

Statement of Investment Principles

For the Pearson Pension Plan

Effective from: 4 December 2024



1. Introduction

This Statement of Investment Principles (“SIP”) has been prepared by the Trustee of the Pearson Pension Plan.

It sets out the Trustee’s policies on various matters governing investment decisions for the Pearson Pension Plan (“the Plan”), which has Final Pay and Defined Contribution (“DC”) sections. This SIP also covers the Additional Voluntary Contribution arrangements (“AVCs”).

This SIP replaces the previous SIP dated 25 June 2024.

This SIP has been prepared after obtaining and considering written advice from LCP, the Plan’s investment adviser, whom the Trustee believe to be suitably qualified and experienced to provide such advice. The advice considered the suitability of investments including the need for diversification given the circumstances of the Plan and the principles contained in this SIP.

The Trustee has consulted with the plan sponsor in producing this SIP.

The Trustee will review this SIP from time to time and will amend it as appropriate. Reviews will take place without delay after any significant change in investment policy in the demographic profile of the members invested in the DC default investment option and at least once every three years.

This SIP contains the information required by legislation, and also considers the Pension Regulator’s guidance on investments.

2. Investment objectives for the Final Pay and DC Sections

The primary objective for the **Final Pay Sections** is to ensure that the benefit payments are met as they fall due. In addition to this primary objective, the Trustee has the following objectives:

- An overall objective to invest the Plan’s assets in such a way that sufficient money is available to meet the liability to provide benefits to the members of the Plan into the future. This includes, where possible and agreed with the Principal Employer, discretionary increases to pensions in payment in excess of the guarantees in the Plan Rules, so that total pension increases over time broadly aim to protect against cost of living increases.
- As a precondition of the above, the Trustee will endeavour to invest the Plan’s assets to achieve returns in excess of the growth in the liabilities, whilst maintaining a prudent approach to meeting the Plan’s liabilities.

The Trustee’s primary objectives for the **DC Sections** are to:

- Provide an appropriate range of investment options, reflecting the membership profile of the DC sections and the variety of ways that members can draw their benefits in retirement;
- Provide clear information on the investment options and their characteristics that will allow members to make informed choice and;
- Provide a default investment option that the Trustee believes to be reasonable for those members that do not wish to make their own investment decisions.

The Plan Trustee is required to designate a default arrangement into which members who are automatically enrolled are invested. The Trustee has designated the Drawdown Lifecycle as the main DC default arrangement for the Plan. The objective of the Drawdown Lifecycle is to generate returns above inflation whilst members are some distance from retirement, but then to switch automatically and gradually to investments that more closely match the intentions of members.

This is also the default arrangement for AVC assets for new and existing members that have assets invested in the Money Purchase and Auto Enrolment sections. This does not apply, however, to AVC benefits where the member has no assets already invested in the Drawdown Lifecycle through the Money Purchase or Auto Enrolment sections, or is a DB member with AVC benefits but no assets in these aforementioned DC sections.

The Trustee has designated the Cash Lifecycle as the default arrangement for AVC assets within the Plan where existing members do not have assets invested in the Money Purchase and Auto Enrolment sections, or are DB members with AVC benefits who do not have assets invested in the Money Purchase or Auto Enrolment sections of the Plan.

Additionally, there is a legacy default option, the Annuity Lifecycle, which remains a lifecycle option for members to select. This option targets the purchase of an annuity at retirement.

The aim and objective of all the default Lifecycle strategies is to provide members with the potential for higher levels of growth during the accumulation of their retirement savings through exposure to equity and diversified growth funds (“DGFs”) and then to gradually diversify their investments in the years approaching retirement. The asset allocation throughout the default Lifecycles and the phasing of the gradual switching of investments aims to take into account members' greater capacity for risk early on and reduced capacity for risk closer to retirement. Each option is designed to reflect the Trustee's belief that most members in that strategy will take their benefits in the specified form.

A default was also created as a result of temporary suspension of the Threadneedle Pensions Property Fund. This default option is a fixed allocation to the BlackRock Sterling Liquidity Fund and targets cash withdrawal at retirement, since the Trustee believes this is the most appropriate alternative for these contributions given the temporary suspension of the Property Fund and the inability for the Trustee to exercise members' choice to invest in the Property Fund for any contributions invested during the suspension period. The aims and objectives are that the fund aims to maximise current income consistent with the preservation of capital and liquidity through the maintenance of a portfolio of high quality short-term money market instruments and to achieve an investment return that is in line with its benchmark.

The DC platform provider closed the MFS Meridian Global Equity Fund in December 2024. The Trustee decided to transfer the member assets remaining in the MFS fund to the Blended Global Equity Fund, and this made the Blended Global Equity Fund a default. The Blended Global Equity Fund aims to provide returns consistent with the composite benchmark by investing in a range of funds that provide exposure to global equities, including emerging market equities.

Some of the DC members are impacted by a Reference Scheme Test (“RST”) underpin.

All policies relating to the **DC default options** are covered in this SIP, rather than in a separate SIP, so all policies on the Plan's investments are in one document.

The Trustee's investment objective for the AVCs is to make available a suitable range of investment options to meet members' risk / return objectives.

3. Investment strategy

With input from the Plan's advisers and in consultation with the Plan sponsor, the Trustee reviewed the investment strategy for the Final Pay and DC Sections in August 2022, considering the objectives described in Section 2.

Asset allocation is considered regularly by the Trustee and reviewed in detail following each actuarial valuation, taking into account the objectives described in Section 2 above.

The Trustee divides the assets of the Final Pay Sections of the Plan into two sections, the **Insurance Portfolio** and the **Main Portfolio**, which are composed as follows:

- The **Insurance Portfolio** consists of assets which are held in the form of insurance contracts matching a portion of the liabilities of the Plan.

The insurer pays the Plan an amount equal to the pension payment in respect of the members underlying the policy. These insurance contracts, known as buy-in policies are assets of the Plan and the pension liability remains within the Plan.

Towards the end of 2017 the Plan purchased two separate buy-in policies. The two policies covered approximately two thirds of the pensioner members' liabilities at the time of the transactions. The Plan purchased a further buy-in policy in February 2019 which covered most of the remaining uninsured pensioner members' liabilities at the time of the transaction.

- The **Main Portfolio** consists of all Plan assets outside of the Insurance Portfolio. The Main Portfolio is composed of **Matching** and **Return Seeking** assets.
 - The **Matching Assets** are those which produce cashflows that can be expected to match the Plan's liabilities for a portion of the membership. The Matching Assets include bonds, inflation-linked property and infrastructure.
 - The **Return Seeking Assets** are invested with a long-term horizon to generate the returns needed to provide the remaining expected cashflows for the beneficiaries. This portfolio is invested in a diversified portfolio of return seeking assets. The Return Seeking Assets are expected to consist of an allocation to trade finance, infrastructure, private equity and property.

- The Plan's total allocation as at 31 December 2023 was c.93% to the Insurance portfolio and Matching Assets and c.7% to Return Seeking Assets. The actual allocation depends on the relevant market values and so will fluctuate over time.

This is a low-risk asset allocation which maintains a low probability of requiring further contributions from the Plan's Sponsor.

The primary focus of the Plan's allocation of investments is accurate cashflow matching and risk control.

The Insurance Portfolio is cashflow matching as it provides payments which are expected to exactly match the benefit payments for the insured members.

A small allocation to Return Seeking Assets has been maintained in the Plan's asset allocation to provide a buffer for any changes in actuarial assumptions, longevity risk, and potentially to allow for discretionary increases to members in certain scenarios.

Based on asset-liability modelling as at 30 June 2022, the Plan's invested assets (excluding the Insurance Portfolio), are expected to generate a return of 1.7% per annum above gilts with an acceptable level of volatility. The Plan's investment strategy is reviewed and modelled following each Actuarial Valuation. The allocation to each asset class will vary due to market movements and will be kept under review by the Trustee.

For the **DC Sections** (which includes the Money Purchase sections and the Auto Enrolment section), the Trustee makes available a range of investment funds for members with different levels of expected risk and return, including equity and bond based funds as well as a cash fund. Each member has the opportunity to specify one or more funds for the investment of their account.

If a member does not choose an investment option, their account will be invested in the **main default option**, the "Drawdown Lifecycle" which is managed as a "lifecycle" strategy (ie it automatically combines investments in proportions that vary according to the time to retirement age). The main default initially invests to target a high expected return (making use of equity-based funds) and then gradually switches to investments with a lower expected return and risk as members get close to retirement.

The main default option was designed to be in the best interests of the majority of the members based on analysis of the demographics of the membership. The default option targets drawdown at retirement, since, based on analysis of the membership, the Trustee believes that most members will wish to take their benefits in this form. This analysis took into account factors such as age, salary, contribution level, accumulated fund values and term to retirement to identify

different types of member in order to test alternative investment strategies. The design of the default Lifecycle strategies reflects this analysis having carried out multiple simulations of future economic and investment scenarios.

The Trustee monitors member behaviour to check whether assumptions made about how members will access their benefits are borne out in practice.

4. Considerations in setting the investment arrangements

When deciding how to invest the Plan's assets, it is the Trustee's policy to consider a range of asset classes, taking account of the expected returns and risks associated with those asset classes, as well as the Trustee's beliefs about investment markets and which factors are most likely to impact investment outcomes.

The primary ways that the Trustee manages investment risk are via diversification, having received professional written advice prior to making any material investment decision, and ongoing monitoring and oversight of the investments. For the Final Pay Sections investment risk is measured using "Value at Risk". For the DC Sections investment risk is measured as standard deviation.

In setting the strategy for the **Final Pay Sections** it is the Trustee's policy to consider:

- the best interests of members and dependents;
- the Plan's investment objectives, including the target return required to meet the Trustee's investment objectives;
- the Plan's cash flow requirements in order to meet benefit payments in the near to medium term;
- the circumstances of the Plan, including the profile of the benefit cash flows (and the ability to meet these in the near to medium term), the funding level, and the strength of the employer covenant;
- the risks, rewards and suitability of a number of possible asset classes and investment strategies and whether the return expected for taking any given investment risk is considered sufficient given the risk being taken; and
- the need for appropriate diversification between different asset classes to ensure that both the Plan's overall level of investment risk and the balance of individual asset risks are appropriate.

In determining the investment arrangements for the **DC Sections including the default options** and for the AVCs it is the Trustee's policy to consider:

- the best interests of members and beneficiaries;
- the profile of the membership and what this is likely to mean for the choices members might make upon reaching retirement;
- the risks, rewards and suitability of a number of possible asset classes and lifecycle strategies and whether the return expected for taking any given investment risk is considered sufficient.
- the need for appropriate diversification within the default strategies and other lifecycle options to ensure that, for each such option, both the overall level of investment risk and the balance of individual asset risks are appropriate;
- the need for appropriate diversification within the other investment options offered to members.

The Trustee also considers any other factors which it believes to be financially material over the applicable time horizons to the funding of the Final Pay Sections, DC and AVC benefits, including environmental, social and governance ("ESG") factors and the risks and opportunities relating to climate change.

The Trustee's key investment beliefs, which influenced the setting of the investment arrangements, are as follows:

- asset allocation is the primary driver of long-term returns;
- Fund management costs may have a significant impact on long-term performance and therefore obtaining value for money from the investments is important;
- investment managers who can consistently spot and profitably exploit market opportunities are difficult to find, and therefore passive management is often better value;
- risk-taking is necessary to achieve return, but not all risks are rewarded. Equity, credit, and illiquidity are the primary rewarded risks. Risks that do not have an expected reward should generally be avoided, hedged, or diversified;
- ESG factors should be considered when making investment decisions, and managers may be able to improve risk-adjusted returns by doing this; and
- climate change is a financially material systemic issue that presents risks and opportunities for the Plan over the short, medium and long term.

5. Implementation of the investment arrangements

Before investing in any manner, the Trustee obtains and considers proper written advice from its investment adviser as to whether the investment is satisfactory, having regard to the need for suitable and appropriately diversified investments.

The Trustee has signed agreements with the investment managers (in respect of the Final Pay sections), and a platform provider in respect of the DC Section, setting out the terms on which the portfolios are to be managed. The DC platform provider makes available the range of investment options to members. There is no direct relationship between the Plan and the underlying managers of the DC investment funds.

The Trustee and investment managers to whom discretion has been delegated exercise their powers to give effect to the principles in this Statement of Investment Principles, so far as is reasonably practical.

The Trustee's view is that the fees paid to the investment managers, and the possibility of their mandate being terminated, ensure they are incentivised to provide a high quality service that meets the stated objectives, guidelines and restrictions of the fund. However, in practice managers cannot fully align their strategy and decisions to the (potentially conflicting) policies of all their pooled fund investors in relation to strategy, long-term performance of debt/equity issuers, engagement and portfolio turnover.

It is the Trustee's responsibility to ensure that the managers' investment approaches are consistent with its policies before any new appointment, and to monitor and to consider terminating any existing arrangements that appear to be investing contrary to those policies. The Trustee expects investment managers, where appropriate, to make decisions based on assessments of the longer term financial and non-financial performance of debt/equity issuers, and to engage with issuers to improve their performance. It assesses this when selecting and monitoring managers.

The Trustee evaluates investment manager performance by considering performance over both shorter and longer-term periods as available. Except in closed-ended funds where the duration of the investment is determined by the fund's terms, the duration of a manager's appointment will depend on strategic considerations and the outlook for future performance. Generally, the Trustee would be unlikely to terminate a mandate on short-term performance grounds alone.

The Trustee's policy is to evaluate each of its investment managers by reference to the manager's individual performance as well the role it plays in helping the Plan meet its overall long-term objectives, taking account of risk, the need for

diversification and liquidity. Each manager's remuneration, and the value for money it provides, is assessed in light of these considerations.

The Trustee recognises that portfolio turnover and associated transaction costs are a necessary part of investment management and that the impact of portfolio turnover costs is reflected in performance figures provided by the investment managers. The Trustee expects its investment consultant to incorporate portfolio turnover and resulting transaction costs as appropriate in its advice on data related to the Plan's investment mandates.

6. Realisation of investments

For the Final Pay Sections, in general, individual investment managers have discretion in the timing of the purchase and sale of investments and in consideration relating to the liquidity of those investments.

The Trustee, and investment managers (to the extent delegated), will use the criteria set out in the Occupational Pension Schemes (Investment) Regulations 2005, when selecting investments on behalf of the Plan. The Trustee expects the investment managers to give effect to the principles in this statement as far as is reasonably practical.

The Trustee has agreed a series of investment restrictions for each manager where there is a separate Investment Management Agreement (IMA) in place. The Trustee will monitor the continuing tenure of the Investment Managers, including the competitiveness of their fee structures, from time to time, based on advice from the Investment Committee (IC) and the external investment adviser. The Trustee will also utilise compliance reporting provided by the custodian, Bank of New York Mellon, in the monitoring of Investment Managers.

For the DC Sections including the default, the Trustee's policy is to invest in funds that offer daily dealing to enable members to readily realise and change their investments. The default includes an allocation to DGFs via pooled funds (a type of collective investment scheme), that may include an allocation to illiquid assets (of direct property and infrastructure) if the DGF manager chooses to do so. As at September 2023, the exposure to the illiquid assets of direct property and infrastructure constituted around 5% of the DGF allocation. Members from 15 years to retirement (age 47 and above assuming a retirement age of 62) who are invested in the default have exposure to illiquid assets via the DGF allocation.

We believe that long-term net risk-adjusted investment returns may be improved by investing in illiquid assets. However, investment in illiquid assets in DC pension schemes is a relatively new and developing area. Therefore, at this time, it is the Trustee's policy not to invest the DC default in illiquid assets other than via the DGFs. But, with the support of its investment advisers, the Trustee intends to

consider investment in more specific illiquid assets as and when appropriate (eg as part of default strategy reviews) and in the context of the Plan.

7. Financially material considerations and non-financial matters

The Trustee believes that environmental, social and governance (ESG) factors are likely to be an area of market inefficiency and so managers may be able to improve risk-adjusted returns by taking account of ESG including climate related factors.

The Trustee has considered how ESG and ethical factors should be taken into account in the selection, retention and realisation of investments, given the time horizon of the Plan and its members. The Trustee expects its investment managers to take account of financially material considerations (including climate change and other ESG considerations). The Trustee seeks to appoint managers that have appropriate skills and processes to do this, and from time to time reviews how its managers are taking account of these issues in practice.

The Trustee has limited influence over managers' investment practices where assets are held in pooled funds, but it encourages its managers to improve their practices where appropriate within the parameters of their funds.

The DC sections include an equity investment option focused on ESG risks as a choice for members to select if they wish to. A small number of members also remain invested in an alternative option which takes account of ESG risks; however, this alternative fund option is now closed to new members. The short duration credit fund, which is both available for members to select and part of the default investment strategy, has an explicit commitment to sustainability in its investment objective. At this time, the Trustee does not believe there are any additional ESG-focused investment options available that meet members' needs appropriately in any other asset classes but will keep this under review.

The Trustee does not consider any non-financial matters (ie matters relating to the ethical and other views of members and beneficiaries, rather than considerations of financial risk and return) in the selection, retention, and realisation of investments. However, it recognises the importance of offering a suitable range of investment options for members who wish to express an ethical preference in their pension saving and so has suitable options available.

The IC proactively monitors all of the Plan's active investment managers. In addition to the usual quarterly monitoring, the active investment managers are required to attend IC meetings periodically. These Manager presentations provide an opportunity for the IC to discuss responsible investment along with other aspects of the manager's mandate and are considered an important aspect of these discussions.

In addition to the above the IC also undertakes the following:

- When appointing new active investment managers, their approach to socially responsible investment and environmental, social and governance factors is incorporated into the selection process and referenced in their Investment Management Agreements.
- The IC reviews the Plan's responsible investment policy, typically once a year. The latest investment manager policies are also reviewed and developments in responsible investment are discussed.
- The Plan monitors whether its Investment Managers are signatories of the UN Principles for Responsible Investment (PRI). The IC encourages investment managers to become PRI signatories and requests explanations where they are not.

8. Voting and engagement

The Trustee recognises its responsibilities as an owner of capital, and believes that good stewardship practices, including monitoring and engaging with investee companies, and exercising voting rights attaching to investments, protect and enhance the long-term value of investments. The Trustee has delegated to its investment managers the exercise of rights attaching to investments, including voting rights, and engagement with issuers of debt and equity and other relevant persons about relevant matters such as performance, strategy, capital structure, management of actual or potential conflicts of interest, risks and ESG considerations.

The Trustee does not monitor or engage directly with issuers or other holders of debt or equity. It expects the investment managers to exercise ownership rights and undertake monitoring and engagement in line with the managers' general policies on stewardship, as provided to the Trustee from time to time, considering the long-term financial interests of the beneficiaries. The Trustee expects the managers to communicate their policies on stewardship to them from time to time, and provide them with reports on the results of their engagement and voting activities at least once a year.

The Trustee seeks to appoint managers that have strong stewardship policies and processes, reflecting where relevant the recommendations of the UK Stewardship Code issued by the Financial Reporting Council, and from time to time the Trustee reviews how these are implemented in practice.