Xylem UK Pension Plan

Statement of Investment Principles

This document is the Statement of Investment Principles (the 'Statement') for the Xylem UK Pension Plan (the 'Plan').

Background information on this Statement

This Statement has been drawn up by the Trustee of the Xylem UK Pension Plan (the 'Trustee'). It sets out the principles governing investment decisions made by the Trustee in relation to the Plan.

This Statement should be read in conjunction with the related document entitled 'Investment Arrangements' which provides further detail on how the investment decisions are implemented. The Statement is also a legal requirement of the Pensions Acts 1995 and 2004, and the Occupational Pension Schemes (Investment) Regulations 2005 as amended (collectively referred to as the 'Pensions Acts'). For the avoidance of doubt the Investment Arrangements document does not legally comprise part of the Statement.

In preparing this document the Trustee has taken into account the requirements of the Pensions Acts. In addition this Statement is designed to fulfil the spirit of the pensions industry Code of Best Practice, published in 2001. The principles set out in this Statement are also consistent with the Trustee's Statement of Funding Principles.

Contents of this Statement

The Statement covers the following principles:

1. Governance arrangements
2. Investment objectives
3. Key risks affecting the Plan
4. General investment policies
5. Agreeing and reviewing this Statement

1. Governance arrangements

Overview of the arrangements

The Trustee has ultimate responsibility for the management of the investment arrangements of the Plan and its assets. In discharging these responsibilities, the Trustee has established clear Investment Objectives setting out what they are aiming to achieve. The Investment Objectives relate to the overall solvency position of the Plan and are explained in more detail in the next section of this Statement. The solvency position is an assessment of the amount of assets which have been put aside to meet the liabilities of the Plan.

Other parties involved

There are a number of parties involved in the Plan's investment arrangements namely:

- Trustee
- Investment Committee, when convened
- Scheme Actuary
- Investment managers
- Providers of direct investments

Responsibility and knowledge

The Trustee has ultimate responsibility for the management of the Plan and its assets. The Trustee has agreed the overall investment objective, permissible assets, investment strategies, derivative usage and guidelines for the assets.

The Trustee confirms that all parties to whom it delegates responsibility have the appropriate knowledge and experience required to take on this role. The Trustee expects each party to carry out the duties so delegated with a view to giving effect to the principles in this Statement, so far as is reasonably practical.

2. Defined Benefit Section

a) Investment objectives

The Trustee's aim is to provide sufficient assets to pay benefits as they fall due. The Trustee has set an objective for the Plan's investments in order to achieve this. This is called the 'Investment Objective'. To this end, the Trustee, in consultation with the Scheme's sponsoring employer, Xylem Water Solutions UK Limited, has selected Rothesay Life plc (the 'Insurance Provider') to provide a buy-in policy for the Scheme. This policy is designed to meet all members' benefit payments as they fall due.

The Trustee and the sponsoring employer have implemented a buy-in policy with Rothesay Life. It is expected that the buy-in policy will be converted into a buy-out policy within the next two years (the 'Buy-out Objective'). At that point, the responsibility for meeting members' benefits will be transferred from the Trustee to the Insurance Provider.

In the meantime, the Trustee retains overall responsibility for reviewing the ongoing operation of and risks associated with the buy-in policy. This includes, but is not limited to, the Insurance Provider's ongoing credit quality and the timeliness and accuracy of payments made to the Plan.

b) Key risks affecting the Plan

The key risk to the Plan is that the value of assets is insufficient relative to the value of the liabilities. This is called solvency risk and ultimately could lead to there being insufficient assets to secure all benefits.

There are many other individual risk factors which have the potential to contribute to solvency risk. Due to the complex and interrelated nature of these risks, the Trustee considers these in a qualitative rather than a quantitative manner in accordance with regulatory requirements.

In practice, these risks are minimised through the execution of the buy-in policy which requires the Insurance Provider to meet benefit payments as they fall due; and the laws that regulate the Insurance Provider and provide protection for policyholders.

As the Trustee retains overall responsibility for ensuring member benefits are met until the Buy-out Objective is achieved, its primary risk focus is now on the credit quality of the Insurance Provider. The Trustee measures and manages this risk (and the other risks relating to the Buy-out Objective) through professional covenant, actuarial / consulting and legal advice and through the terms of the buy-in policy and the expected buy-out.

Other risk factors

There are a number of other risks affecting the Plan. These risks and the Trustee's policy on how each risk should be managed and measured is shown below:

Risk factor	What is the risk?	How is this measured?	How is this managed?
Sponsor risk	The sponsoring employer does not/cannot make sufficient contributions to support the payment of the Plan benefits. With the buy-in policy in place, this will be relevant if the Insurance Provider becomes insolvent	The Trustee considers the ability and willingness of the sponsor to support the continuation of the Plan if the Insurance Provider becomes insolvent	The Trustees are looking to manage this risk via a buy out. Trustees are aware of the risk and continue to monitor this in the interim period between buy-in and buy out with the Insurance Provider
Liquidity risk	There is a shortfall in liquid assets relative to the Plan's immediate cashflow requirements.	The Trustee monitors the level of cashflow required on a regular basis.	The Trustees will manage this through the buy-in policy, members' benefits will be matched by the premiums due to the Plan under the policy

c) General investment policies

The Trustee has set a number of investment policies in relation to their investments. These cover:

- Balance between investment types
- Expected return on investments
- Realisation of investments
- Responsible investment & corporate governance
- Arrangements with Investment Managers
- Ensuring compliance with the Pensions Acts
- Fee basis for service providers

Balance between investment types

The need to maintain an appropriate balance between different kinds of investments must now be considered in the context of the Buy-Out Objective and the selection of the buy-in policy.

Expected return on investments

The nature of the buy-in policy is such that its expected return is equal to the change in value of the member benefits covered.

Realisation of investments

The intention of the Trustee is to hold the buy-in policy until it is converted to a buy-out within the next two years.

3. Defined Contribution Section

The Defined Contribution Section (also known as the 'Money Purchase Section') arrangements consist of:

- Original Xylem Plan assets, consisting of market-linked funds held with Legal & General Investment Management
    - Including a Default Fund (also known as the 'Standard Investment Programme')
- Ex - C&K Switches Ltd Pension Plan assets (which merged with the Xylem Plan during 2017), including:
    - Clerical Medical Market-linked funds managed by Aberdeen Standard; and
    - With-profits funds managed by Aviva and Phoenix Life

The assets of the Default Fund are invested in a range of different funds at different points in time. Members also have the option to select from a range of funds, where the return achieved will depend on their selection. These funds include a balanced fund (investing across a range of asset classes), a global equity fund, a bond fund, and a cash fund.

The Default aims to provide exposure to a range of asset classes in order to deliver investment growth over time, gradually de-risking to protect the value of members' account against stock market fluctuations as members approach retirement.

Highest growth is targeted, with a corresponding level of potential volatility of the capital value, in the period up to 15 years before a member's expected retirement age. As a member gets closer to retirement, assets are gradually switched into less volatile holdings, which are also expected to provide lower investment returns.

Number of years before expected retirement age	Fund Type
Over 15 years	Global Equity
Between 5 -15 years	Multi Asset Fund
Less than 5 years	Gradually switched into a Bond and a Cash Fund

a) Investment objectives

The Trustee is responsible for investing the DC assets in line with members' preferences. Their key investment objective is to provide a range of investments that are suitable for meeting members' long and short-term investment objectives allowing for members' differing individual circumstances. In particular, the range of members' attitudes to risk and term to retirement are considered.

Strategy

The Trustee's policy is to provide suitable information to members so that they can make appropriate investment decisions. The Trustee is currently reviewing their DC provision as part of a wholesale Plan review. In choosing investment options, it is the Trustee's policy to consider:

- A full range of asset classes
- The suitability of the possible styles of investment management and the need for manager diversification
- The suitability of each asset class
- The need for appropriate diversification of asset classes

Where a member does not wish to make a decision, the Trustee offers a Standard Investment Programme (the 'Default Fund').

The assets of the Default Fund are invested in a range of different funds at different points in time. Members also have the option to select from a range of funds, where the return achieved will depend on their selection. These funds include a balanced fund (investing across a range of asset classes), a global equity fund, a bond fund, and a cash fund.

The Default Fund aims to provide exposure to a range of asset classes in order to deliver investment growth over time, gradually de-risking to protect the value of members' account against stock market fluctuations as members approach retirement.

Highest growth is targeted, with a corresponding level of potential volatility of the capital value, in the period up to 15 years before a member's expected retirement age. As a member gets closer to retirement, assets are gradually switched into less volatile holdings, which are also expected to provide lower investment returns.

b) Risk management

The Trustee considers the following sources of risk:

- Member understanding – the risk that the Trustee does not provide clear, balanced and timely information to members to aid their understanding. The Trustee is aware that poor information could lead to members' reasonable expectations not being met
- Investment practices – the risk that the range of funds does not meet members' requirements. The range of funds is monitored for both suitability and competitiveness on an ongoing basis
- Risk of default funds, where provided, being unsuitable for the requirements of some members
- Manager risk - risk of fund managers not meeting their objectives. This risk is considered by the Trustee and its advisers both upon the initial appointment of the fund manager and on an ongoing basis thereafter
- The risk of fraud, poor advice or acts of negligence ("operational risk"). The Trustee has sought to minimise such risk by ensuring that all advisers and third party service providers are suitably qualified and experienced and that suitable liability and compensation clauses are included in all contracts for professional services received

Due to the complex and interrelated nature of these risks, the Trustee considers these risks in a qualitative rather than quantitative manner as part of each formal strategy review. The Trustee's policy is to review the range of funds offered and the suitability of its approach to a default strategy on a regular basis.

These risks are considered as part of each normal strategy review. In addition, the Trustee measures risk in terms of the performance of the assets compared to the benchmarks on a regular basis (at least annually) along with monitoring any significant issues with the fund manager that may impact their ability to meet the performance targets set by the Trustee.

4. General Investment Policies for both Sections

Responsible investment & corporate governance

Financially material considerations over the appropriate time horizon of the investments

The Trustee considers responsible investment to be the integration of environmental, social and governance considerations into investment decisions in respect of the Plan's investment portfolio where financial risk and / or return is or could be materially affected ("Responsible Investment"). The Trustee acknowledges the importance of being a responsible investor, however, as the Trustee is aiming to buy out the Plan's liabilities with an insurer in the short term they do not expect Responsible Investment considerations to have a significant impact on the Plan's assets over this timeframe.

The Plan Defined Benefit assets are now substantially invested in an insurance policy. The Defined Contribution assets are held in pooled arrangements and the Trustee expects investment managers to take into account environmental, social and governance considerations (including but not limited to climate change) when making investment decisions where financial risk and / or return is, or could be, materially affected.

The Trustee takes account of environmental, social and governance considerations in investment decision making and periodically monitors how the investment managers take account of Responsible Investment.

The extent to which non-financial matters are taken into account in the selection, retention and realisation of investments

The Trustee does not take the views of the members and beneficiaries, including (but not limited to) their views in relation to governance, social and environmental impact, into account when making investment decisions. However, the Trustee believes that by being a responsible investor, they are managing investment risk with the aim of enhancing long term portfolio returns, which is in the best interests of the members and beneficiaries of the Plan.

The exercise of the rights (including voting rights) attaching to the investments

The Trustee's policy is to delegate responsibility for the exercising of rights (including voting rights) attaching to investments to the investment managers. The Investment Adviser encourages the Plan's investment managers to discharge their responsibilities in respect of investee companies in accordance with the Stewardship Code published by the Financial Reporting Council.

Undertaking engagement activities in respect of the investments

Where relevant, the Trustee prefers their investment managers to have an explicit strategy, outlining the circumstances in which they will engage with a company (or issuer of debt or stakeholder) on relevant matters (including performance, strategy, capital structure, management of actual or potential conflicts of interest, risks, social and environmental impact and corporate governance matters) and how they will measure the effectiveness of this strategy.

The Investment Adviser is responsible for engaging with investment managers regarding their voting records and level of engagement with the underlying investments, where this is expected to have meaningful impact and affect financial risk and / or return.

Arrangements with Investment Managers

The Trustee believes that an understanding of, and engagement with, investment managers' arrangements is required to ensure they are aligned with Trustee's policy, including its Responsible Investment policy. In accordance with latest regulation, the Trustee's policy covers the following areas:

Incentivising investment managers

The Trustee monitors investment managers' performance against the investment strategies and objectives of the Plan.

The fees paid to the investment managers and the possibility of their mandates being terminated ensure they are incentivised to provide a high quality service that meets the stated objectives, guidelines and restrictions agreed with the Trustee.

Assessing medium to long-term performance of investments

Investment managers are appointed based on their capabilities and, therefore, their perceived likelihood of achieving the expected return and risk characteristics required for the asset class being selected. The underlying investment managers are aware that their continued appointment is based on their success in delivering the mandate for which they have been appointed to manage. Investment managers are appointed on an ongoing basis which helps to incentivise them to focus on medium to long term performance.

Monitoring performance and remuneration

The Trustee receives performance reports from its Investment Adviser on a quarterly basis, which present performance information over three months, one year, and three years. The Trustee reviews absolute and relative performance against suitable indices or targets. Whilst the Trustee focuses on long-term performance, it also takes shorter-term performance into account.

If an underlying manager is not meeting performance objectives, or their investment objectives have changed, the Trustee will review the suitability of the manager, and change managers where required. As managers are remunerated based on the level of assets managed, there is a direct interest for investment managers to perform in line or ahead of targets in order to retain mandates and continue to receive compensation on an ongoing basis.

Monitoring portfolio turnover and costs

The Trustee does not currently define target portfolio turnover ranges for investment managers. However, the Trustee considers portfolio turnover costs indirectly through consideration of overall costs incurred throughout the year (including all manager fees and expenses), provided within reports the Trustee receives annually.

Duration of arrangements with investment managers

The majority of investment vehicles are open-ended, with no set end date for the arrangements. An investment manager's appointment may be terminated due to a change in the overall investment strategy or changes in expectations of their ability to deliver against the agreed mandate or in line with the investment policies of the Trustee.

Compliance with the Pensions Acts
The Pensions Acts distinguish between investments which are purchased directly by the Trustee (‘direct investments’) and investments where management is delegated to an investment manager under a written contract. An example of the former would be the purchase of an insurance policy by the Trustee (e.g. additional voluntary contributions policies), where there is no investment management agreement.

When deciding whether to make any new direct investments, the Trustee will obtain written advice from their Investment Adviser. It will also consider whether future decisions about those investments should be delegated to an investment manager.

The Trustee’s policy is to review its direct investments and to obtain written advice about them at regular intervals.

This written advice will cover the issues set out in the Pensions Acts and the principles contained in this Statement.

It is the Trustee’s policy to regularly monitor and review the practices of any investment manager appointed by the Trustee under the Pensions Acts to ensure that the Trustee’s powers of investment are being exercised in accordance with the Pensions Acts, and with a view to giving effect to the principles in this Statement as far as practicable. If the Trustee becomes aware that any manager is not carrying out its duties in accordance with the Pensions Acts or this Statement, they will promptly review this situation with the investment manager.

Additional Voluntary Contributions (AVCs)

The Trustee has made available various investment vehicles for the investment of AVCs, consistent with the fund options offered to members of the DC section. The Trustee acknowledges the same specific risks and objectives apply to AVC members as apply to DC section members.

Fee basis for service providers
The Trustee uses a range of fee arrangements which may include performance related fees, fees as a percentage of the assets managed and fixed fees.

5. Agreeing and reviewing this Statement

Advice received

The Trustee has obtained written advice on the content of this statement from their Investment Adviser. They will also take written advice on any future major changes to this Statement.

The Trustee is satisfied that the Investment Adviser has the knowledge and experience required by the Pensions Acts to perform this role.

Consultation

The Trustee has consulted the sponsoring employer, Xylem Water Solutions UK Limited, on the content of this Statement and will consult with them on future changes.

Compliance and review

The Trustee will monitor compliance with this Statement regularly and in any event will review this Statement at least every three years and also following any significant change in investment policy.

APPENDIX A – Investment responsibilities of different parties

The division of investment responsibilities for the Plan is set out below. This list is not meant to be exhaustive.

Trustee

The Trustee has ultimate responsibility for decision-making on investment matters. The Trustee's investment responsibilities include:

- Deciding on an appropriate governance structure for the management of the Plan including the role of advisers and other third parties
- Setting appropriate investment objectives, following advice from the Investment Adviser and Scheme Actuary
- Agreeing the range of investment types to be used to achieve the investment objectives, taking account of the need to manage risks
- Agreeing the policies for governing investment manager arrangements
- Monitoring the Plan's compliance with the pensions industry's Code of Best Practice
- Reviewing the content of this Statement at least every three years and following any significant change in investment strategy
- Modifying this Statement, if deemed appropriate, in consultation with the sponsoring employer and with written advice from the Investment Adviser
- Monitoring compliance with this Statement on an ongoing basis

Investment Committee, when convened

The Trustee has the ability to delegate to an Investment Committee, should it be deemed appropriate. The Investment Committee's responsibilities could include:

- Identifying the training needs of its members and the members of the Trustee who are not also on the Investment Committee, on an annual basis
- Considering and making recommendations to the Trustee in relation to strategic investment issues including investment objectives, risk tolerance and investment guidelines
- Monitoring the Investment Adviser and making recommendations to the Trustee on the replacement or appointment of the Investment Adviser
- Considering and making recommendations to the Trustee in relation to changes in AVC providers
- Taking certain decisions on behalf of the Trustee, to the extent delegated to them by the Trustee and as set out in the Investment Committee Terms of Reference

When an Investment Committee is not being utilised, the Trustee retains direct responsibility for the above.

Investment Adviser (Cardano Risk Management Limited)

The Investment Adviser's role includes providing investment advice to the Trustee. A summary of the duties that fall into this category are shown below:

- Advice on setting the Investment Objective

- Advice and monitoring of the DC and AVC arrangements and other direct investments, excluding the buy-in policy
- Trustee investment training and education
- Advice relating to investment governance and compliance
- Advice on this Statement
- Advice relating to potential conflicts of interest, including their own

Scheme Actuary (Kevin Davey, FIA of Mercer)

The key aspects of the Scheme Actuary's role that have a bearing on investment decisions include:

- Liaising with the Investment Adviser on the suitability of the Plan's Investment Objective given the liabilities of the Plan
- Ensuring consistency between the Statement of Funding Principles and the Trustee's Investment Objectives and investment strategy
- Assessing the funding ratio of the Plan by performing valuations and advising on the appropriate contribution levels
- Estimating the cashflows of the Plan, to be used in the calculation of the value of liabilities
- Advice relating to potential conflicts of interest, including their own

Investment managers

The investment managers' responsibilities include:

- Managing the assets delegated to them within the terms of their agreement
- Providing regular reports on their performance, including any agreed benchmark and performance targets
- Instructing their custodian on corporate governance and voting issues, including issues relating to Socially Responsible Investment
- Ensuring that they are complying with the requirements applicable to them in this Statement. In particular, when investing the assets delegated to them they must be invested in the best interests of members and beneficiaries. Their powers of investments must be exercised so as to ensure the security, quality, liquidity and profitability of the portfolio as a whole

Providers of direct investments

Investments held directly by the Plan are held in the form of units in pooled funds or in the form of insurance policies. The responsibilities of the providers are set out in the relevant documentation. There is then usually an agreement between the provider and an organisation which manages the assets underlying the direct investment on a day-to-day basis. This agreement sets out the responsibilities of this organisation to the provider.

Before investing, the Trustee obtains and considers advice from a suitably qualified investment adviser. This advice considers the overall suitability of the investments in relation to a number of key investment principles.