

Statement of Investment Principles for the Siemens Healthineers Benefits Scheme SHL Section

10 July 2019

1. Introduction

This Statement of Investment Principles (“SIP”) sets out the policy of the Trustees (“the Trustees”) of the Siemens Healthineers Benefits Scheme (“the Scheme”) on various matters governing decisions about the investments of the SHL Section (“the Section”), a Defined Benefit (“DB”) Scheme.

The SIP is designed to meet the requirements of Section 35 (as amended) of the Pensions Act 1995 (“the Act”), the Occupational Pension Schemes (Investment) Regulations 2005 (as amended) and the Pension Regulator’s guidance for defined benefit pension schemes (March 2017).

This SIP has been prepared after obtaining and considering written professional advice from LCP, the Scheme’s investment adviser, whom the Trustees believe to be suitably qualified and experienced to provide such advice. The advice takes into account the suitability of investments including the need for diversification, given the circumstances of the Section, and the principles contained in this SIP. The Trustees have consulted with the relevant employers in producing this SIP.

The Trustees will review this SIP from time to time and, with the help of their advisers, will amend it as appropriate. These reviews will take place as soon as practicable after any significant change in investment policy, and at least once every three years.

Appendix 1 sets out details of the respective key responsibilities of the Trustees, investment advisers and investment managers. It also contains a description of the basis of remuneration of the investment adviser and the investment managers.

2. Investment objectives

The Trustees’ primary objectives are that:

- the Section should be able to meet benefit payments as they fall due; and
- the Section’s funding position (ie the value of its assets relative to the assessed value of its liabilities) should remain at an appropriate level. The Trustees are aware that there are various measures of funding and have given due weight to those considered most relevant to the Section. In particular, the Trustees have taken into account the funding requirements detailed in the Occupational Pension Schemes (Scheme Funding) Regulations 2005.

The Trustees’ investment objective is to maximise the return on the Section’s assets whilst managing and maintaining investment risk at an appropriate level, and taking into account the primary objectives.

3. Investment strategy

The Trustees, with the help of their advisers and in consultation with the employer, reviewed the investment strategy in May 2019, taking into account the objectives described in Section 2 above.

The result of the review was that the Trustees agreed that the investment strategy of the Section should be based on the strategic benchmark allocation shown in the table below.

Asset class	Strategic benchmark allocation (%)
UK equities	10.0
Overseas equities	10.0
Diversified growth fund ("DGF")	15.0
Short duration buy and maintain credit	25.0
Liability Driven Investment ("LDI") and cash	40.0
Total Section assets	<u>100.0</u>

The Section's assets are all invested in pooled investment funds. There is no formal rebalancing policy between investment managers. The Trustees monitor the position from time to time and consider with their advisers whether it is appropriate to rebalance the asset allocation, taking into account factors such as market conditions and anticipated future cash flows.

4. Considerations made in determining the investment arrangements

When deciding how to invest the Section's assets, the Trustees consider a number of risks, including, but not limited to, those set out in Appendix 2. Some of these risks are more quantifiable than others, but the Trustees have tried to allow for the relative importance and magnitude of each risk.

The Trustees considered a wide range of asset classes for investment, taking account of the expected returns and key individual risks associated with those asset classes as well as how these risks can be mitigated where appropriate.

The strategy review included modelling the Section's assets and liabilities over a wide range of possible scenarios for future economic conditions. In setting the strategy, the Trustees considered:

- the Section's investment objectives;
- the characteristics of the projected liability cash flows;
- a wide range of asset classes;
- 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 (please see Appendix 2 for further details of the key risks considered by the Trustees);
- the best interests of members and beneficiaries;
- the circumstances of the Section, 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 need for appropriate diversification between different asset classes to ensure that both the Section's overall level of investment risk and the balance of individual asset risks are appropriate;
- any other considerations which the Trustees consider financially material over the time horizon that the Trustees consider is needed for the funding of future benefits by the investments of the Section; and

- the Trustees' investment beliefs about how investment markets work, and which factors are most likely to impact investment outcomes.

The key financial assumption made by the Trustees in determining the investment arrangements is that equity-type investments will, over the long term, outperform gilts by 5.0% pa. The key long-term assumptions underlying our investment adviser's model as at 31 March 2019 for expected returns above gilts, were as follows:

Asset class	Expected excess return over gilts (% pa)
UK equities	5.0
Overseas equities	5.0
Diversified growth	3.0
Short duration buy and maintain credit	1.0
Dynamic LDI	1.0
Money market cash	0.0

The expected return assumptions for gilts and cash are updated daily based on observed market yields.

The assumptions above are set to be best estimates; this means that for each assumption there is a 50/50 chance that the observed value will either be higher, or lower than assumed.

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

- asset allocation is the primary driver of long-term returns;
- 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;
- investment markets are not always efficient and there may be opportunities for good active managers to add value;
- environmental, social and governance (ESG) factors may be one area of market inefficiency and so managers may be able to improve risk-adjusted returns by taking account of ESG factors;
- investment managers who can consistently spot and profitably exploit market opportunities are difficult to find and therefore passive management, where available, can represent better value;
- long-term environmental, social and economic sustainability is one factor that trustees should consider when making investment decisions; and
- costs have a significant impact on long-term performance and therefore obtaining value for money from the investments is important.

5. Implementation of the investment arrangements

Before investing in any manner, the Trustees obtain and consider proper written advice from their investment adviser on the question of whether the investment is satisfactory, having regard to the need for suitable and appropriately diversified investments.

Details of the investment managers are set out in Appendix 3.

The Trustees have signed agreements with the investment managers setting out in detail the terms on which the portfolios are to be managed. The investment managers' primary role is the day-to-day investment management of the Section's investments. The managers are authorised under the Financial Services and Markets Act 2000 (as amended) to carry out such activities.

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

6. Realisation of investments

The investment managers have discretion over the timing of realisation of investments of the Section within the portfolios that they manage, and in considerations relating to the liquidity of investments. When appropriate, the Trustees, on the administrators' recommendation, decide on the amount of cash required for benefit payments and other outgoings and inform the investment managers of any liquidity requirements.

7. Consideration of financially material and non-financial matters

The Trustees have considered how social, environmental, governance ("ESG") and ethical factors should be taken into account in the selection, retention and realisation of investments, given the time horizon of the Section and its members.

The Trustees expect their investment managers to take account of financially material considerations (including climate change and other ESG considerations). The Trustees seek to appoint managers that have appropriate skills and processes to do this, and from time to time reviews how their managers are taking account of these issues in practice.

The Trustees have limited influence over managers' investment practices where assets are held in pooled funds, but they encourage their managers to improve their practices where appropriate.

The Trustees do not take into account 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.

8. Stewardship

The Trustees recognise their responsibilities as owners of capital, and believe 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 Trustees have delegated to their 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, risks and ESG considerations.

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The Trustees do not monitor or engage directly with issuers or other holders of debt or equity. They expect 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 Trustees from time to time, taking into account the long-term financial interests of the beneficiaries. The Trustees seek 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 Trustees review how these are implemented in practice.

SIP signed for and on behalf of the Trustees of the SHL Section of the Siemens Healthineers Benefits Scheme:

Signed:

The Trustees have decided on the following division of responsibilities and decision-making for the Section. This division is based upon the Trustees' understanding of the various legal requirements placed upon it, and its view that this division allows for efficient operation of the Section overall, with access to an appropriate level of expert advice and service. The Trustees' investment powers are set out within the Section's governing documentation.

1. Trustees

In broad terms, the Trustees are responsible in respect of investment matters for:

- developing a mutual understanding of investment and risk issues with the employer;
- setting the investment strategy, in consultation with the employer;
- formulating a policy in relation to financially material considerations, such as those relating to ESG considerations (including but not limited to climate change);
- reviewing the investment policy as part of any review of the investment strategy;
- setting the policy for rebalancing between asset classes;
- setting a policy on the exercise of rights (including voting rights) and undertaking engagement activities in respect of the investments;
- putting effective governance arrangements in place and documenting these arrangements in a suitable form;
- appointing (and, when necessary, dismissing) investment managers, investment advisers, actuary and other service providers;
- monitoring the exercise of the investment powers that they have delegated to the investment managers and monitoring compliance with Section 36 of the Act;
- communicating with members as appropriate on investment matters, such as the Trustees' assessment of its effectiveness as a decision-making body, the policies regarding responsible ownership and how such responsibilities have been discharged;
- reviewing the investment policy as part of any review of the investment strategy;
- reviewing the content of this SIP from time to time and modifying it if deemed appropriate; and
- consulting with the employer when reviewing the SIP.

The Trustees have delegated consideration of certain investment matters to an investment sub-committee ("ISC"), and the Trustee and ISC understand the different areas where each party makes decisions, provides oversight or recommendations. The terms of reference for the ISC detail clearly its responsibilities.

2. Investment managers

In broad terms, the investment managers will be responsible for:

- managing the portfolios of assets according to their stated objectives, and within the guidelines and restrictions set out in their respective investment manager agreements and/or other relevant governing documentation;

- taking account of financially material considerations (including climate change and other ESG considerations) as appropriate when managing the portfolios of assets;
- exercising rights (including voting rights) attaching to investments and undertaking engagement activities in respect of investments;
- providing the Trustees with regular information concerning the management and performance of their respective portfolios; and
- having regard to the provisions of Section 36 of the Act insofar as it is necessary to do so.

The custodians of the portfolios (whether there is a direct relationship between the custodian and the Trustees or not) are responsible for safe keeping of the assets and facilitating all transactions within the portfolios.

3. Investment adviser

In broad terms, the investment adviser will be responsible, in respect of investment matters, as requested by the Trustees, for:

- advising on how material changes within the Section's benefits, membership, and funding position may affect the manner in which the assets should be invested and the asset allocation policy;
- advising on the selection, and review, of the investment managers; and
- participating with the Trustees in reviews of this SIP.

4. Fee structures

The Trustees recognise that the provision of investment management and advisory services to the Section results in a range of charges to be met, directly or indirectly, by deduction from the Section's assets.

The Trustees have agreed Terms of Business with the Section's actuarial and investment advisers, under which work undertaken is charged for by an agreed fixed fee or on a "time-cost" basis.

The investment managers receive fees calculated by reference to the market value of assets under management. The fee rates are believed to be consistent with the managers' general terms for institutional clients and are considered by the Trustees to be reasonable when compared with those of other similar providers.

The fee structure used in each case has been selected with regard to existing custom and practice, and the Trustees' view as to the most appropriate arrangements for the Section. However, the Trustees will consider revising any given structure if and when it is considered appropriate to do so.

5. Performance assessment

The Trustees are satisfied, taking into account the external expertise available, that there are sufficient resources to support their investment responsibilities. The Trustees believe that they have sufficient expertise and appropriate training to carry out their role effectively.

It is the Trustees' policy to assess the performance of the Sections investments, investment providers and professional advisers from time to time. The Trustees will also periodically assess the

6. Working with the Scheme's employer

When reviewing matters regarding the Section's investment arrangements, such as the SIP, the Trustees seek to give due consideration to the employer's perspective. While the requirement to consult does not mean that the Trustees need to reach agreement with the employer, the Trustees believe that better outcomes will generally be achieved if the Trustees and employer work together collaboratively.

Risk appetite and risk capacity

Risk appetite is a measure of how much risk the Trustees' are willing to bear within the Section to meet their investment objectives. Taking more risk is expected to mean that those objectives can be achieved more quickly, but it also means that there is a greater likelihood that the objectives are missed, in the absence of remedial action. Risk capacity is a measure of the extent to which the Trustees can tolerate deviation from their long-term objectives before attainment of those objectives is seriously impaired. The Trustees aim is to strike the right balance between risk appetite and risk capacity.

When assessing the risk appetite and risk capacity, the Trustees considered a range of qualitative and quantitative factors, including:

- the strength of the employer's covenant and how this may change in the near/medium future;
- the agreed journey plan and employer contributions;
- the Section's long-term and shorter-term funding targets;
- the Section's liability profile, its interest rate and inflation sensitivities, and the extent to which these are hedged;
- the Section's cash flow and target return requirements; and
- the level of expected return and expected level of risk (as measured by Value at Risk ("VaR"), now and as the strategy evolves.

Approach to managing and monitoring investment risks

The Trustees consider that there are a number of different types of investment risk that are important for the Section. These include, but are not limited to:

1. Risk of inadequate returns

A key objective of the Trustees is that, over the long-term, the Section should have adequate assets to meet its liabilities as they fall due. The Trustees therefore invest the assets of the Section to produce a sufficient long-term return in excess of the liabilities. There is also a risk that the performance of the Section's assets and liabilities diverges in certain financial and economic conditions in the short term. This risk has been taken into account in setting the investment strategy and is monitored by the Trustees on a regular basis.

2. Risk from lack of diversification

This is the risk that failure of a particular investment, or the general poor performance of a given investment type, could materially adversely affect the Section's assets. The Trustees believe that the Section's assets are adequately diversified between different asset classes and within each asset class. This was key consideration when determining the Section's investment arrangements.

This is the risk that an investment manager fails to meet its investment objectives. Prior to appointing an investment manager, the Trustees receive written advice from a suitably qualified individual, and will typically undertake an investment manager selection exercise. The Trustees monitor the investment managers on a regular basis.

4. Liquidity/marketability risk

This is the risk that the Section is unable to realise assets to meet benefit cash flows as they fall due. The Trustees are aware of the Section's cash flow requirements and believe that this risk is managed by maintaining an appropriate degree of liquidity across the Section's investments.

5. Environmental, social and governance (ESG) risks

Environmental, social and corporate governance (ESG) factors are sources of risk to the Section's investments, some of which could be financially material, over both the short and longer term. These potentially include risks relating to factors such as climate change, unsustainable business practices, and unsound corporate governance. The Trustees seek to appoint investment managers who will manage these risks appropriately on their behalf and from time to time review how these risks are being managed in practice.

6. Collateral adequacy risk

The Section is invested in leveraged Liability Driven Investment ("LDI") arrangements to provide protection ("hedging") against adverse changes in interest rates and inflation expectations. The LDI manager may from time to time call for additional cash to be paid to the LDI portfolio in order to support a given level of leverage. Collateral adequacy risk is the risk that the Trustees when requested to do so will not be able to post additional cash to the LDI fund within the required timeframe. A potential consequence of this risk is that the Section's interest rate and inflation hedging could be reduced and that the Section's funding level could suffer subsequently as a result. In order to manage this risk, the Trustees ensure that the Section has a sufficient allocation to cash and other highly liquid assets which can be readily realised, so that cash can be posted to the LDI manager at short notice.

7. Credit risk

This is the risk that one party to a financial instrument will cause a financial loss for the other party by failing to discharge an obligation.

The Section invests in pooled funds and is therefore directly exposed to credit risk in relation to the solvency of the investment manager and custodian of those funds.

This risk is mitigated by the underlying assets of the pooled arrangements being ring-fenced from the investment managers, the regulatory environment in which the investment managers operate and diversification of the Section's investments amongst a number of pooled arrangements. The Trustees, with the help of their advisers, carry out due diligence checks on the appointment of any new investment manager or fund, and monitor for changes to the operating environment of the existing pooled funds.

The Section is indirectly exposed to credit risks arising from the underlying investments, where they invest in bonds and other assets of a contractual nature. The indirect exposure to credit risk arises from the Section's short duration buy and maintain credit fund and DGF investments.

The managers of the pooled funds typically manage credit risk by having a diversified exposure to bond issuers, by considering the probability of default of those issuers, and having only limited exposure to bonds rated below investment grade. The magnitude of credit risk within each fund will vary over time, as the manager changes the underlying investments in line with its views on markets, asset classes and specific bonds.

Within the LDI portfolio, there is exposure to credit risk as BMO uses derivatives instruments. The terms under which the LDI portfolio is managed include provisions to manage the exposure to credit risk, such as limits on the exposure to any single counterparty and minimum credit ratings that all counterparties must meet. In addition, the derivative positions are collateralised daily, so as to limit credit risk to one day's market movements.

8. Currency risk

This is the risk that the fair value or future cash flows of a financial asset will fluctuate because of changes in foreign exchange rates. As the Section's liabilities are denominated in Sterling, any non-Sterling currency exposure within the assets presents additional currency risk.

Whilst the majority of the currency exposure of the Section's assets is to Sterling, the Section is subject to currency risk because some of the Section's investments are held in overseas markets. The Trustees consider the overseas currency exposure in the context of the overall investment strategy, and believe that the currency exposure that exists diversifies the strategy and is appropriate.

9. Interest rate and inflation risk

These are the risks that the fair value or future cash flows of a financial asset will fluctuate because of changes in market interest rates and inflation expectations.

The Section's assets invested in the BMO LDI funds are subject to interest rate and inflation risk and the assets invested in BlackRock's short duration buy and maintain credit funds are subject to interest rate risk. However the overall exposure hedges part of the corresponding risks associated with the Section's liabilities. The net effect will be to reduce the volatility of the funding level, and therefore the Trustees believe that it is appropriate to have exposure to these risks in this manner.

10. Other price risk

This is the risk that the value of an asset will fluctuate due to changes in market prices (other than those arising from the risks above), whether those changes are caused by factors specific to the individual financial instrument or its issuer, or factors affecting similar financial instruments.

This risk will vary depending on the particular market / asset class invested in and the Trustees monitor it on a regular basis, looking at the performance of the Section as a whole as well as each individual portfolio. The Trustees believe that the Section's assets are adequately diversified between different asset classes and within each asset class to manage this risk.

11. Other non-investment risks

The Trustees recognise that there are other, non-investment, risks faced by the Section, and takes these into consideration as far as practical in setting the Section's investment arrangements.

Examples include:

- longevity risk (the risk that members live, on average, longer than expected); and
- sponsor covenant risk (the risk that, for whatever reason, the sponsoring employer is unable to support the Section as anticipated).

Together, the investment and non-investment risks give rise generally to funding risk. This is the risk that the Section's funding position falls below what is considered an appropriate level. By understanding and considering the key risks that contribute to funding risk, the Trustees believe they have appropriately addressed and are positioned to manage this general risk.

Page 13 of 15 Details of the investment managers, their objectives, investment guidelines and custody arrangements are set out below.

1. Legal & General Investment Management (“L&G”) – passive equity

The Trustees have selected L&G as the investment manager for the Section’s passive equity portfolio. The benchmark indices for the funds and the strategic allocation are set out in the table below.

Asset class	Benchmark index	Strategic allocation (%)
Total Equities		100.0
UK Equities	FTSE All-Share	50.0
Overseas Equities		50.0
US Equities	FTSE AW Developed North America	17.0
Europe (ex-UK) Equities	FTSE AW Developed Europe (ex-UK)	17.0
Japanese Equities	FTSE AW Japan	8.0
Pacific Basin Equities	FTSE AW Developed Asia Pacific (ex-Japan)	8.0

All funds are priced daily. The funds are open-ended and unlisted. L&G is responsible for the custody of the assets of the funds. The Trustees do not have a direct relationship with the custodian.

2. Fulcrum Asset Management (“Fulcrum”) – diversified growth

The Trustees have selected Fulcrum as one of the investment managers for the Section’s diversified growth fund allocation. The fund is managed on an active basis. The fund is not managed with reference to a particular benchmark. The performance objective for the fund is as follows:

Fund	Performance objective
Diversified Core Absolute Return Fund	To achieve long-term absolute returns of inflation + 3% - 5% in all market conditions over rolling five-year annualised periods, with lower volatility than equity markets.

The fund is priced daily. The fund is open-ended and is unlisted.

Fulcrum is responsible for custody of the assets of the fund. The Trustees do not have a direct relationship with the custodian.

3. BlackRock International Limited (“BlackRock”) – diversified growth and short duration buy and maintain credit

The Trustees have selected BlackRock as one of the investment managers for the Section’s diversified growth fund allocation and as the investment manager for the Section’s short duration buy and maintain credit allocation. The performance objectives for the funds are as follows:

Fund	Performance objective
Dynamic Diversified Growth Fund	To outperform UK 3-month LIBOR by 3% pa over rolling three-year periods (after the deduction of fees).
Sterling Short Duration Credit Strategy	To outperform UK 3-month LIBOR by 1.5% pa over rolling three-year periods (before the deduction of fees).

The funds are priced daily. The funds are open-ended and unlisted. The Trustees have appointed the Bank of New York Mellon (“BNY Mellon”) as custodian for the Section’s investments with BlackRock. The Trustees therefore have a direct relationship with the custodian.

4. BMO Global Asset Management plc (“BMO”) – LDI and cash

The Trustees have selected BMO as an investment manager for the Section’s LDI and cash portfolios. The LDI element consists of investments in BMO’s Real Dynamic LDI Fund and Nominal Dynamic LDI Fund. The cash element consists of an investment in BMO’s Sterling Liquidity Fund. The benchmarks and performance objectives for the funds are as follows:

Fund	Benchmark index	Performance objective
BMO Real Dynamic LDI Fund	Liability hedging benchmark based on cash flows of a generic UK pension scheme	To provide a hedge against real rate liabilities
BMO Nominal Dynamic LDI Fund	Liability hedging benchmark based on cash flows of a generic UK pension scheme	To provide a hedge against nominal rate liabilities
BMO Sterling Liquidity Fund	7-day Sterling LIBID	Maintain high levels of liquidity, preserve capital and generate a return in line with the benchmark

The Real Dynamic LDI Fund and Nominal Dynamic LDI Fund are priced weekly and at month end. The Sterling Liquidity Fund is priced daily. The funds are open-ended and are unlisted.

BMO is responsible for custody of assets of the funds. The Trustees do not have a direct relationship with the custodian.

The strategic benchmark allocation to the LDI and cash is 40% of the total Section assets. Given the nature of the investments BMO does not have a fixed benchmark allocation and hence does not carry out any automatic rebalancing between the pooled funds, except when LDI deleveraging or releveraging events occur.

The allocations to the BMO funds have been determined based on the following principles:

- the LDI allocation has been set with reference to the target interest rate and inflation hedging level of 80% of the Section's liabilities (measured on a Technical Provisions basis);
- the allocation to cash has been set with reference to the expected amount required to top up the LDI fund in the event of a deleveraging event, plus an additional amount to cover the Section's near-term future cashflow requirements.

In a **deleveraging event** (when the value of the LDI fund falls to the extent that the capital required to support the hedge needs to be topped up) BMO will disinvest from the Sterling Liquidity fund to top up the LDI Fund.

In a **releveraging event** (when the value of the LDI fund increases to the extent that there is too much capital supporting the hedge) BMO will invest cash proceeds from the LDI fund into the Sterling Liquidity fund.

The Trustees will monitor the allocation to LDI and cash over time and will consider with their advisers whether it is appropriate to rebalance the portfolio, taking into account factors such as market conditions, the target hedging levels and any cash requirements.

5. Custodian

The role of a custodian is to ensure safe keeping of the assets and facilitate all transactions in respect of the portfolios for which it provides custody. The Trustees have appointed BNY Mellon to provide custody services for the Section's investments with BlackRock.

The remaining assets of the Section are invested in pooled funds where the investment manager is responsible for appointing a custodian. As such, the Trustees are not required to select a custodian for the assets invested in these funds.