ASHLAND UK PENSION FUND

STATEMENT OF INVESTMENT PRINCIPLES

1. Introduction

1.1 The Trustees of the Ashland UK Pension Fund (the “Fund”) have 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 is intended to affirm the investment principles that govern decisions about the Fund’s investments.

1.2 In preparing this Statement, the Trustees have obtained written advice from the Fund’s Investment Consultant, Mercer Limited (“Mercer”). Where matters described in this Statement may affect the Fund’s funding policy, input has also been obtained from the Scheme Actuary. The Trustees will obtain similar advice whenever it reviews this Statement.

1.3 The Trustees’ investment powers are set out within the Fund’s governing documentation and relevant legislation. The Trustees note that, according to the law, it has ultimate power and responsibility for the Fund’s investment arrangements.

1.4 The Fund’s Principal Employer; Ashland Specialities UK Limited will be referred to as the “Sponsoring Company” in this Statement. The Trustees will seek to maintain a good working relationship with the Sponsoring Company and will discuss any proposed changes to this Statement with the Sponsoring Company. However, the Trustees’ fiduciary obligations to the Fund’s members will take precedence over the Sponsoring Company’s wishes, should these ever conflict.

2. Fund Governance

2.1 The Trustees have appointed a firm of professional consultants (the “Investment Consultant”) to provide relevant advice to the Trustees. The Trustees also take advice as appropriate from the Scheme Actuary and other professional advisers.

2.2 The Trustees retain responsibility for determining the overall investment strategy, having taken advice from the Investment Consultant, Scheme Actuary and other professional advisers as appropriate.

2.3 The Trustees have taken steps to satisfy themselves that Mercer has the appropriate knowledge and experience to choose and combine the underlying investment managers and ensure that they are fit to manage the Fund’s investments. The Trustees receive monthly and quarterly investment monitoring reports provided by Mercer and regularly review the continuing suitability of the Fund’s investments, including Mercer’s ability to select, appoint, remove and monitor the appointed managers. Mercer is regulated by the Financial Conduct Authority.

2.4 The Scheme Actuary performs a valuation of the Fund at least every three years, in accordance with regulatory requirements. The main purpose of the actuarial valuation is to assess the extent to which the assets cover the accrued liabilities and agree an appropriate funding strategy for the Fund.

3. Investment Objectives

3.1 The Trustees' objective is to invest the Fund's assets in the best interest of its members and beneficiaries. Within this framework the Trustees have agreed a number of objectives to help guide it in its strategic management of the assets and control of the various risks to which the Fund is exposed.

3.2 The Trustees' primary aims are:

- To ensure the Fund's obligations to its beneficiaries can be met;
- To closely align the performance of the Fund's assets and liabilities by hedging approximately 100% of the sensitivity of the Fund's liabilities on a Technical Provisions basis to changes in interest rate and inflation expectations;
- To achieve an asset return above the return from gilts over the long term, whilst recognising the need to balance risk control and return generation;
- To ensure consistency between the Fund's investment strategy and the return assumptions used by the Fund Actuary;
- To pay due regard to the Sponsoring Company's interests in the size and incidence of employer contribution payments.

3.3 The Trustees would expect to review the appropriateness of these objectives at least every three years, following the results of the triennial Actuarial Valuation of the Fund.

4. Risk Management & Measurement

4.1 There are various risks to which any pension fund is exposed. The Trustees recognise that whilst increasing risk increases potential returns over a long period, it also increases the risk of a shortfall in returns relative to that required to cover the Fund's liabilities as well as producing more short-term volatility in the Fund's funding position.

4.2 In addition to targeting an appropriate overall level of investment risk, the Trustees seek to spread risks across a range of different sources, believing that diversification limits the impact of any single risk. The Trustees aim to take on those risks, for which a reward, in the form of excess returns, is expected over time.

4.3 The following risks are recognised and considered by the Trustees:

- **Mismatch risk –** The primary risk upon which the Trustees focus is that arising through a mismatch between the Fund's assets and its liabilities.
- **Sponsor Covenant risk –** the financial capacity and willingness of the Sponsoring Company to support the Fund is a key consideration of the Trustees and is reviewed on a regular basis.

- **Diversification risk -** The Trustees recognise the risks that may arise from the lack of diversification of investments. Subject to managing the risk from a mismatch of assets and liabilities, the Trustees aim to ensure the asset allocation policy in place results in an adequately diversified portfolio. Due to the size of the Fund's assets and recognising the need to diversify, investment exposure is obtained via pooled vehicles.

- **Concentration risk** – The Trustees recognise the risks that may arise from the lack of diversification of investments. The Trustees are also aware of concentration risk which arises for example when a high proportion of the Fund's assets are invested in securities, whether debt or equity, of the same or related issuers. The overall investment arrangements are intended to provide an appropriate spread of assets by type and spread of individual securities within each asset class.

- **Inflation risk** – Due to the long term nature of the Fund there is a significant risk that investments do not keep pace with inflation. The Trustees have sought to invest in a portfolio which is diversified and is expected to outperform inflation over the longer term, for an acceptable level of risk.

- **Liquidity risk –** The Trustees recognise that there is liquidity risk in holding assets that are not readily marketable and realisable. Given their long-term investment horizon, the Trustees believe that a degree of liquidity risk is acceptable, given the potential return. The majority of the Fund's assets are realisable at short notice.

- **Manager risk –** The Trustees recognise the risk reduction benefits of investing across more than one investment manager. By delegating the implementation of the investment strategy to Mercer, the Trustees are able to benefit from manager diversification without unduly increasing the governance burden of the Trustees. Mercer is responsible for appointing (and removing where appropriate) specialist investment managers as well as monitoring those investment managers.

- **Regulatory and political risk** - Across all of the Fund's investments, there is the potential for adverse regulatory or political change. Regulatory risk arises from investing in a market environment where the regulatory regime may change. This may be compounded by political risk in those environments subject to unstable regimes. The Trustees will attempt to invest in a manner which seeks to minimise the impact of any such regulatory or political change should such a change occur.

- **Exchange rate risk –** This risk arises from unhedged investment overseas. The Fund's assets are predominantly invested in sterling denominated funds and where assets are invested overseas, these assets are hedged against exchange rate movements.

- **Counterparty risk** – The underlying assets within the Hedge Management Portfolio are transacted with a range of counterparties, typically AA rated banks. There is a risk that one or more of these counterparties could default on their obligations resulting in a loss to the Fund. This risk is mitigated to some extent by the underlying manager(s) requiring collateral from each counterparty, which is monitored on a daily basis. Where the underlying investment manager(s) uses derivatives/swaps it is the investment manager's responsibility to monitor the counterparty exposure.

- **Environmental, Social and Governance ("ESG") risk -** The Trustees recognise that ESG issues, including climate change, may have a material impact on the global economy and subsequently investment returns. The Trustees consider how ESG, climate change and stewardship are integrated within the investment structure and monitoring is undertaken on a regular basis. Further details regarding the Trustees' policy on ESG, Stewardship and Climate Change is set out in section 9.

4.4 The documents governing each of the underlying investment managers' appointment includes a number of guidelines which, among other things, are designed to ensure that only suitable investments are held by the Fund.

- Arrangements are in place to monitor the Fund's investments to help the Trustees check that nothing has occurred that would bring into question the continuing suitability of the current investments.

- The safe custody of the Fund's assets is delegated to professional custodians (via the use of pooled vehicles).

4.5 Should there be a material change in the Fund's circumstances, the Trustees will review whether and to what extent the investment arrangements should be altered; in particular, whether the current strategy and risk profile remains appropriate.

5. Investment Strategy and Structure

5.1 The Trustees have adopted a Cashflow Driven Financing ("CDF") strategy whereby the assets are invested in such a way that the expected cashflows (or income) generated by the assets broadly match a proportion of the Fund's expected liability cashflow profile, whilst still targeting a return in excess of gilts (noting that the intention is to match as high a proportion as possible, subject to the level of expected return required).

5.2 The Fund's broad target asset allocation is set out in the table below.

Asset Class	**Target Allocation (%)**
Hedge Management	35.5
Non-Hedge Management	64.5
Total	**100.0**

5.3 There is no automatic re-balancing between the Hedge Management Portfolio and the Non-Hedge Management Portfolio and the asset allocation will vary over time as asset performance and market conditions vary.

5.4 The CDF strategy targets a hedge ratio of 100% of interest rates and inflation as measured on the Technical Provisions basis.

5.5 The **Non-Hedge Management Portfolio** comprises of investments in the following funds:

Fund name	**Target asset allocation %**
Mercer Tailored Credit Fund 1	64.50
Schroder Secured Finance Fund	7.75
Insight Secured Finance Fund	7.75
Mercer Multi-Asset Credit Fund	20.0

The allocation to the Tailored Credit Fund contributes to the interest rate hedge.

5.6 **Hedge Management Portfolio:** The objective of the hedge management portfolio is to hedge, in a pragmatic manner, the interest and inflation risk relative to the Technical Provisions liabilities (after allowing for any hedging provided by the non-hedge management portfolio).

The Hedge Management Portfolio comprises investments in a portfolio of liability driven investment funds (LDI funds) investing in fixed interest and index-linked gilts, swaps, cash and any other assets and in such proportions as determined by Mercer in its discretion. Mercer will monitor the ongoing liability hedge ratio and will rebalance assets within the Hedge Management Portfolio as appropriate to maintain the target hedge ratio, subject to reasonable limits around leverage.

A moderate degree of leverage is required for the Hedge Management assets, to fully hedge the interest rate and inflation risks related to the liabilities. Leverage and the management of collateral are closely monitored by Mercer and the Trustees.

6. Expected return

The CDF strategy aims to deliver a return that is consistent with the discount rate used to value the liabilities, allowing for a prudence ‘haircut’ for default and re-investment risk.

7. Re-balancing, cashflows and distributions

7.1 ***Re-balancing:***

There is no pre-defined or automatic rebalancing between the Hedge Management Portfolio and Non-Hedge Management Portfolio, nor between the funds within the Hedge Management Portfolio and Non-Hedge Management Portfolio, other than where required for liability hedge management purposes.

If a recapitalisation event occurs (where the Hedge Management Portfolio requires additional capital in order to manage leverage), Mercer will review the Fund’s overall asset allocation and has discretion to implement any trades / rebalancing deemed to be appropriate. Mercer will seek to notify the Trustees as soon as practicable, ideally prior to implementation of the relevant trades (if this is possible).

7.2 ***Cashflows:*** In the event of cash-flows into, or out of, the Fund, Mercer will invest or disinvest these as soon as reasonably practicable as follows:

- **Investments**: will be invested in the underlying funds at Mercer's discretion.
- **Disinvestments:** will be disinvested from the underlying funds at Mercer's discretion. Disinvestments are expected to be met by redeeming any holdings in the MGI UK Cash Fund and then from other funds as deemed appropriate by Mercer at its discretion.

7.3 ***Distributions:***

Where possible, income or capital distributions from the assets will be paid into the Trustees' bank account in order to meet benefit payments from the Fund.

8. Additional Voluntary Contribution Assets ("AVCs")

8.1 The Fund provides a facility for members to pay AVCs into the Fund to enhance their benefits at retirement. Members are offered some choice of arrangements in which to invest their AVC payments, so as to provide a suitable long term return for members, consistent with members' needs and reasonable expectations.

8.2 AVCs are held with Prudential Portfolio Managers Limited, Scottish Mutual and Royal & Sun Alliance. The Trustees monitor the suitability and performance of these vehicles from time to time.

9. ESG, Stewardship and Climate Change

9.1 The Trustees believe that environmental, social and corporate governance (ESG) factors may have a material impact on investment risk and return outcomes, and that good stewardship can create and preserve value for companies and markets as a whole. The Trustees also recognise that long-term sustainability issues, particularly climate change, present risks and opportunities that increasingly may require explicit consideration.

9.2 The Trustees have delegated day to day management of the assets to Mercer who in turn delegates responsibility for the investment of the assets to a range of underlying investment managers. These investment managers are expected to evaluate ESG factors, including climate change considerations, and exercise voting rights and stewardship obligations attached to the investments, in accordance with their own corporate governance policies and current best practice, including the UK Corporate Governance Code and UK Stewardship Code.

9.3 The Trustees consider how ESG, climate change and stewardship are integrated within Mercer's investment processes and those of the underlying managers, and monitoring is undertaken on a regular basis. Mercer is expected to provide reporting at least annually, on ESG integration progress, stewardship monitoring results, and climate-related metrics where relevant.

9.4 Members' views are not explicitly taken into account in the selection, retention and realisation of investments, but members have a variety of methods by which they can make views known to the Trustees.

10. **Arrangements with the Investment Managers**

10.1 Mercer is responsible for the selection, appointment, removal and monitoring of the underlying investment managers. The underlying investment managers have discretion to buy and sell investments on behalf of the Fund subject to agreed constraints.

10.2 The underlying investment managers are appointed based on their capabilities and, therefore, their perceived likelihood of achieving the expected return and risk characteristics required for the asset class being selected for. The Trustees look to Mercer for their forward looking assessment of a underlying investment manager's ability to outperform over a full market cycle and this is the primary means of incentivising managers. This view is based on Mercer's assessment of the manager's idea generation, portfolio construction, implementation and business management, in relation to the particular investment fund that the Fund invests in.

10.3 The Trustees have taken steps to satisfy themselves that Mercer has the appropriate knowledge and experience to choose and combine the underlying investment managers and ensure that they are fit to manage the Fund's investments consistent with the objectives of the CDF strategy.

10.4 The Trustees regularly review the continuing suitability of the Fund's investments, including Mercer's ability to select, appoint, remove and monitor the appointed managers.

10.5 Mercer is regulated by the Financial Conduct Authority.

Evaluation of the Investment Manager Performance

10.6 The Trustees receive monthly and quarterly reporting from Mercer. The Trustees monitor the effectiveness of the CDF strategy quarterly, by assessing performance against the key objectives, for example, funding level stability, cashflow generation and hedging targets. The Trustees will also review the ongoing suitability of the strategy as part of the annual investment strategy recalibration and in detail in conjunction with the triennial actuarial valuation.

10.7 The Trustees receive investment performance reports on a quarterly basis, which present performance information and commentary of portfolios and underlying investment managers over 3 months, 1 year, 3 years and since inception. The Trustees review the absolute performance and relative performance against an appropriate benchmark (over the relevant time period) on a net of fees basis. The Trustees' focus is on long-term performance.

Duration of the Arrangement with the Investment Manager

10.8 The Trustees are long term investors and are not looking to change the investment arrangements on a frequent basis. As noted above, Mercer is responsible for the selection, appointment, removal and monitoring of the underlying investment managers.

Fee Structures and Turnover costs

10.9 Mercer levies a fee (plus VAT where applicable) based on a percentage of the value of the assets under management which covers the design and annual review of the CDF strategy, and investment management of the assets. Underlying investment manager fees are payable in addition to the Mercer fee. Fees payable to the underlying investment managers will vary according to the following factors:

- The allocation to the Hedge and Non Hedge Management portfolios and allocations within them;
- The appointment and termination of underlying investment managers, as well as the fees negotiated with those managers.

10.10 Details of all costs and expenses are included in the Fund Supplements, the Report & Accounts and within the Fund's annualized, MiFID II compliant Personalised Cost & Charges statement. The Fund's Personalised Cost & Charges statement also includes details of the transaction costs incurred in the Mercer Funds, which is reviewed on an annual basis by the Trustees.

10.11 Mercer Fund performance is reviewed net of portfolio turnover costs, with the review of portfolio turnover of the underlying investment managers delegated to Mercer.

11. Investment Restrictions

11.1 The Trustees have not set any investment restrictions on the appointed investment managers in relation to particular products or activities, but may consider this in future.

12. Compliance with and review of this Statement

12.1 On a regular basis, the Trustees will review this Statement in response to any material changes to any aspects of the Fund, its liabilities, finances and the attitude to risk of the Trustees and the Sponsoring Company, which is judged to have a bearing on the stated Investment Policy.

12.2 This review will occur on an annual basis and will be based on expert investment advice, in consultation with the Sponsoring Company.

C. McGregor

Trustee | Trustee

28th July 2020

The Trustees of the Ashland UK Pension Fund