Statement of Investment Principles for Defined Benefit Section – John Lewis Partnership Pensions Trust
(September 2019)

Introduction

1 This Statement of Investment Principles ('SIP') sets out the principles governing investments for the John Lewis Partnership Trust for Pensions (the 'Trust'), made by or for the Board of the John Lewis Partnership Pensions Trust (the 'Trustee'). This SIP is drafted in accordance with the requirements of Section 35 of the Pensions Act 1995, as amended by the Pensions Act 2004 and regulations made under them; ("the Pensions Acts").

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

3 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 has taken written advice from the Trust's Investment Consultant (Mercer) and has consulted with the employer, the John Lewis Partnership (the 'Partnership').

4 The Trustee is responsible for the Trust's investment strategy and for ensuring that this is recorded in the SIP. The Trustee delegates responsibility for the implementation and monitoring of the investment strategy to its Investment Sub-Committee ("ISC").

5 This document focuses on the high level principles of the Trustee. The details of the asset allocation and the implementation arrangements are matters for the ISC and will vary over time. The ISC will prepare and maintain a separate document, the Investment Policy Implementation Document, which sets out further details. That document does not form a part of the SIP. This document considers matters relating to the Defined Benefit (DB) section of the Scheme only.

Objectives

6 The Trustee aims to invest the assets of the Trust prudently to ensure that the benefits promised to members are provided. The recovery plan is predicated on an investment return of ILG +1.6% for the first 3 years and ILG +2.3% for years 4 to 10. The Trustee will pursue an investment strategy which aims to generate an investment return in excess of ILG +2.3%, with a risk level commensurate with the strength of the covenant. The expected return on our investments (based on the Willis Towers Watson 'hybrid' model) was ILG +2.9% at 31 March 2016. The Trust intends to monitor the funding position regularly, with a view to de-risking further by taking advantage of unanticipated improvements in the funding ratio.

In seeking to achieve the performance objective, the Trustee is mindful of the need to:

– take account of current market conditions when positioning the portfolio at any time

– limit the risk of the assets failing to meet the liabilities over the long-term, noting that asset growth is expected to be made up of investment returns plus future contributions.

Investment Principles

7 The Trustee has taken advice in determining an appropriate investment strategy for the Trust. The Trustee has a desire to diversify its risk exposures and to manage its investments efficiently and has therefore delegated responsibility for implementation of its investment strategy to its Investment Sub-Committee ('ISC').

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

– a diversified range of return-seeking assets, including (but not limited to) equities, corporate bonds, property and hedge funds ("the Return-Seeking Portfolio")

– a range of instruments, including (but not limited to) physical bonds, swaps, repos and total return swaps, that provide a better match to changes in liability values ("the Liability Matching Portfolio")

As well as these investment assets, the Trust has the following additional sources of security over the liabilities:

– It holds an interest in a Pensions Deficit Mitigation Structure (the "Scottish Limited Partnership"), whose purpose is to provide an income and additional security to the Trust. The Trust's interest in these payments is backed by real estate assets of the Partnership and is subject to annual valuation by the Investment Consultant.

– The Trustee has a formal legal guarantee provided by John Lewis Properties plc, a subsidiary of the principal employer. This gives the Trustee a right to claim against that company in the event of the principal employer failing to pay any amount due. The assets of that company consist of real estate with a market value of at least £800m.

9 The Trustee will monitor the risk profile of the Trust and will regularly review, in conjunction with the Investment Consultant and the Scheme Actuary, the appropriateness of its investment strategy. Consequently, the balance within and between the Return-Seeking and Liability Matching portfolios will be determined from time to time with regard to maximising the probability of achieving the Trust's investment objective while minimising the risk of the asset portfolio relative to the Trust's liabilities. The overall level of risk will be consistent with the strength of the covenant which is regularly monitored as set out in section 24 under "Sponsor and solvency risk".

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

11 The Trustee's policy is that, where possible, there will be sufficient investments in liquid or readily realisable assets to meet cash-flow requirements in foreseeable circumstances so that the realisation of assets will not disrupt the Trust's overall investments. The Trustee will hold sufficient cash to meet benefit and other payment obligations due in the short-term.

12 The Trustee does not intentionally invest in Employer Related Investments (ERI), as set out in the Pensions Act 2004 and in the Occupational Pension Trusts (Investment) Regulations 2005. There may be rare occasions when the Trust is involved in indirect ERI; for example, where the Sponsor is the tenant in a property owned by the Trust. All such transactions are carried out by the Trust's property manager on the basis of an open market transaction, with the Sponsor treated in the same commercial way as any other tenant. The Trustee monitors the level of ERI exposure quarterly.

Current Investment Strategy

13 The Trustee formally reviewed the investment strategy in March 2017 on the advice of the Investment Consultant. The Board retained the following target allocations (excluding the value of the Scottish Limited Partnership):

Asset Allocation	Target (%)	Range (%)*
Liability Matching Portfolio	60	15-70
Return-Seeking Portfolio	80	70-90

** The sum of the two portfolios' exposures may add to more than 100% if derivatives are used to leverage the Liability Matching Portfolio.*

The Trustee and the Partnership have agreed to hedge increasing amounts of interest rate and inflation risk in the portfolio. The target allocation to the liability matching portfolio has therefore been set to 60% of assets. This target was achieved by the end of 2018.

Investment Management

14 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 an appointed investment manager or managers. The investment managers are expected to possess the skills and expertise necessary to manage the investments of the Trust competently.

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

16 The Pensions Acts distinguish between investments where the management of assets is delegated to a fund manager with a written contract and those where a product is purchased directly, e.g. the purchase of an insurance policy or units in a pooled vehicle. The latter are known as direct investments.

When deciding whether or not to make any new direct investments, the Trustee will obtain written advice from a suitable advisor. The Trustee's policy is to review its direct investments and to obtain written advice about them from the Investment Consultant at regular intervals.

17 The custody of stocks and shares is handled mostly by the Trust's global custodian (except for direct investments, where there are separate custodians/administrators, and the property assets of the Trust). The global custodian provides safekeeping of the Trust's assets and performs administrative duties.

Title deeds of property assets and the certificates for property pooled vehicles are held for safekeeping by the Trustee's property solicitors.

18 The Trust also participates in a programme of security lending, organised by its global custodian. The borrowers are major banks or finance houses, and they provide collateral that has a value greater than that of the securities that are lent to them. The Trustee puts restrictions on the type of collateral it is willing to accept and sets a strict policy on permissible investment of cash collateral.

Responsible Investment

19 The Trustee has adopted the following policy on responsible investment:

- The Trustee's fiduciary duty is to ensure that benefits can be paid when they are due. In this respect the Trustee is a long-term investor

- The Trustee believes that environmental, social and governance (ESG) factors, including climate change, can have an impact on the long-term performance of its investments and, therefore, that the management of ESG risks and opportunities can assist the Trustee in fulfilling its investment duties

- The Trustee formally incorporates ESG factors into the investment due diligence process:

  - Selection of managers: the in-house investment team will request information about an investment manager's ESG policies and these will be used as part of the decision-making process taking into account how ESG risks and opportunities apply to each asset class and/or manager under consideration. If available, ratings from both Mercer (the Trustee's investment consultant) and the PRI will be used to support this process by either corroborating or challenging the investment manager's assertions

  - Ongoing monitoring of managers: a bespoke ESG questionnaire is completed by investment managers on an annual basis in order to assess, monitor and track changes in ESG processes. Again, if available, ratings will be used to support this process. The results are reviewed by the Investment Sub-Committee. Any potential concerns will be discussed with the investment managers by the in-house investment team. If responses are not satisfactory, these will be flagged for further consideration by the Investment Sub-Committee. The Investment Sub-Committee will assess whether there is a material financial risk and, if so, may recommend exit to the Trustee

- The Trustee will not take into account non-financial factors in the investment decision making or monitoring process

- The Trustee believes that active ownership can enhance the value of the Scheme's underlying portfolio and help manage risks. The Trustee is a signatory of the UK FRC Stewardship Code and, in September 2018, became a signatory to the Principles for Responsible Investment. The Trustee reviews its stewardship policy to ensure that it continues to hold its investment managers to account on voting and engagement

- The Trustee's ESG policy is reviewed at least every year.

Risk

20 The key risk faced by the Trust is that it is unable to provide in full the benefits as set out in the Trust Deed. The risk arises if the Trust is unable to achieve the investment returns expected (see paragraph 6) and the Partnership is unable to pay sufficient additional contributions to cover this shortfall.

21 The Trustee reviews, on a quarterly basis, the funding level of the Trust, both on a technical provisions basis and on a self-sufficiency basis. This analysis utilises Mercer's asset/liability model to show projected funding levels of the Trust. Various other risk statistics are considered on both actuarial bases, including tracking errors of the assets vs. the liabilities and VaR(95%) and CVaR(95%).

22 A full asset/liability model is run in conjunction with the triennial actuarial valuation or following significant changes in the benefit structure of the Trust, a significant deterioration in the funding level of the Trust or a material deterioration of the covenant. This enables the Trustee to determine the likelihood of the investment strategy meeting the Trust's investment objectives and to assess the downside risks to the strategy.

23 A De-risking Working Group (DWG) has been established, comprising representatives of the Trustee and the Partnership. The DWG is responsible for considering the scope for de-risking the Trust and the means by which this should be done. The DWG is largely advisory and makes recommendations for the consideration of the ISC. It may, however, be delegated authority to implement risk mitigation measures within a strategy agreed by the ISC from time to time.

24 Additionally, the Trustee recognises a number of risks involved in the investment of the Trust's assets:

- Deficit risk:
  - is measured through a qualitative and quantitative assessment of the expected development of the liabilities relative to the current and alternative investment policies.
  - is managed through assessing the progress of the actual growth of the liabilities relative to the selected investment policy.
- Manager and market risk:
  - is measured by the expected deviation of the return relative to the benchmark set.
  - is managed by limiting exposure to any one investment manager, consideration of the appropriate amount of the Trust to allocate to each active portfolio and by monitoring the actual deviation of returns relative to the benchmark and factors supporting the managers' investment process. The Trust diversifies its investments across a range of asset classes, industry sectors and geographical regions.
  - counterparty risk is addressed through the investment manager guidelines with respect to cash management and ongoing monitoring.
- Liquidity risk:
  - is measured by monitoring the level of cash-flow required by the Trust over a specified period.
  - is managed through holding assets of appropriate liquidity.
- Currency risk:
  - is measured by the level of exposure to non-Sterling denominated assets.
  - is managed by the implementation of a currency hedging programme (through a combination of a segregated currency hedging overlay and currency hedging carried

out by some of the Trust's investment managers) which reduces the impact of exchange rate movements on the Trust's asset value.

- Interest rate and inflation risk:

  - is measured by comparing the likely movement in the Trust's liabilities and assets due to movements in inflation and interest rates.

  - is managed by allocating a proportion of the Trust's assets to a Liability Matching Portfolio which is designed to reduce the Trust's exposure to the risk of adverse movements in inflation and interest rates. The Trustee regularly reviews the split of the Trust's portfolio between the Return-Seeking Portfolio and the Liability Matching Portfolio.

- Hedging Risk

  - is measured by monitoring the level of leveraged hedging undertaken, the level of collateral held, the concentration of the hedging risk exposure with individual counterparties and the credit quality of those counterparties. This covers hedging within both the Return-Seeking and Liability Matching portfolios.

  - is managed by setting maximum amounts of leveraged hedging, limiting the choice of instruments, setting minimum levels of the amount of collateral that can be held in respect of any hedges and imposing financial limits on the total value that can be held with any one counterparty.

- Longevity risk:

  - the Trust has reduced its longevity risk in the following ways:

    - for service after April 2008 through a risk-sharing mechanism, the Life Expectancy Adjustment Factor (LEAF). Actuarial assumptions concerning mortality are reviewed triennially.

    - for service after April 2016, the retirement age is linked to the State Retirement Age.

- Sponsor and solvency risk:

  - the Trustee monitors the Sponsor's covenant by means of a bi-annual internal review and a triennial external review which is timed to coincide with the actuarial valuation. Additional monitoring of the Partnership's trading and other commercial activities takes place on a day-to-day basis.

  - the funding and investment strategies and policies are set by reference to the triennial covenant assessment which measures the strength of the balance sheet and the affordability of the required contributions. The funding level of the Trust is monitored on a daily basis (on a technical provisions basis) and is considered on a formal basis each quarter by the DWG. The DWG will consider the progress of the funding ratio of the Trust and the expected return on the Trust's assets and will make recommendations to the ISC to de-risk the Trust on an opportunistic basis. In addition, the Trustee considers these risks when undertaking triennial or interim strategy reviews.

  - the Trust has a Pension Deficit Mitigation Structure and a Guarantee as described in paragraph 8.

- Political risk:

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

- Reputational risk:
  - the Trustee is aware of the importance that the Sponsor attaches to this risk and works closely with the Sponsor to ensure that the reputational risks associated with the investment portfolio are monitored and managed.

- Operational risk:
  - is addressed through the establishment and maintenance of policies, monitoring and compliance processes and systems. There is a risk register which is reviewed quarterly by the Audit and Risk Committee who report to the Trustee Board.

- Custodian risk:
  - custodian risk is addressed through the custody agreement and regular monitoring of the custodial arrangements. The credit rating of the custodian is also monitored. Restrictions are applied on who can authorise transfers of cash and the accounts to which transfers can be made.

Further Information

25 The Annual Report and Accounts for the Trust are published in July every year and are available on the Partner intranet. For more information on the Trust's investment strategy please contact Imtayaz Ahmed (Pensions Investment Manager) 020 7931 4678 (External) and 777-3678 (Internal).

Signed: Andrew Ingram

Name: ANDREW INGRAM

Date: 24.09.19

Authorised for and on behalf of the Trustee of the Trust