall objectives.

54 The Trustee recognises the UK Stewardship Code as best practice and encourage their Investment Managers to comply with the UK Stewardship Code or explain where they do not adhere to this policy. The Code aims to protect and enhance shareholder value by enhancing the quality of engagement between investors and companies by setting out good practice.

Illiquid investments – DC Section (default arrangement)

55 Currently, the default arrangements do not invest directly in illiquid assets. However, illiquids may be held indirectly, through the investments in the Diversified Investments Fund, an underlying fund of the default Lifestyle strategy. Any investment in illiquids in this fund will be at the discretion of LGIM as investment manager, with decisions taken in the context of the fund's overall risk and return objectives. Members in the default Lifestyle strategy will start to invest in the Diversified Investments Fund when they are 25 years from their target retirement age, and will continue to hold a portion of their total investments in this fund through to retirement.

56 The Trustee considers its current investment strategy for the default arrangements to be appropriate to achieve its investment objectives for members. The Trustee will keep this policy under review and, in future, may consider investing in illiquid assets more explicitly if it believes this would improve the risk and return profile and result in better expected retirement outcomes for members.

Signed: I Dhingra

Name: Inderpreet S Dhingra - Chair of YBS Pension Trustees Ltd

Date: 28 November 2024

Authorised for and on behalf of the Trustee of the Yorkshire Building Society Pension Scheme