
# Scheme funding report

## Actuarial valuation of the Diageo Pension Scheme at 1 April 2021

| | |
|---|---|
| Prepared for: | The Directors of the Diageo Pension Trust Limited |
| Prepared by: | James Miller FIA |
| Date: | 21 February 2022 |

# Introduction

## Why bring you this report?

Section 224(2)a of the Pensions Act 2004 requires the Trustee to receive this formal report from me (as Scheme Actuary) setting out the results and conclusions from the actuarial valuation of your Scheme as at 1 April 2021.

My report summarises the key aspects of the valuation process, including:

- The funding objective and background details
- The technical provisions
- The corresponding future service costs
- The agreed contributions
- The results on the solvency basis.

Some further information is provided for compliance purposes.

- The legal framework within which the valuation has been completed
- A summary of the membership and asset data, the benefits valued and details of the assumptions used for the valuation
- My statutory certification of the technical provisions
- A glossary of some technical pensions terms

## Next steps

Some key deadlines are highlighted on the right.

The valuation process is complete when all the following have been agreed and are in place:

- This scheme funding report, including my certification of the technical provisions
- Schedule of contributions, including my actuarial certification of the adequacy of the schedule of contributions.

**21 February 2022**

**Signature** **Date**

### Key deadlines

**By 28 February 2022:** For the Trustee to provide a copy of this report to the Company within 7 days.

**By 7 March 2022:** The valuation summary must be submitted to The Pensions Regulator via Exchange.

**By 30 September 2022:** A summary funding statement must be provided to members within 18 months of the valuation date.

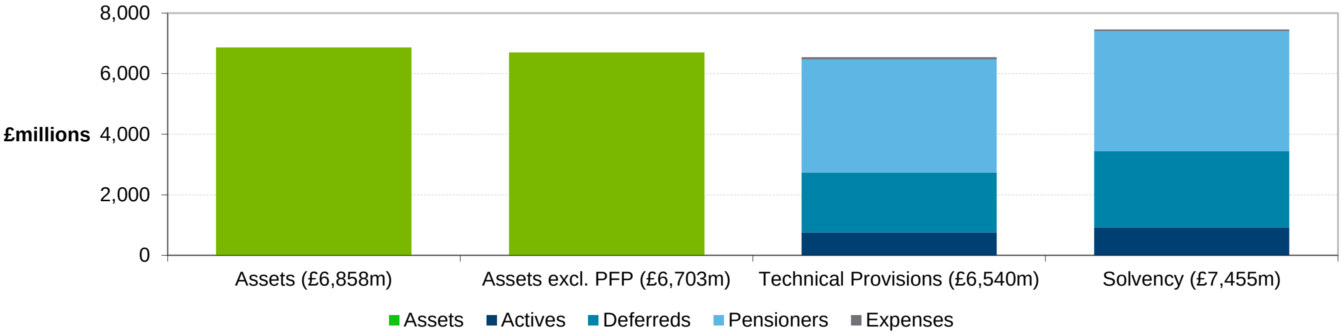
### The terms in this report

A summary of any 'shorthand' legal references and a glossary of key valuation terms can be found at the back of this report.

# At a glance…

As your Scheme Actuary, I have carried out an actuarial valuation of the Scheme at 1 April 2021.

## Funding summary




### Technical provisions

£318M

Surplus

### Solvency estimate

£752M

deficit

## Contributions

Following discussions, the Company will pay the following contributions to the Scheme for future accrual of benefits:

From 1 April 2021 to 31 March 2022: 38.25% of Pensionable Pay

From 1 April 2022 to 30 June 2025: 8.0% of Pensionable Pay

From 1 July 2025: 35.5% of Pensionable Pay

LESS any element met by member contributions for future accrual of benefits.

### Important

The report concentrates on the Scheme's financial position at the valuation date. As time moves on, the Scheme's finances will fluctuate.

If you are reading this report some time after it was produced, the Scheme's financial position could have changed significantly.

# Contents

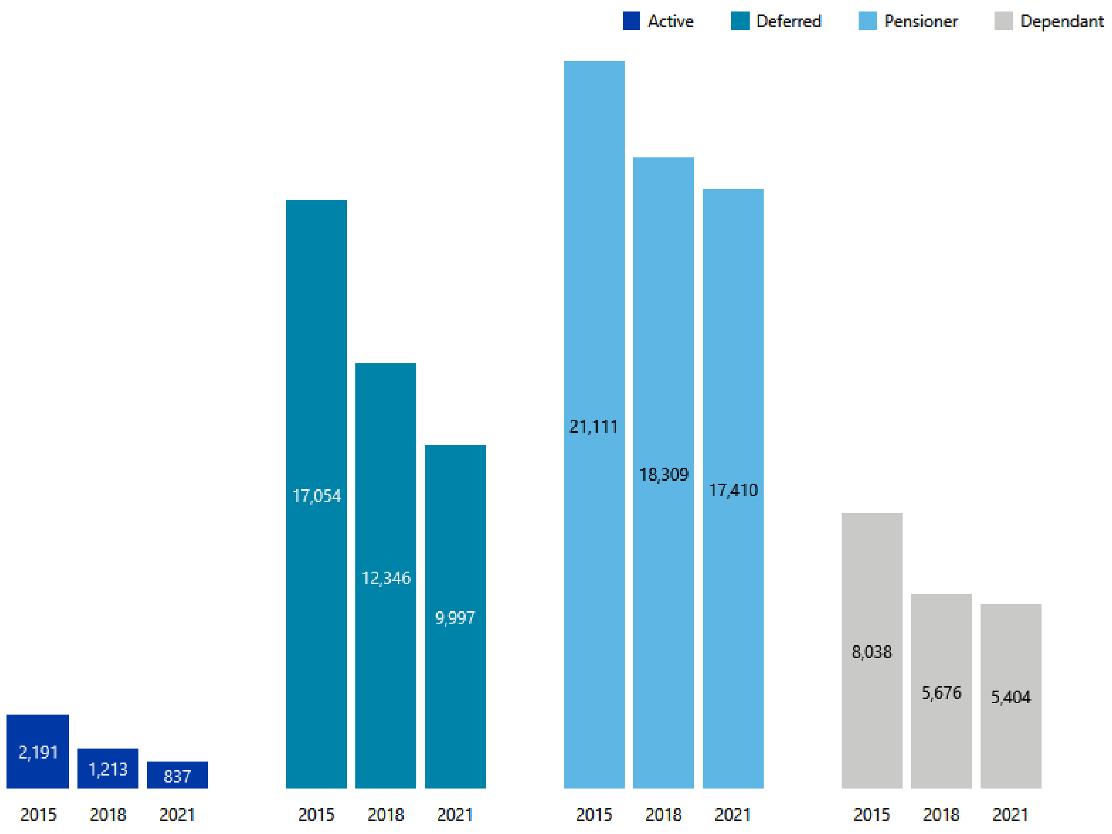

# Background to your actuarial valuation

# Data and benefits valued

Key information on the membership data used and benefits valued in the valuation are summarised here.

## Member data

The Scheme has continued to become increasingly mature with the proportion of pensioners increasing. The membership numbers are shown graphically below.




The membership data was provided by Capita. This was the first valuation where Capita have provided the data since the transition of administration from Diageo to Capita. There are some areas where the data is currently not complete. This is an area that the Trustee are working with Capita on. For the purpose of this valuation we have supplemented the data provided by Capita with historical data held by Aon. If full and complete data was available this may have led to results that are different from those set out in this report. However, I would not expect this to lead to different conclusions on the level of future contributions agreed as part of this valuation. Further details of the data can be found in an appendix.

## Benefits

Members are entitled to the benefits defined in the Rules. A summary of the benefits is included in the appendix.

### GMP equalisation

An approximate allowance for equalising GMPs has been made by adding 1% to the Scheme's technical provisions. This includes an approximate allowance for both past and future benefit payments.

This is consistent with the approach at the previous valuation.

### UURBS pensions

Some members' benefits payable from the Scheme are restricted either by Inland Revenue limits or to enable members to avoid a lifetime allowance charge. The amount of the restriction is not known until retirement, for this valuation the following approach has been adopted:

Members who have not yet retired

| | |
|---|---|
| Pre A-day leavers | No restrictions have been applied and all benefits have been valued in the Scheme |
| Post A-day leavers | A deduction has been applied based on the projected restriction assumed to apply at retirement. This deduction is applied to the member pension and the contingent spouse's pension |

### Discretionary benefits

The Scheme has a policy for paying discretionary increases to pensions in deferment on top of member's basic entitlements under the Rules. I have incorporated an allowance for the granting of these discretionary benefits.

I have also allowed for benefits on death to dependants who are not the spouse or civil partner of the deceased member.

Pensioners and Dependants

| | |
|---|---|
| Pre A-day leavers | The member and spouse's pension restriction has been determined at retirement |
| Post A-day leavers | The member's pension restriction has been determined at retirement, the contingent spouse's pension is all assumed to be payable from the Scheme |

### AVC and Insurance policies

For presentational simplicity, the assets for defined contribution AVC accounts are excluded from both the assets and from the liability measures. There are no insurance policies in place to provide any of the benefits of the Scheme.

# Funding objectives and investment strategy

The Trustee's funding objective is to hold assets which are at least equal to the technical provisions (i.e. to meet the statutory funding objective).

## Your funding target

The Trustee's funding objective is to be fully funded on the technical provisions basis.

The Trustee also has a longer-term aim to be fully funded by 31 March 2030 on a basis which would permit the Scheme, once fully funded, to have low dependency on the employer covenant for ongoing financial support thereafter. This is separate from the statutory funding objective and is not covered further in this report.

## Employer covenant

A key factor in setting the level of the technical provisions is the Trustee's assessment of the employer covenant. The Trustee has carried out a review of the employer covenant themselves and concluded that the covenant is strong. The covenant strength rating is similar to when assessed for the previous valuation and this has been taken into account in setting the assumptions to be adopted for the technical provisions and in agreeing the level of Company contributions.

## Investment strategy

The current assets are described in an appendix.

The Trustee's investment strategy is set out in its statement of investment principles.

In summary, the Trustee's benchmark strategy is to invest:

- 14% in growth assets such as private equity and property
- 38% in income assets such as bonds and loans
- 48% in protection assets such as gilts, swaps and cash

The benchmark asset allocation excludes the Pension Funding Partnership and AVC investments.

The Trustee has a liability hedging programme, designed to mitigate the impacts on the Scheme of changes in the rates of interest and inflation. At the valuation date this broadly hedges the movement of the technical provisions to movements in inflation and interest rates.

# Method & assumptions

The Trustee has agreed, after consulting the Company, the assumptions used to calculate the technical provisions and the cost of future benefit accrual. The table below summarises the key assumptions, together with those used for the previous valuation, and the reasons for any change.

## Method

As for the previous valuation, the technical provisions have been calculated using the projected unit method.

This method, with a three-year control period, has also been used to calculate the cost of future benefit accrual. This is the same control period as was adopted in the previous valuation.

The assets are valued at the audited value contained in the Trustee Report and Accounts for the year ended 31 March 2021. DC AVCs have been excluded in the main body of this report as the asset exactly matches the liability.

### Further information

Your Actuarial valuations handbook contains further information on valuation methods and Aon's approach to assumption setting.

## Assumptions

The table below summarises the key assumptions, together with those used for the previous valuation, and the reasons for any change.

Further details of all the assumptions are set out in the statement of funding principles dated 21 February 2022.

| Assumption | Previous valuation | This valuation | Rationale for change |
|---|---|---|---|
| Discount rate | UK Gilt yield curve plus 1.3% at April 2018 reducing linearly to 0.5% p.a. by April 2030 | UK Gilt yield curve plus 1.1% at April 2021 reducing linearly to 0.5% p.a. by April 2030 | No change |
| RPI inflation | Break-even inflation curve | Break-even inflation curve | No change |
| CPI inflation | RPI inflation assumption less 0.75% p.a. | RPI inflation assumption less 0.75% p.a. till February 2030 and RPI inflation assumption less 0.0% p.a. thereafter | Updated to reflect RPI reform from 2030 when RPI will equal CPIH |
| Salary inflation (excluding promotional increases) | RPI inflation assumption | RPI inflation assumption | No change |
| Post-retirement mortality assumption - base table | S2PMA and S2PFA tables with individual scaling factors | S3PMA and S3PFA_M tables with individual scaling factors | Updated to reflect the latest tables and the Scheme's pensioner mortality experience since the last valuation |
| Post-retirement mortality assumption - projection | CMI 2017 core projections with Sk of 8.0 and long-term improvement rate of 1.75% p.a. for men and women | CMI 2020 core projections with Sk of 7.0, 'A' parameter of +0.50% and a long-term improvement rate of 1.75% p.a. for men and women | Updated to reflect the latest research |


# Valuation results

# Past service results

The Scheme's technical provisions and resulting funding position have been calculated at 1 April 2021.

## Results

| | Technical provisions (£M) |
|---|---|
| Value of past service benefits for: | |
| ▪ Actives (including Hybrid members) | 757 |
| ▪ Deferreds | 1,977 |
| ▪ Pensioners | 3,741 |
| ▪ Expenses | 65 |
| Value of liabilities | 6,540 |
| Value of assets (incl. £155M PFP) | 6,858 |
| Past service surplus/(deficit) | 318 |
| Funding Level | 105% |

My formal certificate of your technical provisions is included in this report.

## Sensitivity of the funding level

The key assumptions are the discount and inflation rates. The sensitivity of the funding level to these key assumptions is as follows:

**Discount rate decreases by 0.25%**

A 0.25% pa decrease in the discount rate increases the technical provisions by £288M, reducing the funding level to 100% assuming no change to the assets.

**RPI inflation increases by 0.25%**

A 0.25% pa increase in the RPI inflation assumption (also allowing for the consequent impact on the assumptions derived directly from that assumption) increases the technical provisions by £192M, reduces the funding level to 102% assuming no change to the assets.

The Trustee and the Company agreed not to allow for post-valuation-date experience when setting the contributions in this valuation.

## Pension Funding Partnership contribution

The Scheme has a Pension Funding Partnership (PFP). Under the terms of the PFP, annual contributions are payable depending on the funding position of the Scheme on the technical provisions basis excluding the value of the PFP.

Deducting the £155M value of the PFP at 1 April 2021 leaves the Scheme with a £163M surplus at 1 April 2021 excluding the PFP. As a result of the Scheme being in surplus at 1 April 2021 (excluding the PFP), there is no contribution due in March 2022 under the PFP.

# Future service results

The table below shows the cost at the valuation date of benefits that members will earn in the Scheme in future.

## Results

This has been calculated using the same assumptions as for the technical provisions

| | % Pensionable Pay |
|---|---|
| Value of benefits accruing from 1 April 2021 (on 70ths CARE accrual) | 54.7% |
| Less member contributions | (8.0%) |
| Net cost to the Company | 46.7% |

## Cost capping mechanism

Under the Scheme's rules there is a cost capping mechanism. This means that as the results of this valuation have revealed a net cost to the Company which is outside of the range 24.75% to 30.25%, the CARE accrual rate from 1 April 2022 needs to be amended. The new accrual rate from 1 April 2022 is determined by first calculating what accrual rate would give a net cost of accrual to the Company of 27.5% and then rounding the accrual rate so the denominator is a whole number. As a result of the cost capping mechanism the CARE accrual rate will change to 108ths from 1 April 2022, unless the Company instead notifies the Trustee in writing of an increased accrual rate to be used. The cost of accrual of benefits from 1 April 2022 is as follows:

| | % Pensionable Pay |
|---|---|
| Value of benefits accruing (on 108ths accrual) | 35.6% |
| Less member contributions | (8.0%) |
| Net cost to the Company | 27.6% |

Please note that:

- The rates shown represent the cost of new benefit accrual, providing the death in service lump sum benefit and the cost of providing life cover to members who have either left the Scheme or commenced the payment of their pension, in both cases while continuing employment with the Company. No allowance has been made for administration expenses.
- The rates shown exclude localised members (who aren't earning new benefits in, or contributing to, the Scheme) and members aged over normal retirement age at the valuation date (who are assumed to retire on the valuation date).

## Sensitivity of the cost of future benefit accrual

The key assumptions are the discount and inflation rates. The sensitivity of the cost of post April 2022 benefit accrual to these key assumptions is as follows:

**Discount rate decreases by 0.25%**

A 0.25% pa decrease in the discount rate increases the net cost to the Company of future benefit accrual to 29.4% of Pensionable Pay.

**RPI inflation increases by 0.25%**

A 0.25% pa increase in the RPI inflation assumption (and the knock-on impact on the other assumptions derived from it) increases net cost to the Company of future benefit accrual to 29.2% of Pensionable Pay.

## Automatic enrolment

For the purposes of the 'alternative quality requirements' under automatic enrolment legislation, it may be necessary for the Company to consider the cost of accrual for groups with material differences in the cost of providing benefits.

However, this is not required in this instance as:

- All active members within the Scheme accrue the same future service benefit
- The cost of accrual from 1 April 2022 will be 35.6% of pensionable salary. This cost is greater than any of the minimum levels in the alternative quality requirements

Based on the above, I confirm that the Scheme meets the alternative quality requirements.

# Approximate developments since the valuation date

Since the valuation date, the Scheme's funding position is estimated to have changed.

The chart below illustrates how the position has changed over time.

It is approximate. The value of the Scheme's liabilities is based on assumptions consistent with those used to calculate the technical provisions, with financial assumptions updated to reflect changes in market conditions. It is assumed that demographic experience (e.g. mortality experience is in line with the assumptions). Approximate allowance has been made for the Scheme’s actual cashflows and investment performance up to 31 December 2021.

# Solvency position

The statutory estimate of the Scheme's solvency position is set out below.

## Results

| | Solvency (£M) |
|---|---|
| Value of past service benefits for: | |
| ▪ Actives (including Hybrid members) | 923 |
| ▪ Deferreds | 2,518 |
| ▪ Pensioners | 3,970 |
| ▪ Expenses | 44 |
| Value of liabilities | 7,455 |
| Value of assets[1] | 6,703 |
| Past service surplus/(deficit) | (752) |
| Funding Level | 90.0% |

[1] The value of assets excludes the Pension Funding Partnership valued at £155M as this would have had zero value if insolvency had occurred at the valuation date

This solvency estimate represents the estimated cost of purchasing annuities at the valuation date from an insurance company to meet the Scheme's benefits.

The assumptions include an allowance for the expenses of winding-up the Scheme. The assumptions used in the solvency estimate are summarised in an appendix.

## In practice

In practice, if the Scheme were to be discontinued with no solvent employer then the assets are unlikely to be sufficient to provide the benefits in full. If this were the case then:

- Benefits corresponding to those covered by the PPF would be met first (either through the PPF or, if there were sufficient funds, by securing these benefits with an insurance company).
- Any remaining assets would be used to secure part of the remaining benefits with an insurance company.

**The proportion of full benefits provided will vary from member to member and may be higher or lower than the statutory estimate of solvency quoted above.**

### Why higher?

The solvency estimate is higher than the technical provisions.

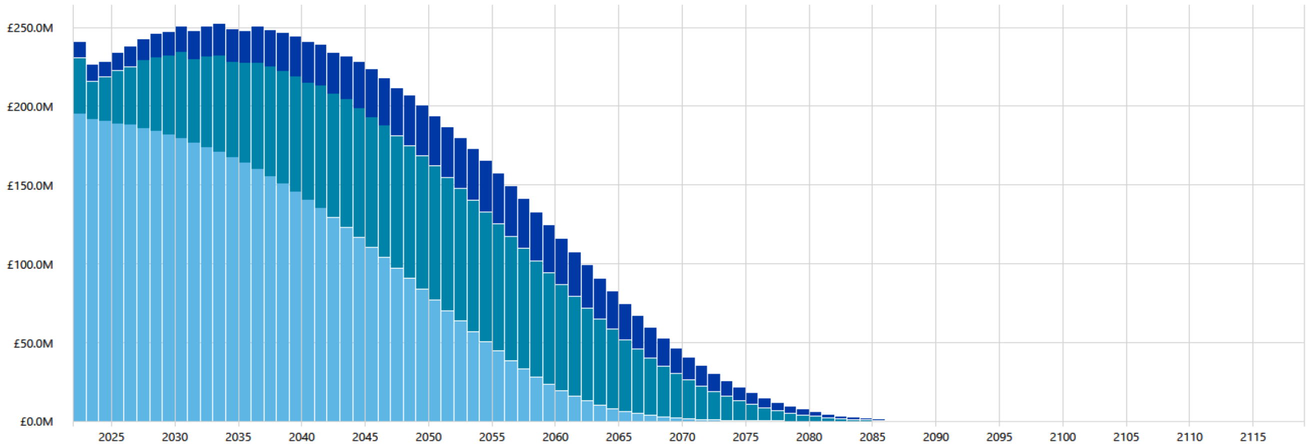
Broadly, this is for the following reasons:

- Insurers will typically hold less risky assets which provide **lower investment returns** than are expected to be achieved on the Scheme's assets
- Insurers typically hold **larger margins**, for example by assuming that members will live longer than is assumed in calculating the technical provisions
- Insurers need to cover **costs**, including administering the benefits, and also make a **profit**, and
- Allowance is made for the **cost of winding up** the Scheme.

# Funding and investment risks

## The funding level is likely to exhibit volatility.

The benefit payments from the Scheme are expected to be made for a very long period. The chart below shows the projected cashflows on the technical provisions basis for the Scheme.




## Key risks

The Scheme faces a number of key risks which could affect its future cashflows and funding position, including:

### Funding risk

The risk that the technical provisions are set too low and prove insufficient to meet the liabilities (e.g. in the event of unexpected discontinuance).

### Investment risk

The risk that investment returns are lower than assumed in the valuation, and also that the assets are volatile and move out of line with the liabilities, so the funding position is volatile.

### Liquidity risk

The risk that cashflows are higher than expected as members commute more than is assumed or take transfer values, possibly leading to the sale of assets at inopportune times.

### Longevity risk

The risk that Scheme members live for longer than assumed and that pensions would therefore need to be paid for longer.

### Inflation risk

The risk that the relevant inflation metric is higher than assumed, increasing the pensions that need to be paid.

### Sponsor risk

This is the risk that the sponsor is no longer willing or able to support the Scheme to fund any future losses that arise.

## Other risks

The Scheme is exposed to other risks too, which may also impact on the funding, investments and sponsor covenant. For example, those relating to climate change and other environmental issues as well as long-term uncertainty around geopolitical, societal and technological shifts.

## Risk mitigation

The Trustee takes an integrated approach to managing the Scheme's risks. The key actions taken to mitigate the risks include:

**Investment**

- Adopting a diversified investment strategy
- Investing in liability-driven investments, so that changes in the value of the liabilities will be partially matched by changes in the asset values, thus reducing the funding volatility

**Covenant**

- Holding an interest in a Pension Funding Partnership which will cover a technical provisions deficit (up to £430M) in 2030.

**Funding**

- Setting a funding and investment strategy under which the Scheme aims to reduce its dependence on the sponsor's continuing financial support.
- Making prudent assumptions in the technical provisions.


# Recovery plan and future contributions

# Recovery plan

Based on the position of the Scheme at the valuation date no recovery plan is needed.

## No recovery plan required

As the Scheme is in surplus (relative to the technical provisions), a recovery plan is not required.

# Agreed contributions

The contributions agreed as a result of this valuation and the projected position at the next triennial valuation are summarised below.

## Company contributions

Following discussions, the Company will pay:

- From 1 April 2021 to 31 March 2022: 38.25% of Pensionable Pay
- From 1 April 2022 to 30 June 2025: 8.0% of Pensionable Pay
- From 1 July 2025: 35.5% of Pensionable Pay

LESS any element met by member contributions for future accrual of benefits

- The cost of any augmentations to benefits

Contributions are payable monthly, with the contributions due in respect of a particular month payable within 19 days of the end of the calendar month to which they relate.

Expenses of running the Scheme, including the insurance premiums for lump sum death-in-service benefits, the Pension Protection Fund levy and other levies collected by The Pensions Regulator are to be met from the Scheme’s assets.

## Member contributions

Member contributions will continue at 8.0% of Pensionable Pay, with AVCs payable in addition.

### Schedule of contributions

These contributions are set out in the schedule of contributions.

As agreed, my certification of the schedule is based on the position at the valuation date.

A full review of the Company's contributions will be completed no later than following the next valuation, which is due to take place at 1 April 2024.

# Projections

I have illustrated below how I expect the Scheme's funding position to develop over the future.


## Projected future funding levels

I estimate that, by the next valuation:

- The **technical provisions** funding level will have reduced to about 104%, and
- The **solvency** level will have improved to about 92%.

## Assumptions

These estimates assume that:

- The experience of the Scheme between the two valuation dates is in line with the assumptions underlying the technical provisions and as set out in the statement of funding principles dated 21 February 2022; and
- The assumptions underlying the technical provisions and solvency bases remain unchanged.


## Rationale

The main reason for the expected deterioration in the technical provisions funding level is the lower expected value of the PFP as there will be fewer potential coupon payments and the probability of the terminal payment being needed will be lower.

Although not illustrated, it is also reasonable to expect that actual experience will lead to improvements in the funding position to the extent that the assumptions underlying the technical provisions are prudent.

The solvency level is expected to improve more strongly, mainly due to:

- The solvency assumptions typically containing more prudence
- The scheme maturing, particularly members retiring which removes uncertainty and so improves the terms of annuity purchase.


# Certificates

# Certificate of technical provisions

Actuarial certificate given for the purposes of Regulation 7(4)(a) of the Occupational Pension Schemes (Scheme Funding) Regulations 2005

**Diageo Pension Scheme**

## Calculation of technical provisions

I certify that, in my opinion, the calculation of the scheme's technical provisions as at 1 April 2021 is made in accordance with regulations under section 222 of the Pensions Act 2004.

The calculation uses a method and assumptions determined by the Trustee of the scheme and set out in the statement of funding principles dated 21 February 2022.

**21 February 2022**

| | |
|---|---|
| **Signature** | **Date** |

| | |
|---|---|
| **Name** | James Miller FIA |
| **Employer** | Aon Solutions UK Limited |
| **Qualification** | Fellow of the Institute and Faculty of Actuaries |
| **Address** | Aon<br>Verulam Point<br>Station Way<br>St Albans<br>AL1 5HE |


# Further information

Reference appendices and glossary

# Membership data

## The results in this report are based on the membership data summarised below.

I have conducted high level checks on the membership data provided by Capita. There are some areas where the data is currently not complete. This is an area that the Trustees are working with Capita on. For the purpose of this valuation I have supplemented the data provided by Capita with historical data held by Aon. If full and complete data was available this may have led to results that are different from those set out in this report. However, I would not expect this to lead to different conclusions on the level of future contributions agreed as part of this valuation. I am therefore satisfied the data I have used is adequate for the purpose of this actuarial valuation.

The average ages shown in these tables are unweighted.

| Active members | Number | Average age | Total Pensionable Pay (£000 pa) | Average Pensionable Pay (£ pa) | Average accrued Percentage |
|---|---|---|---|---|---|
| 2015 | 2,191 | 47 | 99,114 | 45,237 | 36.0 |
| 2018 | 1,136 | 50 | 53,954 | 47,495 | 39.5 |
| 2021 | 802 | 51 | 39,076 | 48,723 | 42.1 |

Note: The average accrued percentage above includes transferred-in percentages but does not allow for underpin pensions on previous transfers-in

| Hybrid members | Number | Average age | Total Pensionable Pay (£000 pa) | Average Pensionable Pay (£ pa) | Average Accrued Percentage |
|---|---|---|---|---|---|
| 2015 | - | - | - | - | - |
| 2018 | 77 | 52 | 4,800 | 62,330 | 48.4 |
| 2021 | 35 | 52 | 4,128 | 117,938 | 42.9 |

| Deferred members | Number | Average age | Total pension (£000 pa) | Average pension (£ pa) |
|---|---|---|---|---|
| 2015 | 17,054 | 57 | 74,411 | 4,363 |
| 2018 | 12,346 | 55 | 65,644 | 5,317 |
| 2021 | 9,997 | 57 | 58,146 | 5,816 |

Note: The deferred pension amounts shown above include revaluations to the April of the appropriate year.
The amounts of deferred pension above exclude any temporary pensions

| Pensioners | Number | Average age | Total pension (£000 pa) | Average pension (£ pa) |
|---|---|---|---|---|
| 2015 | 21,111 | 73 | 138,495 | 6,560 |
| 2018 | 18,309 | 74 | 147,552 | 8,059 |
| 2021 | 17,410 | 74 | 159,241 | 9,147 |

| Dependants | Number | Average age | Total pension (£000 pa) | Average pension (£ pa) |
|---|---|---|---|---|
| 2015 | 8,038 | 79 | 34,024 | 4,233 |
| 2018 | 5,676 | 79 | 34,269 | 6,038 |
| 2021 | 5,404 | 79 | 36,109 | 6,682 |

Note (pensioners and dependants): The pension amounts shown above include the increase awarded in April of the appropriate year.
Note: Dependants average age excludes children's age

# Benefits valued

The Scheme is divided into a number of subsections. The benefits given by these sections are set out in the legal documentation of the Scheme.

For illustration, this section includes an overview of the benefits provided to members of the Silver and Gold benefit levels for service up to 31 March 2018 and all members for service on or after 1 April 2018.

## Silver and Gold benefit levels for service up to 31 March 2018:

| | |
|---|---|
| Normal Retirement Age | 65 |
| Pensionable Pay | Basic Salary plus any other regular items stated as pensionable in the member's contract of employment |
| Final Pensionable Pay | The member’s highest Pensionable Pay in any consecutive 12 month period in the last 10 years before retirement or earlier exit. |
| Normal Retirement Pension | A pension of 1.6% for Silver members and 2.0% for Gold members of Final Pensionable Pay for each year of Pensionable Service until 31 March 2021. Pensionable Service is service from 1 April 1999 plus any benefits accrued in the GPF or GUD Pension Trust before 1 April 1999 (adjusted for any difference in accrual rates and pensionable pay definitions). |
| Early Retirement Pension | A pension is currently provided on retirement after the age of 50 for those with a protected pension age or 55 otherwise, calculated using completed service and reduced to allow for early payment. |
| Leaving Service | A deferred pension payable from Normal Retirement Date or a transfer payment to equivalent in value to the deferred pension. |
| Pension Increases | Increases in line with RPI up to a maximum of 5% are provided to pensions in payment in excess of the GMP accrued up to 31 March 2012 and CPI up to a maximum of 5% are provided to pensions in payment in excess of the GMP accrued after 31 March 2012. Ex-GPF members have an additional guarantee that their pension will increase by no less than 3% p.a. for benefits accrued prior to 1 April 2011. |
| Lump Sum | A member may exchange some of their pension for pension commencement lump sum on retiring. |

## CARE benefits for service on or after 1 April 2018:

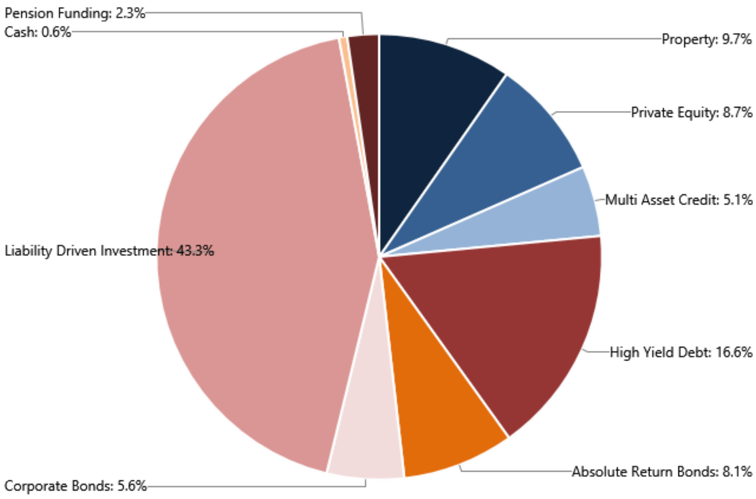
| | |
|---|---|
| Normal Retirement Age | 65 |
| Pensionable Pay | Basic Salary plus any other regular items stated as pensionable in the member's contract of employment |
| Member Contributions | 8% of pensionable pay |
| Normal Retirement Pension | **1 April 2018 to 31 March 2022**<br>Each year, members build up a block of pension equal to 1/70th of their Pensionable Pay during that year. When the member comes to take their pension benefits, all the blocks of pension that they have built up will be added together to give a total amount of pension payable to the member for life.<br><br>**From 1 April 2022**<br>Each year, members build up a block of pension equal to 1/108th of their Pensionable Pay during that year, subject to the 'cost control mechanism' set out in the Rules. When the member comes to take their pension benefits, all the blocks of pension that they have built up will be added together to give a total amount of pension payable to the member for life. |
| Early Retirement Pension | Members are able to take their CARE pension from age 60 without any reduction for early payment, subject to the consent of Diageo and the Trustee.<br>If the member retires before age 60, the pension will currently be reduced by 5% for each year they retire early before age 60. For example, if they retired at age 58, their pension would be reduced by 10%. |
| Leaving Service | A deferred pension payable from Normal Retirement Date; or<br>A transfer payment to either a new employer's scheme or a suitable insurance policy, equivalent in value to the deferred pension. |
| Pension Increases | Each block of pension will increase each April (on the 1st of the month) between the date the member earns it and the date that they draw their pension. These increases will be equal to the rise in Consumer Prices Index (CPI) inflation up to a maximum of 5% a year. |
| Lump Sum | A member may exchange some of their pension for pension commencement lump sum on retiring. |

# Assets

The Scheme's assets are held in a trust, which is a legally separate entity to the Company.

The audited accounts for the Scheme for the year ended 1 April 2021 show the assets were £6,865M, of which £7M relate to DC and AVC assets.

The chart shows how the balance of the assets of £6,858M is broadly invested.



# Previous valuation results

This page sets out the results and conclusions of the previous actuarial valuation of the Scheme at 1 April 2018.

## Key results

The key results from the previous valuation at 1 April 2018 were:

- There was a surplus of £234M relative to the **technical provisions**, which corresponded to a funding level of 104%.
- There was an estimated deficit of £1,289M relative to the **solvency** liabilities.

## Contributions

Based on the position of the Scheme at the 2018 valuation date no recovery plan was needed.

It was agreed that the Company would pay:

- 57% of Pensionable Pay to 31 December 2018 and 38.25% of Pensionable Pay from 1 January 2019, both LESS any element met by member contributions for future accrual of benefits.
- Monthly amounts to meet the budgeted expenses of administering the Scheme, including the payment of PPF levies until 31 December 2018. Unless agreed otherwise at the 2021 valuation, the Company would recommence paying the budgeted expenses from 1 January 2022.

# Notable changes since the previous valuation

There have been some significant changes to the Scheme since the previous valuation, which have impacted the funding assessment.

## Benefit changes

In October 2018, the Lloyds Bank Court Judgement established that pension schemes cannot provide unequal benefits in respect of post 17 May 1990 service to men and women as a consequence of the Guaranteed Minimum Pension ('GMP') element of the pension being unequal. A subsequent judgement in November 2020 established that the October 2018 ruling extends to the calculation of transfer values paid since 17 May 1990.

## Pension Funding Partnership

The Pension Funding Partnership was updated as follows:

- To reflect the potential deficit on the technical provisions as at 31 March 2030 (this was previously 31 March 2024).
- Annual contributions reduced from £25.0M to a maximum of £11.4M p.a. and are only now payable if there is a deficit on the technical provisions basis excluding the PFP in the relevant actuarial report.

## Liability management exercises

The Scheme undertook the following member options exercises in the inter-valuation period:

- Pension Increase Exchange that offered pensioners the opportunity to exchange higher future pension increases in payment for a higher pension now and lower pension increases in the future
- Bulk Transfer exercise for active and deferred members

# Analysis of the change since the previous valuation

I have analysed the change in the past service results from the previous valuation to this new one.

## Past service changes

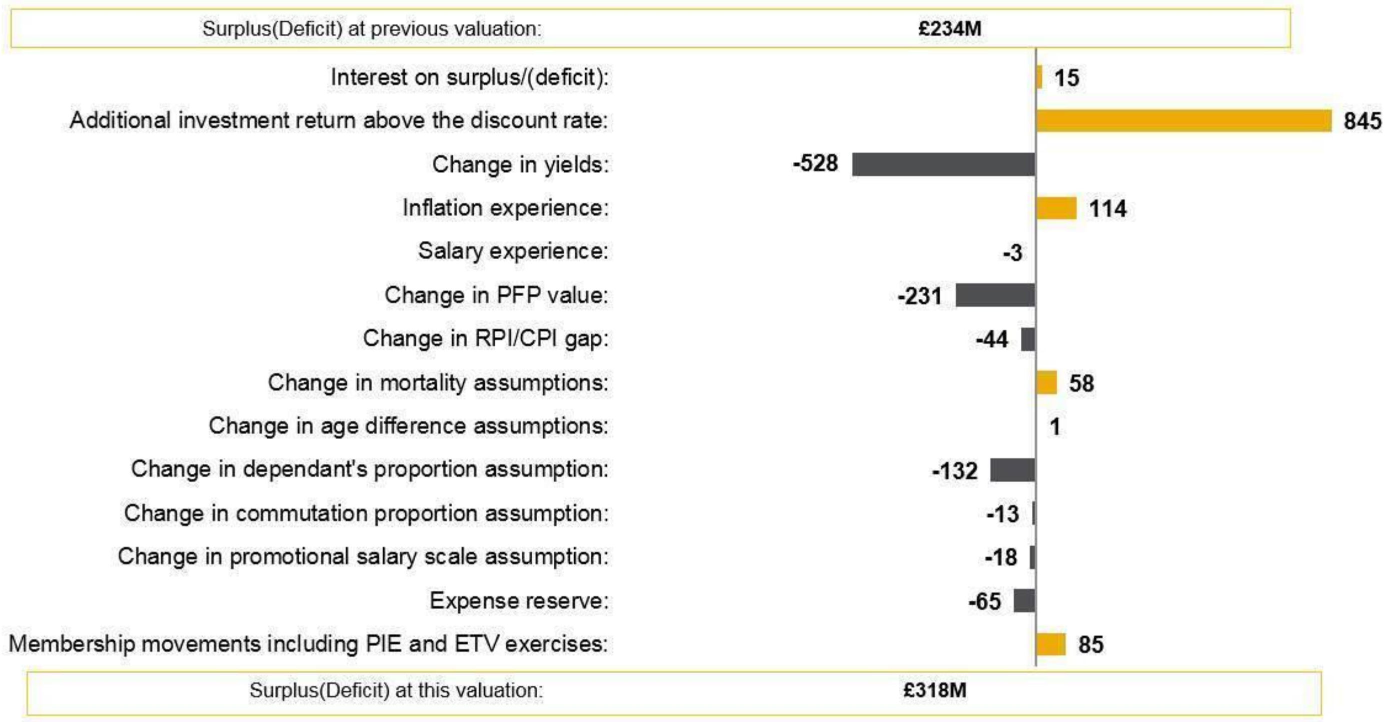
The past service results show that the surplus of £234M in the Scheme at the previous valuation has become a surplus of £318M at this valuation.

The chart below quantifies the key reasons for this change:

## Key factors

The analysis shows that the main factors affecting the funding position since the previous valuation have been:

- Changes in yields have deteriorated the position since the previous valuation
- This has been more than offset by positive investment returns above the discount rate.



# Solvency estimate: assumptions

The key assumptions used in calculating the solvency estimate are summarised below.

## Statutory solvency estimate

The solvency estimate has been calculated in line with statutory requirements. I have taken into account the investment strategies that a life assurance company is likely to use to back its annuity business and the resulting pricing we would expect to see under the market conditions at the valuation date, taking into account the size of the Scheme.

This considers the position if:

- The Scheme were discontinued on the valuation date.
- The Pension Funding Partnership has a value of £0M
- Member benefits were crystallised and, for active members, were based on their Pensionable Service and Salary at the valuation date.
- The assets were used to buy immediate and deferred annuities from an insurer.

The solvency estimate is a regulatory requirement and also provides a useful benchmark against which the Trustee and others can assess the relative prudence of other funding measures.

The basis used is described below.

### Estimate vs actual cost

This estimate is only a guide. The true position can only be established by conducting a competitive buy-out auction and fully defining the scope and likely cost of a wind-up process for the Scheme.

| Assumption | Solvency |
|---|---|
| Pre-retirement discount rate | Aon's Bulk Annuity Market Monitor yield curve for non pensioners. |
| Post-retirement discount rate | Aon's Bulk Annuity Market Monitor yield curve for non-pensioners (actives and deferreds) or pensioners. |
| RPI inflation | Term dependent rates derived from RPI swap markets |
| CPI inflation | RPI inflation assumption less 0.75% p.a. till 2030 and RPI inflation assumption less 0.10% p.a. thereafter |
| Salary inflation | Not applicable |
| Post-retirement mortality assumption - base table | S3PMA and S3PFA_M tables with individual scaling factors |
| Post-retirement mortality assumption - projection | CMI 2020 core projections with a smoothing parameter of 7.0, an initial adjustment parameter of +0.50% and a long-term improvement rate of 1.75% p.a. for men and women |
| Pre-retirement mortality assumption | 80% of AM/FC00 Ultimate standard table |
| Withdrawals | All members are assumed to leave active service immediately. |

| Assumption | Solvency |
|---|---|
| Early Retirements | All members are assumed to retire at their normal retirement date |
| Commutation | No allowance |
| Age Difference | Pensioners<br>Male pensioners are three years older than their wives. Female pensioners are same age as their husbands.<br><br>Non-pensioners<br>Male non-pensioners are two years older than their wives. Female non-pensioners are one year younger than their husbands. |
| Proportion Married | Pensioners<br>91% of male pensioners and 70% of female pensioners are assumed to be married or have a dependant at age 65, lower percentages apply at older ages.<br><br>Non-pensioners<br>88% of male non-pensioners and 80% of female non-pensioners are assumed to be married or have a dependant at age 65 |
| Expenses | A reserve equal to estimated expenses and charges associated with winding up the scheme |
| Discretionary benefits | No allowance made, other than for deferred revaluation which is in line with the approach used to value the technical provisions |
| GMP Equalisation | The solvency liabilities are increased by 1% as an approximate allowance of the cost of having to equalise GMPs within the Scheme |

# Legal framework and compliance

## TAS compliance

This report, and the work relating to it, complies with ‘Technical Actuarial Standard 100: Principles for Technical Actuarial Work’ (‘TAS 100’) and 'Technical Actuarial Standard 300: Pensions’ (‘TAS 300’).

The compliance is on the basis that Directors of the Diageo Pension Trust Limited are the addressees and the only users and that the report is only to be used as a summary of the outcome of the valuation. If you intend to make any other decisions after reviewing this report, please let me know and I will consider what further information I need to provide to help you make those decisions.

The report has been requested by the Trustee. It has been prepared under the terms of the Scheme Actuary Agreement between the Trustee and me on the understanding that it is solely for the benefit of the addressees.

This report should be read in conjunction with the statement of funding principles dated 21 February 2022.

## Shorthand in this report

**Scheme:** Diageo Pension Scheme

**Trustee:** The Diageo Pension Trust Limited

**Company:** Diageo Plc

**Rules:** The Trust Deed and Rules dated 21 March 2018, and amending legal documents

# Glossary

This glossary explains some common terms from the actuarial valuation process. Not all of them may be used in your report.

## Attained age method

This is one of the methods historically used by actuaries to calculate actuarial liabilities and contribution rates. It is similar to using the projected unit method but with a control period equal to the average future working lifetime of the active membership.

## Best estimate assumption

It is equally likely that actual experience will be better-than or worse-than such an assumption. Best estimate assumptions are subjective and therefore those referenced in one report may differ from best estimate assumptions derived elsewhere.

## Cash transfer sum

This is a benefit available to early leavers who have between three months and two years of pensionable service. It is calculated in the same way as the cash equivalent transfer value payable to longer-serving early leavers and is calculated at the date of leaving pensionable service.

## Consumer Prices Index (CPI)

Measure of UK price inflation published monthly by the Office of National Statistics. It is the Government's preferred measure of inflation. It is based on different items and weightings to the Retail Prices Index (RPI) and is also calculated using a different formula.

## Control period

This is the period of time from the valuation date that is considered when calculating the future service cost for schemes which are still open to accrual. The control period is commonly set to cover the next year, the 3-year period to the next valuation or the expected future working lifetime of the active membership.

## Current unit method

This is one of the possible methods used by actuaries to calculate actuarial liabilities and contribution rates. This method only allows for increases applicable to deferred pensioners beyond the effective valuation date (when calculating liabilities) or the end of the control period (when calculating contribution rates) and so does not allow for any further projected future increases to pay.

## Deficit

This is the funding target less the value of assets. If the value of assets is greater than the funding target, then the difference is called the surplus.

## Defined accrued benefits method

This is one of the possible methods used by actuaries to calculate actuarial liabilities and contribution rates. This method assumes that the scheme will be discontinued at the effective valuation date (when calculating liabilities) or at the end of the control period (when calculating contribution rates) and so does not allow for any further projected future increases to pay or any other terms applicable to active members. This method may be appropriate for schemes which anticipate winding up.

## Discount rate

This is used to place a present value on a future payment. A 'risk-free' discount rate is usually derived from the investment return achievable by investing in government gilt-edged stock. A discount rate higher than the 'risk-free' rate is often used to allow for some of the extra investment return that is expected from investing in assets other than gilts.

## Discretionary benefits

These are benefits which are not guaranteed under a scheme's rules and which are only granted to members at the discretion of the trustees and/or the sponsor.

## Duration of liabilities

The duration of a scheme’s liabilities represents the average term to payment of the liabilities. In broad terms, if a scheme has a duration of 20 years, then it will respond to changes in discount rate in the same way that a single cashflow which is payable in 20 years' time would. In practice, there are several different technical definitions of duration.

## Formula effect (in calculation of RPI and CPI)

The difference between measures of inflation arising from the use of different formulae to construct the RPI and CPI indices at the first stage of aggregation – the RPI uses a (simple) arithmetic average whereas the CPI uses a (compound) geometric average.

## Forward rate

A forward rate is a rate which is expected to apply over a future time period. For example, to discount a single payment from one future date (say, five years from now) back to a closer future date (say, three years from now).

## Funding level (or funding ratio)

This is the ratio of the value of assets to the funding target.

## Funding target

An assessment of the present value of the benefits that will be paid from the scheme in the future, normally based on pensionable service prior to the valuation date. Often, the funding target is equal to the technical provisions.

## Future service contribution rate (FSCR)

Only relevant for schemes still open to accrual; this is the cost of benefits accruing expressed as a percentage of the members’ pensionable pay. It considers the present value of the benefits expected to accrue to members and the pensionable pay expected to be paid to members over a given period (referred to as the control period). Provided that the distribution of members remains stable, with new members joining to take the place of older leavers, and if all the other assumptions are borne out, the calculated contribution rate can be expected to remain stable. If there are no new members, however, the average age will increase and the contribution rate can be expected to rise or fall depending respectively upon whether the discount rate is higher or lower than the salary increase assumption.

## Gilt yield curve

The term-dependent yields on gilts derived from fixed-interest gilts published by the Bank of England, which are extended by Aon for years beyond those published.

## Guaranteed Minimum Pension (GMP)

Most schemes that were contracted out of the State Earnings Related Pension Scheme (SERPS) before April 1997 have to provide a pension for service before that date at least equal to the Guaranteed Minimum Pension (GMP). This is approximately equal to the SERPS pension that the member would have earned had the scheme not been contracted out. GMPs ceased to build up on 6 April 1997, when the legislation changed.

## Hedging

A liability is said to be hedged if a scheme holds investments which respond in the same way as it does to changes in the risk being hedged (e.g. interest rates or inflation). Gilts and swaps are examples of investments which are commonly used to hedge liabilities.

## Inflation risk premium (IRP)

The difference between the best estimate of future inflation and its market price.

## Inflation uncertainty

Whilst, over the medium to long term, inflation is often considered to be reasonably stable, and a simple single assumption is often used for projections, in reality inflation can vary up and down significantly from one year to the next. This variation is sometimes referred to as inflation uncertainty.

## Limited Price Indexation (LPI)

The Pensions Act 1995 required schemes to provide a minimum level of annual increase to pensions in payment. The minimum level is the smaller of 5% and the increase in inflation* and applies to the pension earned from 6 April 1997 to 5 April 2005. With effect from 6 April 2005, the cap for statutorily-required LPI for future service was reduced from 5% to 2.5%.

*Until 2010, inflation for the purpose of this minimum was defined with reference to changes in the Retail Prices Index. From 2011, inflation was defined with reference to changes in the Consumer Prices Index.

## Longevity risk

This is the risk that life expectancies exceed those assumed and the pension scheme's liabilities are therefore higher than expected.

## Mortality future improvements

This is the assumption about how the number of people dying each year will reduce in the future. A higher rate of improvement will lead to a higher life expectancy. Also referred to as future longevity improvements.

## Mortality rate

A mortality rate measures the likelihood that an individual will die between one birthday and the next.

## Mortality table

Mortality tables summarise mortality rates across all ages.

## Ongoing best estimate

This is the present value of the benefits members are entitled to, should the scheme continue without being wound up early, assessed using a set of assumptions whereby the key assumptions are best estimates. Best estimate assumptions are subjective and therefore the figure provided in one report may differ from other best estimate valuations.

## Partly projected unit method

This is one of the possible methods used by actuaries to calculate actuarial liabilities and contribution rates. This method allows for some, but not full, projected future increases to pay between the valuation date and retirement or date of leaving service. This method may be appropriate for schemes which anticipate ending the link to future salary increases at a future date.

## Pension increase exchange (PIE)

An option that may be offered to members on or after retirement whereby members are granted a higher initial pension but must give up future inflationary increases in return. This can only be done with pension increases that are in excess of statutory minimum increases.

## Pension Protection Fund (PPF)

The PPF was established with effect from 6 April 2005. The PPF will normally take over the assets of a pension scheme in the event of its sponsor becoming insolvent and the scheme having insufficient assets to provide the PPF benefits. The PPF will not provide the scheme benefits in full. The PPF is financed by a levy on most defined benefit pension schemes. The PPF benefits are broadly 100% of benefits for pensioners over normal retirement age and 90% of benefits up to a cap for all other members. Pension increases granted on benefits are at lower levels than apply in many schemes, in particular, benefits earned before 6 April 1997 would not be given any pension increases within the PPF.

## Present value

Actuarial valuations involve projections of pay, pensions and other benefits into the future. To express the value of the projected benefits in terms of a cash amount at the valuation date, the projected amounts are discounted back to the valuation date by a discount rate. This value is known as the present value. For example, if the discount rate was 6% a year and if we had to pay a lump sum of £1,060 in one year’s time the present value would be £1,000.

## Projected unit method

This is one of the common methods used by actuaries to calculate actuarial liabilities and contribution rates. This method allows for full projected future increases to pay through to retirement or withdrawal.

## Protected Rights

Prior to April 2012, schemes could contract out of SERPS/S2P on a 'Protected Rights' basis. The accumulated National Insurance rebates in respect of each member as a result of being contracted out (known as Protected Rights) must be applied as an underpin to the member's benefits. Schemes that were contracted out on this basis before 6 April 1997 provided this underpin instead of GMPs.

## Prudent assumption

It is more likely that actual experience will be better than a prudent assumption than that it will be worse. The value of the liabilities will be higher when measured using prudent assumptions than using best estimate assumptions.

## Recovery plan

Where a valuation shows a funding shortfall against the technical provisions, trustees must prepare a recovery plan setting out how they plan to meet the statutory funding objective.

## Retail Prices Index (RPI)

Measure of UK price inflation published monthly by the Office of National Statistics. It is no longer the Government's preferred measure of inflation. As well as being based on different items and weightings to the Consumer Prices Index (CPI), it is also calculated using a different formula. However, it is the index that pension benefits have historically tended to be linked to and is the index used to determine increases in index-linked gilt coupons.

## RPI inflation curve

The term-dependent RPI inflation expectations derived from fixed-interest and index-linked gilts published by the Bank of England which are extended by Aon for years beyond those published.

## Scaling factor

Differences in life expectancy between schemes are typically allowed for by multiplying the chance of dying at each age by a scaling factor. Scaling factors of less than 100% mean that people are assumed to live longer than under the standard tables. For example, a scaling factor of 90% means that a member has a 10% less chance of dying each year than is assumed in the standard mortality tables. Similarly, scaling factors of more than 100% mean that people are assumed to live for less time than under the standard tables.

## Schedule of contributions

Trustees of pension schemes must prepare and maintain a schedule of contributions. This shows the dates and amounts of contributions due from the sponsor and members. Under the Pensions Act 2004, the schedule must be put in place within 15 months of the valuation date.

## Section 179 valuation

An actuarial valuation of a pension scheme in accordance with section 179 of the Pensions Act 2004. The Pension Protection Fund will take the results of a section 179 valuation into account when calculating a scheme's PPF levy.

## Solvency estimate

This represents an estimate of the cost of buying out a scheme’s benefits with an insurance company at the valuation date. Supply and demand factors also mean that no single solvency estimate can be relied on and so this estimate is unlikely to be the same as the actual cost of buying out the benefits. Assumptions are set by the Scheme Actuary.

## Solvency ratio

This is the ratio of the market value of a scheme's assets to the estimated cost of securing a scheme's liabilities in the event of the discontinuance of the scheme.

## Sponsor covenant

A sponsoring employer's 'covenant' is their legal obligation and financial ability to support the pension scheme, both now and in the future.

## Spot rate

A rate which is expected to apply between now and a future date. For example, to discount a single payment at a future date (say, five years from now) all the way back to time 0.

## Statement of funding principles

The Pensions Act 2004 requires trustees to prepare (and from time to time review and, if necessary, revise) a written statement of their policy for securing that the statutory funding objective is met. This is referred to as a statement of funding principles.

## Statutory funding objective

Under the Pensions Act 2004, every scheme is subject to the statutory funding objective, which is to have sufficient and appropriate assets to cover its technical provisions.

## Surplus

This is the value of assets less the funding target. If the funding target is greater than the value of assets, then the difference is called a deficit.

## Swap yield curve

The term-dependent yields on fixed-interest swaps derived by Aon from market data.

## Technical provisions

This is the present value of the benefits members are entitled to, based on their pensionable service to the valuation date and assessed using the assumptions agreed between a scheme's trustees and the sponsor. It generally allows for projected future increases to pay through to retirement or date of leaving service.

## Transfer value

Members generally have a legal right to transfer their benefits to another pension arrangement before they retire. In taking a transfer, members give up their benefits in a scheme, and a sum of money (called the transfer value) is paid into another approved pension scheme; this is used to provide pension benefits on the terms offered in that scheme.

## Withdrawal

Members may leave a pension scheme before their normal retirement age (typically because they leave employment with the sponsor). When they do so, their accrued benefits will no longer be linked to future salary increases (where applicable), and will instead be linked to future inflation. Benefits will still be payable at normal retirement age.

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