Caterpillar Pension Plan – Annual Engagement Policy Implementation Statement

Introduction

This statement sets out how, and the extent to which, the Engagement Policy in the Statement of Investment Principles ('SIP') produced by the Trustee has been followed during the year to 30 September 2024. This statement has been produced in accordance with The Pension Protection Fund (Pensionable Service) and Occupational Pension Schemes (Investment and Disclosure) (Amendment and Modification) Regulations 2018 and the guidance published by the Pensions Regulator.

Investment Objectives of the Plan

The Trustee believes it is important to consider the policies in place in the context of the investment objectives they have set. The objectives of the Plan included in the SIP are as follows:

- To make sure that the Plan remains sufficiently funded to meet the expected obligations to the beneficiaries of the Plan, assuming that the Plan remains on-going and after making reasonable allowance for the Plan assets to deliver returns in excess of the least risk assets, i.e. gilts;
- To ensure that the Plan Sponsor's accounting cost is kept within a tolerable range from year to year.

Policy on ESG, Stewardship and Climate Change

The Plan's SIP includes the Trustee's policy on Environmental, Social and Governance ('ESG') factors, stewardship and Climate Change. This policy sets out the Trustee's beliefs on ESG and climate change and the processes followed by the Trustee in relation to voting rights and stewardship. This was last reviewed in November 2023 as part of a review of the SIP following the bulk annuity contract purchase from Aviva that took place in November 2023.

In order to establish these beliefs and produce this policy, the Trustee undertook investment training provided by the investment consultant on responsible investment. The training covered ESG factors, stewardship, climate change and ethical investing. The Trustee undertook further ESG beliefs training at the 26 November 2021 Investment Sub-Committee meeting. At this meeting, the Trustee's investment beliefs were discussed with the investment consultant to assist the Trustee in reviewing the policy in place. The ISC revisited the Plan's investment beliefs (as set out in the SIP) in advance of TCFD training provided in February 2023, and also developed a draft set of Responsible Investment ("RI") beliefs that draw on the policies used by the Plan's managers and take into account the views of the principal employer, Caterpillar (UK) Limited. The RI beliefs were finalised in 2023 alongside the ISC considering climate risk and the Plan's objectives in greater detail. As part of the consideration of climate risk, the ISC engages with the Plan's investment managers on the implementation of climate targets. Following consultation with the investment managers in 2024, trading was carried out to reduce the carbon intensity of the funds in which the Plan invests. The Trustee have also engaged with LGIM on accelerating the temperature alignment of their Buy & Maintain Credit portfolio with discussions ongoing on targeting alignment to 1.5 degrees by 2030.

The following work was undertaken during the year relating to the Trustee's policy on ESG factors, stewardship and climate change, and sets out how the Trustee's engagement and voting policies were followed and implemented during the year.

Engagement

As set out in the SIP, the Trustee has elected to invest the Plan's assets through segregated mandates and has specified criteria in the investment manager agreements for the asset class manager to invest in line with. The criteria align with the Trustee's specific investment requirements. This gives the Trustee the ability to directly influence levels of engagement.

In the year to 30 September 2024, the Trustee has not monitored or queried portfolio turnover costs. The Trustee focuses on net of fees outcomes from the managers which takes into account portfolio turnover costs through the performance generated.

The Trustee may choose to monitor portfolio turnover costs in the future.

Voting and Engagement policies and activities are most relevant for mandates where equities are held directly or indirectly. Given the Plan invests entirely in fixed income securities, a large portion of which are UK Government Debt, these policies are less applicable and only apply to a portion of the Plan's assets.

- A summary of LGIM's general approach to voting and engagement is provided below.
    - LGIM's direct engagement with companies is a way they seek to identify ESG risks and opportunities. On-going dialogue with companies is a fundamental aspect of LGIM's responsible investment commitment. LGIM aims to raise the performance of the whole market through their ESG capability and engagement of companies globally. LGIM believe that ESG issues are fundamentally important to investors regardless of the type of exposure, noting the majority of themes they engage on are relevant to bond investors. Therefore, LGIM explicitly take into account both debt and equity exposures when engaging on behalf of clients.

    - In the Buy & Maintain Credit portfolio, LGIM's team organises their engagement activities including voting across strategies and asset classes to ensure they speak to companies with one voice.

    - Across the companies within the LGIM portfolio, over the year to 30 September 2024, LGIM carried out 319 engagements, covering 57% of the portfolio value. An engagement example is set out below.

        - LGIM have engaged with global pharmaceutical company, Eli Lilly, who have developed successful drugs to treat diabetes with a side effect of significant weight loss, on the danger of drug misuse, and discussed their procedures and marketing and development. LGIM asked them to:
            - Work with appropriate charities to educate and raise awareness
            - Monitor social media
            - Emphasis BMI limits in adverts
            - Monitor excessive prescription by doctors and pharmacies.

          LGIM were happy to see Eli Lilly's public statement against the use of its drugs for cosmetic weight loss and continue to monitor.

    - In relation to the derivatives within the LDI portfolio, LGIM have confirmed they continue to view ESG as an essential component and integrate it into their approach via:

        - Governance: Engaging with many banks globally on a regular basis to discuss varied governance issues such as strategic direction, risk management, succession planning and board refreshment, social risks and other ESG topics.

        - LGIM also continue to engage with a number of market participants with regard to green gilt issuance.

- A summary of RLAM's approach to voting and engagement over the 12 month period to 30 September 2024 is provided below.

    - RLAM's engagement with issuers covers a number of ESG related matters, and over the year, topics included Climate change; Social & financial inclusion; Innovation, technology & society; Governance & corporate culture; Health; and Nature and biodiversity amongst others. RLAM engaged with 140 companies on 268 occasions spanning these topics. RLAM categorise engagements into two sections, "for information" and "for change and influence".

    - RLAM previously launched a net zero engagement program which included a systematic assessment of companies and their carbon transition plans in the previous year. 16 companies were engaged with in the final quarter of the year. An engagement example is included below for NatWest Group Plc, which is held within the Plan's portfolio.

        - NatWest Group Plc: RLAM engaged with NatWest as part of a collaborative engagement with banks to integrate just transition principles into their climate transition plans. NatWest initially expressed concerns about being evaluated solely on financial returns which it felt constrained its incentives for ESG activities. NatWest however recognised the value of aligning with RLAM's just transition investor expectations for the sector and found the guidelines beneficial in setting ambitious goals and taking subsequent actions. NatWest acknowledged the importance of integrating the principles into its plans to enhance credibility and were receptive to feedback from RLAM on improving communication around the issue.

- The investment performance report, produced by the Plan's investment consultant, is reviewed by the Trustee on a quarterly basis – this includes ratings (both general and ESG specific) from the investment consultant. Where managers are not highly rated from an ESG perspective, the Trustee has discussed the reasons with the investment consultant. The investment performance report includes how each investment manager is delivering against their specific mandates.

Voting Activity

The Trustee has delegated their voting rights to the investment managers. Where relevant, investment managers are expected to provide voting summary reporting on a regular basis, at least annually.

When the investment managers present to the Trustee, the Trustee or investment consultant may ask the investment managers to highlight key voting activity and will question managers' voting decisions if it deems them out of line with the investment fund's objectives or the objectives / policies of the Plan. The Trustee does not use the direct services of a proxy voter.

Over the prior 12 months, due to the nature of the securities that the Plan is invested in, there was no key voting activity to report.

Over the prior 12 months, the Trustee has not actively engaged with the Plan's managers on their voting activity due to the nature of the mandates in place. Going forwards, when investment managers present, the Trustee may be more active in reviewing and challenging voting activity where relevant, particularly in respect of its beliefs on climate change.