PDN
Pensioenfonds DSM Nederland

PDN Investment Beliefs (March 2018)

Financial markets

1. A return on investments is needed to achieve adequate pension results for members. An investment return implies accepting risks.

Why? Pension contributions only finance a part of the full pension ambition. The Fund therefore needs additional financing, which it expects from investment returns, for which it is necessary to run the corresponding risks. Investors in equities and corporate bonds, for example, run an investment risk and are rewarded accordingly. Due to the volatility of the risk premiums and the mutual correlations, diversification across the various risk sources and investment categories is essential.

Consequence: To fulfil the objective of the pension fund, the required return and the extent to which risks must be taken need to be determined. The adoption of the strategic investment policy, including the choice and size of investment categories to be used, is the starting point for this purpose.

2. As a long-term investor, PDN can earn additional risk premiums on illiquid investments.

Why? Part of the pension fund's invested capital can be illiquid because the pension fund is a long-term investor and the payment of its commitments are spread and planned over time. Due to the long investment horizon, the pension fund can profit from the available risk premiums.
Consequence: PDN allocates part of the capital to illiquid investments.

3. Diversifying investments across different investment categories can reduce investment risks. Unless it is contrary to other investment beliefs, no investment category is excluded in advance.

Why? Given that correlations are generally lower than 1, the risk profile of the total investment portfolio can be reduced by combining investment categories.

Consequence The investment portfolio consists of different investment categories whose mutual correlations are lower (than 1) in the long term.

4. Although the value of investments fluctuates, the return tends towards an average value in time.

Why? Capital markets are unpredictable and risk premiums can vary over a longer period (three to five years). In the longer term, the nominal interest, for example, tends to be compensation for real economic growth, supplemented by an inflation component. In relation to the risk premiums, this compensation for additional risk is realized in the longer term.

Consequence: Through temporary deviations from the long-term average, additional returns can be achieved by granting tactical policy latitude.

<u>Governance</u>

5. The investment policy is tailored to the members' pension result

<u>Why</u>? To be able to pay all pensions, now and in the future, the pension fund must have sufficient capital in relation to its commitments. For this reason, the Board tailors the investment policy to the nature and extent of the pension fund commitments (including the indexation ambition).

<u>Consequence:</u> The strategic investment policy is determined by means of ALM analyses, for which purpose the total balance serves as input. Additions and changes to investment categories are not evaluated in isolation but in conjunction with the entire balance sheet.

6. Members' confidence is essential for the Fund. The investment portfolio must be transparent and clear, the investment decisions that have been made must be easy to explain, and the costs must be justifiable.

<u>Why</u>? The building blocks of the investment portfolio must be understood by the Board and its supervisory bodies and be easy to explain to the members. The Board should not spend disproportionate time and capacity on one investment category, mandate, or position and excessive use of external expertise, for example in the legal or tax area, should be avoided.

<u>Consequence:</u> The pension fund assesses the existing strategic investment policy and policy adjustment proposals based on complexity and the ease with which these can be explained. The investment costs must fit within the parameters set by the Board for this purpose.

7. Management and administration have the same objective. This is ensured via a strategic partnership with a private administration organization.

<u>Why</u>? It is important that the policy and its implementation are properly aligned and there are no conflicts of interest. This is achieved through a strategic partnership with a private administration organization that operates on a non-profit basis. High-quality and integrated services benefit from insight and knowledge in the area of strategic advice, fiduciary management, and portfolio management.

<u>Consequence:</u> PDN uses DSM Pension Services as its integral services provider. External service providers are engaged if DPS lacks knowledge or cannot provide adequate quality in certain areas. External managers may be selected for the portfolio management of certain parts of the investment portfolio.

<u>Investment process</u>

8. The strategic investment policy largely determines the return to be achieved and the corresponding risk.

<u>Why</u>? The main investment choice that the Fund makes is determining its strategic investment policy. By spreading the investment categories and their risk sources, the overall risk can be reduced without this being to the detriment of the anticipated return. The Board therefore devotes a great deal of attention to compiling the strategic investment policy.

<u>Consequence:</u> Adjustments to the strategic investment policy will be assessed on the added value at total portfolio level via portfolio construction. Accordingly, investments will be added only if they can be easily explained and have sufficient minimum weight within the investment portfolio to have a clear added value at portfolio level.

9. Active management can be worthwhile

Why? Taking active positions in relation to standard weighting can be worthwhile because:

- *Markets can overreact, and the Fund can capitalize on this*
- *Benchmarks lead to herd behavior and inefficient positioning*
- *As a long-term investor, the Fund has the opportunity to 'ride out' a situation*

Consequence: The Board provides an active risk budget to exploit the above inefficiencies. This can be done through Tactical Asset Allocation and active management within the mandates. The Board determines whether an investment category or overlay is filled actively or passively.

Sustainability

10. Integrating sustainability contributes to the long-term objectives of the Fund and its members

Why? In the Fund's opinion:

- *sustainability is a form of long-term risk management, for risks that are not financial and can contribute as such to the Fund's objectives;*
- *the integration of sustainability factors in the investment process ensures better investment decisions, by which the return/risk profile of the investment portfolio is expected to improve;*
- *open dialogue with the companies in which it invests contributes towards a financial and social return;*
- *it can effectively provide added value through targeted investment in specific sectors and themes linked to its members, and so make a difference for its members;*
- *there must be a drive towards greater transparency and visibility of the pension fund in the area of sustainable investment policy.*

Consequence: PDN has adopted a policy in the area of Socially Responsible Investments that consists of exclusions, transparency, corporate governance, ESG integration in mandates, and commitment.