

# Statement of Investment Principles

The New Airways Pension Scheme (NAPS)

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# 1 Introduction

- 1.1. New Airways Pension Scheme Trustee Limited (the “Trustee”), as Trustee of the New Airways Pension Scheme (“NAPS”, the “Scheme”) has prepared this Statement of Investment Principles (the “Statement”) to comply with the requirements of the Pensions Act 1995 (the “Act”) and subsequent legislation.
- 1.2. The Statement sets out the investment principles that govern decisions about the Scheme’s investments and applies to all investments held by the Scheme.
- 1.3. The Trustee maintains an Investment Strategy Framework document (“ISF”) that sets out the Scheme’s current investment arrangements, based on the principles set out in this Statement.
- 1.4. In preparing this Statement the Trustee has considered written advice from the Scheme’s appointed Investment Advisor, who is considered to be suitably qualified. 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), the Occupational Pension Schemes (Investment) Regulations 2005 and subsequent legislation.
- 1.5. The Trustee’s investment powers are set out within the Scheme’s governing documentation and relevant legislation. If necessary, the Trustee will take legal advice regarding the interpretation of these. The Trustee notes that, according to the law, the Trustee has ultimate power and responsibility for the Scheme’s investment arrangements.
- 1.6. The Trustee seeks to maintain a good working relationship with the Sponsoring Company (the “Company”, British Airways Plc) and will discuss any proposed changes to the Statement with British Airways Plc. However, the Trustee’s fiduciary obligations are to the Scheme’s members and these will take precedence over the Company’s wishes, should these ever conflict.
- 1.7. Further information about the Scheme can be found on the Scheme’s publicly accessible website.

## 2 Governance

- 2.1. The Trustee has established, as a sub-committee of the Main Board, an Investment Committee (the "IC") to focus on investment matters. The Trustee has appointed Mercer Limited as the Investment Advisor to provide relevant advice to the IC and the Trustee. The Trustee also takes advice as appropriate from the Scheme Actuary and other professional advisors. Two Independent Investment Experts also attend IC meetings to provide support, expertise and input to the discussions.
- 2.2. The Trustee is accountable for the investment of the Scheme's assets. The Trustee has delegated some aspects of the Scheme's investment arrangements to the IC, the Scheme's Trustee Executive, British Airways Pension Services Limited ("BAPSL") and the Scheme's Investment Manager, British Airways Pension Investment Management Limited ("BAPIML"), in order to manage the Scheme's affairs effectively. The Trustee decides what to delegate after considering whether it has the necessary skills, knowledge and professional support to make informed and effective decisions itself. The Trustee maintains and regularly reviews a strategic plan for the Scheme that sets out the investment (and other) activities planned for the next year and beyond.
- 2.3. The Trustee retains direct responsibility for setting investment objectives, establishing risk and return targets and setting the Scheme's investment manager structure. The Trustee makes these decisions after considering recommendations from the IC. The IC then implements them under delegated powers as set out in the Terms of Reference for the IC.
- 2.4. The NAPS Trust Deed does not specifically exclude any form of investment or investment activity although the Trustee does restrict the types of asset that BAPIML may hold and the type and extent of investment activity which it is permitted to undertake. Assets may be UK or overseas in origin and consist predominantly of investments admitted to trading on regulated markets and where they are not, are kept to a prudent level. Investments in derivative instruments and the use of leverage may only be made in so far as they contribute to a reduction of risks or facilitate efficient portfolio management.
- 2.5. BAPIML is responsible for the day-to-day management of the Scheme's assets in accordance with the guidelines agreed with the Trustee and set out in the Investment Management Agreement ("IMA") and ISF. BAPIML has discretion to buy, sell or retain individual investments in accordance with these guidelines. The Trustee regularly monitors the performance of BAPIML, looking at factors including return and risk measures as well as operational matters.
- 2.6. The safe custody of the Scheme's assets is delegated to professional custodians (either directly or via the use of pooled vehicles). The custodians are also responsible for performing associated duties such as dividend collection and independent calculation of investment performance. The managers of the pooled funds are responsible for the appointment and monitoring of the custodians. For the Scheme's direct investments, State Street Bank & Trust Co is the appointed custodian.
- 2.7. The Scheme Actuary performs a valuation of the Scheme 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 Scheme. Full details of the current funding strategy and contributions payable will be found in the Statement of Funding Principles, Recovery Plan and Schedule of Contributions.

## 3 Investment Objectives

- 3.1. The Trustee's primary investment objective is to invest the Scheme's assets in such a manner that members' benefit entitlements can be paid as and when they fall due.
- 3.2. The Trustee is aiming to achieve a funding level of 100% by 2030 measured on a long-term funding target ("LTFT") basis, currently defined as using a discount rate of gilts plus 0.50% pa.
- 3.3. The Trustee has agreed to move towards the LTFT through a long-term dynamic de-risking framework.
  - 3.3.1. Time based de-risking will be implemented over time at a rate of broadly 3% of assets being moved from the Return Seeking portfolio to the Liability Matching portfolio each year until 2030.
  - 3.3.2. Funding level based de-risking looks to reduce the level of risk taken from the Scheme's assets as the LTFT funding level improves over time. The Trustee will use the funding level as calculated by third party valuation software for the purposes of measuring against de-risking triggers. The de-risking triggers currently in place are set out in the Scheme's ISF. Upon breach of a de-risking funding level trigger, the Scheme's assets will be repositioned to accelerate the de-risking plan by one year.
- 3.4. The Trustee will continue to monitor the appropriateness of the de-risking framework and the path towards the LTFT and will revisit this approach, should it be necessary to do so.

## 4 Risk and Return

- 4.1. In order to meet the LTFT, the Trustee has agreed to take some investment risk relative to the liabilities. This taking of investment risk targets a greater return than that which the Liability Matching assets would be expected to provide whilst maintaining a prudent approach to meeting the Scheme's liabilities. The Trustee has adopted a de-risking approach to reduce the level of investment risk over time and help protect material improvements in the funding position when they are achieved.
- 4.2. In taking investment risk relative to the liabilities, the Trustee received advice from the Investment Advisor and Scheme Actuary and held discussions with the Company. In particular, the Trustee considered carefully the following possible consequences:
  - 4.2.1. The assets might not achieve the excess return anticipated relative to the liabilities (as measured on the LTFT basis) over the longer term. This would result in deterioration in the Scheme's financial position and potentially higher contributions from the Company than are currently expected.
  - 4.2.2. 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 likelihood of there being a shortfall of assets relative to the liabilities in the event of discontinuance of the Scheme. This consequence is particularly serious if it coincides with the Company being unable to make good the shortfall.
  - 4.2.3. The volatility in the relative value of assets and liabilities may also increase the short-term volatility of the Company's contributions set at successive actuarial valuations.
- 4.3. The Trustee's willingness to take investment risk is dependent on the continuing financial strength of the Company and its willingness to contribute appropriately to the Scheme when required. The financial strength of the Company and its perceived commitment to the Scheme is monitored and the Trustee will consider reducing investment risk relative to the liabilities should either of these deteriorate.
- 4.4. The degree of investment risk the Trustee is willing to take also depends on the financial health of the Scheme and the Scheme's liability profile. The Trustee will monitor these with a view to altering the investment objective, risk tolerance and/or return target should there be a significant change in either.
- 4.5. Having regard to the above factors, and after taking advice from the Investment Advisor and Scheme Actuary, from time to time the Trustee sets a target risk level for the assets held relative to the matching assets and a corresponding target return.
- 4.6. In addition to targeting an appropriate overall level of investment risk, the Trustee seeks to spread risks across a range of different sources. The Trustee aims to take on those risks for which the Trustee expects to be rewarded over time, in the form of excess returns. The Trustee believes that diversification limits the impact of any single risk. The Trustee will select a combination of assets and investment management approaches to be consistent with its investment objective, risk tolerance and return target.
- 4.7. Management of investment risk is principally addressed by the Trustee establishing investment parameters in the IMA and ISF, within which BAPIML must operate and, where appropriate, the explicit and systematic inclusion of environmental, social and governance ("ESG") issues in investment analysis and decisions.
- 4.8. The Trustee has identified the following key risks attaching to the Scheme's investments and has taken appropriate steps to mitigate these risks:
  - 4.8.1. Liability Risk exists if the projected cashflow profile of the assets held differs from that of the projected liabilities. The Trustee has a policy of increasing the proportion of invested assets that match the projected liabilities over time and targets interest rate and inflation risk being substantially hedged by 2030 (achieved through physical assets and derivative contracts).

- 4.8.2.** Longevity Risk reflects the possibility that the value of the Scheme's liabilities will increase due to improving life expectancy. The Trustee monitors this longevity risk and periodically considers reducing this risk through hedging subject to attractive pricing.
- 4.8.3.** Counterparty (or Credit) Risk reflects the possibility that payments due or expected from a third party are not made. Management of Counterparty Risk is delegated to BAPIML and BAPSL within certain limits set out in the ISF.
- 4.8.4.** Currency Risk will arise through investment in non-Sterling assets, given that the Scheme's liabilities are denominated in Sterling. Subject to maintaining certain minimum currency hedging requirements, management of currency risk is delegated to BAPIML.
- 4.8.5.** Liquidity Risk concerns the risk arising from holding assets that are not readily realisable be compounded by Volatility Risk where the price achievable is not certain until the point of sale. The Trustee's policy is to ensure that an adequate proportion of sufficiently realisable investments is held to meet additional cashflow requirements in most foreseeable circumstances and to achieve this it delegates the management of cashflow requirements to BAPSL.
- 4.8.6.** Regulatory Risk arises from investing in a market environment where the regulatory regime may change. The Trustee receives regulatory updates from its various advisors and considers how to address any significant changes as and when they arise.
- 4.8.7.** Concentration Risk arises when a high proportion of the Scheme's assets are invested in instruments of the same or related issuers. The Trustee seeks to diversify instruments appropriately to mitigate this risk and specific concentration limits are set out in the ISF.
- 4.8.8.** ESG Risk arises from investing in assets exposed to ESG related matters, including climate change, which could have a material negative impact on the asset's value. The management of ESG related risks is delegated to BAPIML. Section 7 of this Statement sets out the Trustee's responsible investment and corporate governance policy.
- 4.9.** BAPIML is an active manager and the Trustee will regularly review its beliefs in relation to active and passive management, considering whether active management offers sufficient potential to outperform to justify the additional risks and fees compared with passive management. The risks the Trustee will take into account include:
- 4.9.1.** Active risk in that the combination of assets held will differ from the benchmark and may give rise to underperformance relative to passive management.
- 4.9.2.** Tracking error risk in that a passive approach may not track the benchmark index within an appropriate degree of accuracy.
- 4.9.3.** Manager selection risk due to the potential for selecting (or failing to de-select in a timely manner) an active manager that fails to generate sufficient return in excess of the benchmark to justify the active risk taken and the higher fees charged than for passive management.



## 5 Investment Strategy

5.1. The Trustee has adopted a strategy with the aim of generating sufficient investment returns to achieve the Scheme's investment objectives, taking into account the risks and potential returns identified above. Should there be a material change in the Scheme's circumstances, the Trustee will review whether and to what extent the investment strategy should be altered.

5.2. The investment strategy takes account of:

5.2.1. The maturity profile of the Scheme (in terms of the relative proportions of liabilities in respect of pensioners and non-pensioners);

5.2.2. The funding level on the LTFT; and

5.2.3. The assessed strength of covenant provided by the Company.

5.3. The current strategic asset allocation as at 31 March 2020 is broadly as follows. Full details of the Scheme's current benchmark are set out in the ISF.

Asset Class	Benchmark Allocation	Tolerance Ranges
Return Seeking Assets	44.5%	+/-5.0%
Liability Matching Assets	55.5%	+/-5.0%

5.4. The Return Seeking portfolio is allocated to a range of asset classes (including public and private equity, property and alternatives) and, through the use of active management, it is intended that an additional return over a passive investment is generated in an efficient manner (i.e. such that expected returns are maximised relative to expected risk). The Trustee delegates the design of the Return Seeking portfolio to the IC.

5.5. The Liability Matching portfolio is a low risk portfolio relative to the liabilities and consists of real assets, government bonds, corporate bonds, diversified illiquid income funds and derivatives. Its primary aim is to broadly match movements in the value of the liabilities caused by interest rate and inflation changes. The Trustee delegates the design of the Liability Matching portfolio to the IC.

5.6. The Trustee has established tolerance ranges to keep the asset distribution broadly in line with the strategic benchmark and, consequently, to manage the risk of unintended asset exposures. The Trustee aims to manage cashflows efficiently and to keep the Scheme's assets within the intended ranges. The Trustee delegates responsibility of asset rebalancing and cashflow management to BAPIML.



## 6 Appointment and Monitoring of Investment Managers

- 6.1. BAPIML is the appointed Investment Manager of the Scheme and its primary objective is to assist the Trustee in achieving its long-term objective of being 100% funded on the LTFT by 2030. It is appointed on a fully-discretionary basis under which it has delegated responsibility for buying and selling investments on behalf of the Scheme, subject to agreed constraints as set out in the IMA, ISF and relevant legislation. BAPIML may invest in instruments directly or invest in pooled funds managed by other investment managers.
- 6.2. However the assets are managed, the Trustee will take appropriate legal and investment advice regarding the initial and ongoing suitability of the investment management documentation and the investment vehicles. When BAPIML is not operating under a discretionary agreement, the Trustee will obtain written advice from the Investment Advisor regarding the suitability of the chosen funds before making the initial investment. The Trustee will then obtain renewed advice at appropriate intervals while the Trustee continues to invest in the funds.
- 6.3. BAPIML's appointment is indefinite however, the Trustee will assess the continuing suitability of BAPIML, for example by periodic cost-benefit analysis of running BAPIML compared with use of an external asset manager(s).
- 6.4. The CIO of BAPIML (or other BAPIML representative) will regularly attend IC meetings to discuss BAPIML's performance, portfolio activity and wider issues. The Investment Advisor will be asked to assist the Trustee's Executive, BAPSL, in monitoring BAPIML. The Trustee will monitor BAPIML's performance over different time horizons against their performance objectives but will focus on the long-term.
- 6.5. BAPIML is owned in equal shares by the Trustee and Airways Pension Scheme Trustee Limited ("APSTL"). The Chair of the NAPS Trustee sits on the BAPIML Board and participates in remuneration decisions (as does the Chair of the APS Trustee). Remuneration of BAPIML's employees is derived as a result of both quantitative and qualitative factors that reflect the objectives of the Scheme and the Airways Pension Scheme ("APS") and is partially deferred to reflect the long-term time horizon of these objectives. The factors include asset performance (including over the medium to long term), contribution to progress towards the LTFT and implementation of the Trustee's Responsible Investment ("RI") policy as set out in Section 7. Ultimately the budget of BAPIML has to be approved by both the Trustee and APSTL each year.
- 6.6. The Trustee has ultimate responsibility for decision-making on investment matters and has agreed that all strategic policy decisions on investments will be taken by the Main Trustee Board after in-depth consideration by the IC and following receipt of appropriate advice.
- 6.7. Nevertheless, the IC has delegated authority to amend, supplement or delete any of the controls, restrictions or guidelines contained within BAPIML's IMA and ISF (with the exception of those classed as strategic policy decisions) and to monitor BAPIML's investment performance and operations against these documents.
- 6.8. The Trustee monitors portfolio turnover and turnover costs on an annual basis through reporting from BAPIML. This includes looking at the level of turnover and the associated costs in absolute terms and relative to various comparators.

## 7 Responsible Investment (“RI”) and Corporate Governance

- 7.1. The Trustee has produced the following Mission Statement setting out how the Scheme plans to address RI issues:

*“Environmental (including climate change), social and governance (ESG) issues are multifaceted and represent long-term systemic risks.*

*We recognise that ESG risks are financially material and need to be managed as we have a long-term payment horizon. We therefore seek to integrate ESG considerations into our decision-making and reporting processes across all asset classes.*

*Where consistent with our fiduciary duties, and applicable to our investment strategy, we will actively engage and use our voting rights to drive up ESG standards in the organisations in which we invest.”*

- 7.2. Full detail of the Trustee’s RI Policy can be found on the members’ website and does not form part of this Statement. The RI Policy will be subject to regular review.
- 7.3. BA Pensions is currently a signatory to the Carbon Disclosure Project and BAPIML is a member of the International Corporate Governance Network and a signatory to the UK Stewardship Code. The Trustee will regularly review the affiliations of the Scheme.
- 7.4. The Trustee has established an ESG Committee to make recommendations on the RI Policy and strategy for the Scheme as well as to oversee the RI activities of BAPIML.
- 7.5. The Trustee has given BAPIML responsibility for integrating ESG considerations into the investment decision-making process, with support from BAPIML’s specialist ESG team and other advisors where appropriate.
- 7.6. The Trustee expects BAPIML to, where possible, integrate financially material ESG considerations into the investment decision-making processes at a portfolio level, at asset level, across all asset classes and at all stages throughout the entire investment life-cycle including in the selection, retention and realisation of investments.
- 7.7. BAPIML is required to evidence consideration of ESG factors at each stage of the investment life-cycle and is expected to use a variety of RI tools and data sources to inform the decision-making process. The tools will be reviewed regularly to ensure they remain up-to-date and relevant.
- 7.8. The Trustee requires BAPIML to, where consistent with the Trustee’s fiduciary duties and applicable to the Scheme’s investment strategies, actively engage and use voting and other rights attached to the Scheme’s investments to drive up ESG standards in the organisations in which the Scheme is invested.
- 7.9. The Trustee requires BAPIML to engage with investee companies and other relevant stakeholders, using a variety of means including collaboration with other investors, to protect or enhance the value of the Scheme’s assets including over the medium to long term. Engagement can be in relation to a number of matters including, but not limited to, performance, strategy, risks, capital structure and management of actual or potential conflicts of interests. Engagement also aims to bring about change to the investee company’s ESG practices and performance. BAPIML is required to keep records of each engagement and outcome.
- 7.10. Depending on the severity of the issue, potential impact on performance and likelihood of success, BAPIML has various courses of action to follow should an investee company fail to make progress on ESG issues raised within a reasonable length of time. In extreme circumstances, failure to make progress may result in a decision taken to divest from the investee company.
- 7.11. In exercising the voting and other rights attached to the Scheme’s investments, BAPIML is required to consider recommendations on voting from specialist service providers but may follow an alternative course of action based on their informed view of the investee company and knowledge of the issue.

- 7.12. BAPIML is required to proactively monitor investments on an on-going basis to help identify a situation where long-term risk-adjusted returns may be compromised by ESG issues or could place the reputation of the Scheme at risk.
- 7.13. The Scheme's RI activities, annual voting and engagement reports will be made available on a publicly accessible website.
- 7.14. The Trustee and BAPIML have processes in place to continuously learn from practices and experiences.
- 7.15. The Trustee does not currently take into account the views of members and beneficiaries in respect of non-financial matters, including environmental and social issues.
- 7.16. In considering RI and applying the RI policy the Trustee will adhere to the law and latest UK regulation.

## 8 Additional Voluntary Contributions (“AVCs”)

- 8.1. The Trustee has full discretion as to the vehicles made available for members’ AVCs and the British Airways Money Purchase Scheme (“BAMPS”). Only investment vehicles that are considered suitable for AVC investment are considered by the Trustee, having taken appropriate advice.
- 8.2. The Trustee reviews the investment arrangements and performance of the AVC arrangements on a regular basis and takes advice regarding their ongoing suitability.

## 9 Review of this Statement

- 9.1. The Trustee does not expect to update this Statement frequently as it covers broad principles. However, the Trustee will review this Statement at least every three years and without delay if there are changes to the legislative framework or if there are relevant, material changes to the Scheme and/or the Company.
- 9.2. Any change to this Statement will only be made after having obtained and considered the written advice of the Investment Advisor and after consultation with the Company.

Signed on behalf of the Trustee of the New Airways Pension Scheme