United Utilities PLC Group of the Electricity Supply Pension Scheme

Statement of Investment Principles

March 2024

1. Introduction

1.1 The Trustee of the United Utilities PLC Group of the Electricity Supply Pension Scheme ("the Group") 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 is intended to affirm the investment principles that govern decisions about the Group's investments.

1.2 In preparing this Statement the Trustee has consulted the Sponsor Company.

1.3 The Trustee has established an Investment Sub-Committee ("ISC"). It has delegated responsibility for operational matters, including regular investment monitoring and the appointment and termination of investment managers to the ISC. Any decisions regarding the Group's investment strategy are undertaken by the Trustee after receiving advice from the ISC.

1.4 The Trustee has also established a Joint Working Group ("JWG"). The JWG is a joint Trustee and Company Committee. Its role is to provide a framework to achieve an effective, integrated investment and funding strategy for the Group. The aim of the JWG is to achieve these goals whilst maintaining a decision structure where the Trustee Board (via the ISC) retains appropriate control over the investment of the Group's assets.

2. Process For Choosing Investments

2.1 The process for choosing investments is as follows:

- Identify appropriate investment objectives.
- Agree the level of risk consistent with meeting the objectives set.
- Build an investment strategy that achieves the above.
- Throughout, consider relevant environmental, social and governance (ESG) matters.

2.2 In considering the appropriate investments for the Group the Trustee has obtained and considered the written advice of its Investment Consultant, Mercer Limited ("Mercer), whom the Trustee believes to be suitably qualified to provide such advice. 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. Investment Objectives

3.1 The Trustee's objective is to invest the Group's assets in the best interest of the members and beneficiaries and in the case of a potential conflict of interest, in the sole interest of the members and beneficiaries. Within this framework, the Trustee has agreed a number of objectives to help guide the strategic management of the assets and control of the various risks to which the Group is exposed. The Trustee's primary objectives are set out below:

- To maintain a Group funding level of at least 100% on a Technical Provisions basis. The Technical Provisions funding target broadly represents a reasonably cautious calculation of the value of the Group's liabilities;
- To ensure the Group's obligations to its beneficiaries can be met;
- To achieve an asset return above the return from gilts over the longer term, whilst recognising the need to balance risk control and return generation;
- To ensure consistency between the Group's investment strategy and the return assumptions used by the Group Actuary;
- To pay due regard to the Company's interests in the size and incidence of employer contribution payments, and to avoid volatility in the contribution rate;
- To maintain a 100% interest rate and inflation hedge (as measured on the Gilts + 0.25% p.a. basis) on the residual liabilities not covered by the Group's bulk annuity insurance contract.

4. Risk Management and Measurement

4.1 The Trustee considers a range of potentially financially material factors to which the Group is exposed over the anticipated time horizon for which the assets will be held.

4.2 In deciding to take investment risk relative to the liabilities, the Trustee has carefully considered the following possible consequences:

- The assets might not achieve the excess return relative to the liabilities anticipated over the longer term. This would result in deterioration in the Group's financial position and consequently higher contributions than currently expected from the Company.
- The relative value of the assets and liabilities will be more volatile over the short term than if investment risk had not been taken. This will increase the possibility of there being a shortfall of assets relative to the liabilities in the event of discontinuance of the Group.
- This volatility in the relative value of assets and liabilities may also increase the short-term volatility of the Company's contribution rate set at successive actuarial valuations, depending on the approach to funding adopted.
- The risk that the bulk annuity insurance provider may default on their obligations (as contracted). Before entering into the contract with the insurer, the Trustee obtained and carefully considered professional advice regarding the financial strength of the insurer and concluded that the risk was acceptably low.

The Trustee has taken advice on these issues from its Investment Consultant and the Group Actuary. It has also held related discussions with the Company.

4.3 The degree of investment risk the Trustee is willing to take also depends on the financial position of the Group. The Trustee will monitor the funding level of the Group and its liability profile, with a view to altering the investment objectives, risk tolerance and/or return target should there be a significant change in either.

4.4 There are various risks to which any pension scheme is exposed. The Trustee's policy on risk management is as follows:

- The primary risk upon which the Trustee focuses is that arising through a mismatch between the Group's assets and its liabilities. Bearing in mind the above factors, and after taking advice from the Investment Consultant and Group Actuary, the Trustee has adopted a low risk investment strategy, comprised of fixed income assets and a bulk annuity insurance policy, which is expected to maintain a fully funded position on the Technical Provisions basis.
- The Trustee recognises 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 Group's accruing liabilities as well as producing more short-term volatility in the Group's funding position. The Trustee has taken advice on the matter and considered carefully the implications of adopting different levels of risk.
- The Trustee recognises 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 Trustee aims to ensure the asset allocation policy in place results in an adequately diversified portfolio.
- The safe custody of the Group's assets is delegated to professional custodians (either directly or through the use of pooled vehicles).

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

5. Investment Strategy

5.1 The Trustee has decided to implement a Cashflow Driven Financing ("CDF") strategy as part of an integrated risk management approach across investment, funding and security measures.

5.2 Through the Group's investment in pooled Buy & Maintain Credit, income will be received from the bonds that can be used to help pay benefit payments.

5.3 The intention is that the liability discount rate is set equal to the estimated yield on the asset portfolio less a margin for losses (for example due to defaults), manager fees and other costs. This discount rate will then broadly vary in line with market conditions (i.e. it will be 'dynamic' in nature), and as such the funding position is expected to be relatively stable. Any funding deficit will therefore need to be rectified via cash contributions and/or from asset outperformance.

The Investment Strategy takes into account:

- The maturity profile of the Group in terms of the relative proportions of liabilities in respect of pensioners and non-pensioners allowing for the bulk annuity policy;
- The Technical Provisions liability valuation basis; and
- The expected strength of covenant of the Sponsor Company.

5.4 The strategic asset allocation (excluding annuities) is as follows:

Asset Class	Investment Manager	Allocation (%)
Buy & Maintain Investment Grade Credit	Legal & General Investment Management	50.0
Liability Driven Investment (LDI)	Legal & General Investment Management	50.0
Total		**100.0**

5.5 There is no automatic rebalancing between the different portfolios, but the allocation is reviewed on at least a quarterly basis and adjustments are made if appropriate.

5.6 The appointed investment manager is regulated by the appropriate UK regulatory authority. The Group's assets invested with Legal & General Investment Management ("LGIM") are held in pooled funds; the Group Trustee's entitlement being to the cash value of the pooled fund units.

5.7 Day-to-day management of these assets is delegated to LGIM as Investment Manager. LGIM have discretion over the investment of the Group's assets, subject to the restrictions detailed in the paragraphs below and in the respective Pooled Fund Prospectuses in place between the Group Trustee and the Investment Manager.

5.8 Specific considerations for the individual mandates are outlined below:

5.9 LGIM LDI Portfolio (50% of strategic asset allocation)

Investment Objective

- The LDI strategy comprises funds which are designed to achieve the desired interest rate and inflation exposure, and are collateralised by cash and/or gilts.

- Each of the LDI funds used has an upper and lower rebalancing point. Should an upper rebalancing point be reached, LGIM will seek to reduce the "hedging multiple "of the fund. LGIM may either maintain the same exposure and top up the leveraged fund with additional assets, or reduce the exposure. Similarly, when a lower rebalancing point is reached, LGIM will increase the hedging multiple by either maintaining the same exposure and distributing cash, or by increasing the exposure within the fund. The aim is to maintain the targeted level of inflation and interest rate protection.

- The Trustee has adopted a service model whereby LGIM manages the Group's target hedge ratios to the Group specific liability benchmark. LGIM will also manage any collateral calls and cash distributions within the mandate.

5.10 Buy & Maintain Credit Portfolio (50% of strategic asset allocation)

Investment Objective

- The mandate seeks to capture the credit risk premium and liquidity risk premium available in credit markets through investing in a pooled fund of globally diversified bonds, and through avoiding investments in securities which LGIM believes are likely to default or experience a significant deterioration in credit quality.
- The Fund the Group invests in aims to provide a climate warming alignment target of 1.5^{o} C by 2030 and has an awareness of UN Sustainable Development Goals in how the portfolio is constructed. The investment manager will exclude certain companies not deemed to offer sustainable investment characteristics, including violators of the UN Global Compact, and companies involved in mining and extraction of thermal coal, thermal-coal-power generation and oil sands.
- The mandate also assists the Group in its management of its Liability Cashflow matching requirements.
- The interest rate exposure of holdings in non-Sterling denominated bonds will be hedged back to Sterling using permitted derivatives. Whilst the currency exposure is hedged back to Sterling, the ability to make material allocations to overseas bonds gives the Investment Manager the opportunity to benefit from issues and issuers not present in the UK market.

In seeking to achieve the investment objective, LGIM shall not seek to breach the guidelines agreed with the Trustee.

5.11 L&G Bulk Annuity Policy

An annuity policy has been secured to cover a portion of the liabilities. The objective of the policy is to meet the liabilities of all members covered by the policy.

5.12 Rebalancing and Cashflow Policy

Reflecting the Trustee’s desire to mitigate transaction costs and forced trading, there is no formulaic rebalancing, although the asset allocation is reviewed on at least a quarterly basis and any cashflows over and above those required to meet benefit outgo are used to maintain the strategic benchmark allocation.

As required, cash to meet benefit outgo and expenses will be sourced from:

- Available investment income from the Buy & Maintain Credit portfolio;
- Annuity income from L&G, designed to exactly cover a specified portion of member benefits.

These are paid directly into the Trustee Bank Account as they arise.

5.13 Additional Voluntary Contributions (“AVCs”)

Whilst the main Group assets are invested in line with the above, members have four investment options in respect of their Additional Voluntary Contributions (AVCs):

- Aegon platform pooled investment funds:
  - LGIM Future World Global Equity Index Fund
  - BlackRock 50:50 Global Equity Index Fund
  - BlackRock Over 5 Year Index-Linked Gilt Index Fund
  - BlackRock Cash Fund
- In-Group:
  - Added years

5.14 In addition, legacy AVC investments are held with Prudential (with-profits fund). This arrangement is closed to new contributions.

5.15 The Trustee is responsible for the investment of the AVCs paid by members reviewing the investment performance of the chosen providers on an ongoing basis, and taking advice as to the providers’ continued suitability.

5.16 There are no other Group assets.

6. Day-to-Day Management of the Assets

6.1 The Trustee delegates the day-to-day management of the assets to the investment managers. The Trustee has taken steps to satisfy itself that the managers have the appropriate knowledge and experience for managing the Group’s investments and that they are carrying out their work competently.

6.2 The Trustee has determined, based on expert advice, guidelines and ranges within which each appointed investment manager may operate.

6.3 The Trustee regularly reviews the continuing suitability of the Group’s investments, including the appointed managers.

6.4 Each of the appointed managers has been set a specific objective by the Trustee.

6.5 In the event of a change in investment manager, the Trustee may appoint a transition manager to facilitate the required asset transfer.

7. Monitoring

7.1 Arrangements are in place to monitor the Group’s investments to help the Trustee check that nothing has occurred that would bring into question the continuing suitability of the current investments. To facilitate this, the Trustee meets with the Group’s managers and receives regular reports from all the investment managers and the Investment Consultant.

8. Environmental, Social and Governance (ESG) Considerations

8.1 The Trustee believes that ESG issues have an impact on investment risk and return outcomes, and that good stewardship can create and preserve value for companies and markets as a whole, hence having the potential to benefit Group members in the long-term. The Trustee also recognises that long-term sustainability issues, particularly climate change, present risks and opportunities that increasingly require explicit consideration.

8.2 The Trustee accordingly considers these issues in the context of anticipated time horizon over which the assets will be held.

8.3 The Trustee has undertaken ESG training facilitated by its advisers. As part of this training the Trustee carried out an ESG beliefs survey in order to assist with developing a policy in this regard. Alongside the ESG investment policies detailed here, the Trustee maintains an ESG Policy which covers broader matters alongside those that relate to investments.

8.4 The Trustee does not directly manage its investments; the investment managers and annuity provider have full discretion to buy and sell investments within the various funds, within the guidelines of their mandates. ESG considerations are however taken into account in the selection, retention and realisation of investments in the following ways:

- The Trustee has arranged for ESG related exclusions to be implemented within the Buy & Maintain Credit portfolio, consistent with mitigating material ESG risks and enhancing the resilience of the Group to ESG risks including climate change.
- The Trustee considers the ESG research ratings published by its investment advisors, Mercer, when monitoring the Group's investment managers' capabilities. These ratings are reported quarterly and also considered as part of any new selection of investment funds.
- In annual meetings with the Group's investment managers, ESG issues are discussed and the manager is expected to discuss stewardship activities carried out on behalf of the Trustee for mandates where this is relevant.
- An AVC fund option has been made available to members which takes into consideration ESG issues and integrates these factors into how the fund is managed. For example, there is a focus on reducing carbon emissions and companies that don't reflect the values of sustainability are excluded from the fund.

8.5 The Trustee periodically engages with members via surveys, to understand the views of Group members in relation to ESG matters, among other topics.

9. Investment Manager Arrangements

Overview

9.1 The Group's investment managers and annuity provider are appointed based on their capabilities and suitability as regards meeting the Group's objectives.

9.2 The annuity provider does not have investment return related objectives, and the information below covers the residual assets excluding the bulk annuity policy.

9.3 The Trustee receives advice from its Investment Consultant (the "Consultant") in relation to forward-looking assessments of a manager's ability to achieve its performance objective over a full market cycle. This view will be based on the Consultant's assessment of the manager's idea generation, portfolio construction, implementation and business management, in relation to the particular investment portfolios(s) that the Group invests in. The Consultant's manager research ratings assist with due diligence and questioning managers during presentations to the Trustee and are used in decisions around selection, retention and realisation of manager appointments.

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

9.5 Some appointments are actively managed and the managers are incentivised through performance targets. An appointment will be reviewed following periods of sustained underperformance or failure to meet the mandate objectives, and the Trustee has put in place quarterly monitoring to seek to manage this risk. The Trustee will review the appropriateness of using actively managed funds (on an asset class basis) periodically.

9.6 As the Trustee invests in pooled vehicles it accepts that there is no ability to specify the risk profile and return targets of the manager. However, appropriate mandates are selected to align with the overall investment strategy.

Investment Manager Remuneration

9.7 The majority of investment managers are remunerated by way of a fee calculated as a percentage of assets under management. For liability hedging a fee is calculated based on the percentage of liabilities hedged. In each case, the principal incentive is for the investment manager to retain their appointment (in full), by achieving their objectives, in order to continue to receive their fee.

9.8 The Trustee reviews annually fee transparency and total expense ratio charges.

9.9 Investment managers are not remunerated based on portfolio turnover.

Evaluating Investment Managers

9.10 Investment managers are aware that their continued appointment is based on their success in delivering the objectives of the mandate for which they have been appointed to manage. If the Trustee is dissatisfied, then it will look to replace the manager.

9.11 The Trustee meets with its investment managers, with the Consultant also present, as deemed appropriate. During such meetings the Trustee is able to review the decisions made by the managers, including investment decisions, voting history (although voting rights are relatively rare given the nature of the Group's investments) and engagement activity with investee companies, and can question such activities.

9.12 The Trustee considers the Consultant's investment research and ESG research ratings within quarterly reporting. Through these ratings, the Trustee is able to assess for example how each investment manager embeds ESG into its investment process and how each manager's investment philosophy aligns with the Trustee's policies.

Time horizon and Duration of Appointments

9.13 The Trustee receives investment manager performance reports on a quarterly basis, which present performance information over 3 months, 1 year, 3 years. The Trustee reviews the performance of the investments on an absolute basis and relative to defined benchmarks (over the relevant period) on a net of fees basis. The Trustee's focus is long-term performance but will put a manager "on watch" if there are short-term performance concerns.

9.14 If a manager is not meeting its performance objectives, over a sustained period of time, and after consideration of all relevant factors, the Trustee may take the decision to terminate the manager.

9.15 The Trustee is a long-term investor. Accordingly, it does not seek to change the investment arrangements on a frequent basis.

9.16 The funds invested in are open-ended with no set end date for the arrangement. The Trustee will retain an investment manager unless:

- There is a strategic change to the overall strategy that no longer requires exposure to that asset class or manager; or
- The manager appointment has been reviewed and the Trustee has decided to terminate the manager.

9.17 The annuity policy is structured to meet all benefit obligations of the members that it covers and can therefore be considered illiquid and designed as a long term investment.

Portfolio turnover costs

9.18 The Trustee does not monitor portfolio turnover costs and has no set portfolio turnover targets; rather the Trustee assesses investment performance net of the impact of the costs of such activities.

10. Compliance with this Statement

10.1 The Trustee should monitor compliance with this Statement annually and obtain written confirmation from the investment managers that they have given effect to the investment principles in this Statement so far as reasonably practicable and that in exercising any discretion the investment managers have done so in accordance with Section 4 of The Occupational Pension Schemes (Investment) Regulations 2005.

11. Review of this Statement

11.1 The Trustee will review this Statement annually and without delay after any significant change in investment policy. Any change to this Statement will only be made after having obtained and considered the written advice of someone who the Trustee reasonably believes to be qualified by their ability in and practical experience of financial matters and to have the appropriate knowledge and experience of the management of pension scheme investments. In addition, the Trustee will obtain written confirmation from the investment managers that they have complied with its requirements.

Signed on behalf of UU (ESPS) Pensions Trustee Limited

Signed: _ ______________ Date: March 2024

Name: Gary Dixon