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June 2017

Dear Member,

Hermes Group Pension Scheme

Please find attached your Summary Funding Statement for 2016. This includes both the Summary Funding Statement based on the Actuarial Valuation as at 31 December 2014 and values used in the Annual Funding Updates as at 31 December 2015 and 31 December 2016.

Contact Details

Should you need any details on your pension benefits or have changed your personal circumstances, please contact Capita Employee Benefits, the Scheme Administrators:

hermes.pensions@capita.co.uk

01227 771445

Capita Employee Benefits, PO Box 323, Whitstable, CT5 9BY

If you have any further queries with regard to this communication or the management of the Scheme, please contact Inside Pensions, the Scheme Secretary:

hermes@insidepensions.com

01727 733150

Inside Pensions, Third Floor, 54-56 Victoria Street, St Albans, Hertfordshire, AL1 3HZ

The Trustee of the Hermes Group Pension Scheme

HERMES
INVESTMENT MANAGEMENT

June 2017

HERMES GROUP PENSION SCHEME: SUMMARY FUNDING STATEMENT BASED ON THE ACTUARIAL VALUATION AS AT 31 DECEMBER 2014 AND VALUES USED IN THE ANNUAL FUNDING UPDATE AS AT 31 DECEMBER 2016

Introduction

Every year we send members information about the funding of the Scheme. The Scheme Actuary carries out a valuation generally every three years. The most recent valuation was carried out as at 31 December 2014. Between triennial valuations, the Scheme Actuary updates the valuation annually on an approximate basis.

The actuarial valuation compares the value of the benefits earned up to the valuation date that the Scheme will have to pay in the future (the Scheme's liabilities) with the amount of money currently invested in the Scheme (the Scheme's assets).

Over time, the Scheme's 'funding position' (i.e. how its assets compare with its liabilities) will vary. In annual summary funding statements, we will tell you about the Scheme's financial position and how it has changed since the previous year's statement. This statement is based on the actuarial valuation as at 31 December 2014 and values used in the annual funding updates as at 31 December 2015 and 31 December 2016.

The Trustee hopes that you will find these statements useful and reassuring. If you do have any queries, however, please contact Inside Pensions, the Scheme Secretary:

The last actuarial valuation

The most recent valuation of the Scheme showed that on 31 December 2014 the funding position was as follows:

Assets	£138.6m
Estimated amount needed to provide benefits earned up to the valuation date (liabilities)	£170.7m
Shortfall of assets compared with liabilities	£32.1m
Funding level (ratio of assets to liabilities)	81%

There are some important facts to bear in mind about the valuation:

- The funding valuation treated the Scheme as continuing, with the ongoing support of the Employers.
- The valuation used assumptions that were determined by the Trustee after considering actuarial advice and agreed by the Employers. The assumptions relate to future events, for example on investment returns or how long members will live in retirement, and the actual events will differ from those assumed.
- Since in practice assumptions are not borne out, there is a need to monitor the financial position regularly.

Employer contributions

Following the 31 December 2014 valuation, the Employers and the Trustee agreed and signed a Recovery Plan which aims to eliminate the Scheme's shortfall of assets by 31 October 2020. A copy of the Recovery Plan is included as an appendix to the valuation report which is available on the Scheme's website.

In addition to the contributions to fund the shortfall, the Employers also agreed to pay to cover the expenses of the Scheme.

Estimated Funding position as at 31 December 2016

Assets	£181.1m
Estimated amount needed to provide benefits earned up to the valuation date (liabilities)	£203.8m
Shortfall of assets compared with liabilities	£22.7m
Funding level (ratio of assets to liabilities)	89%

The results show the funding of the Scheme has improved overall since the 31 December 2014 valuation.

The funding position has improved from the 82% estimated as at 31 December 2015 to 89% as at 31 December 2016. This was mainly due to positive asset return experience over the period, and the deficit contributions paid by the Employer. This was partially offset by deterioration in market conditions over the year. The current unusually low interest rates have the effect of increasing the size of the Scheme's liabilities.

This is not a full actuarial valuation of the Scheme, but an approximate projection of the previous valuation results, allowing for changes in economic conditions and actual investment returns to 31 December 2016.

The variation in the numbers over time emphasises the fact that these are only snapshots at a particular date. In the kind of volatile markets experienced over the past few years, it is important to take a long term perspective. The strength of the Employers' balance sheets has a more important bearing on the long term security of the Scheme than the snapshots of the funding levels at a particular date.

How is my pension funded?

The Trustee ensures that the Employers pay all contributions necessary so that when members retire the Scheme can pay the pensions due to them and pay all other benefits payable under the Scheme Rules.

The money to pay for members' pensions is held in a single fund separate from, and not controlled by, the Employers. It is not held in separate funds allocated to each individual member.

The importance of the Employers' support

The Trustee's main objective is to have enough money in the Scheme to pay pensions now and in the future. This relies on the Employers' legal obligation to continue to support the Scheme because:

- the Employers will be paying the future expenses of running the Scheme on an annual basis;
- the value of assets and liabilities can fluctuate, and when there is a funding shortfall, the Employers will need to put in more money; and
- the target funding level may turn out not to be enough so that the Employers will need to put in more money.

The Employers are both BT Pension Scheme Trustees Limited, which is the trustee company for the BT Pension Scheme, and Hermes Fund Managers Limited. The Employers are jointly and severally responsible for the funding of HGPS. They are together very strong financially, in particular the BT Pension Scheme currently has assets of just over £40 billion.

Payments to the Employers

There has not been any payment to the Employers out of the Scheme in the period since the 31 December 2014 valuation, or at any other time.

What is the Scheme invested in?

The Trustee's current policy is to invest in a broad range of assets subject to asset class targets as follows:

	Long Term Strategic Asset Allocation	Actual Asset Allocation 31-Dec-15	Actual Asset Allocation 31-Dec- 16
Global developed & emerging market equity	**30.0%**	**41.0%**	**32.0%**
Absolute Return	**0.0%**	**0.4%**	**0.0%**
Multi Asset (Active)	**20.0%**	**17.2%**	**16.8%**
Property (Active)	**10.0%**	**13.1%**	**10.8%**
Diversified Credit	**15.0%**	**13.6%**	**15.7%**
LDI (Passive)	**25.0%**	**14.1%**	**24.2%**
Cash	**0.0%**	**0.6%**	**0.5%**

The actual proportion invested in any particular class of assets at any time will differ from the targets.

The Trustee appointed Hymans Robertson LLP as investment advisors from 1 January 2013 (to replace BT Pension Scheme Management Limited). The Trustee then initiated a full review of the investment strategy, and investment strategy continues to be reviewed ongoing.

Where can I get more information?

Please see attached a list of some of the Scheme documents that are available to you. If you have any other questions, or would like any more information, please contact Inside Pensions, the Scheme Secretary. Contact details are provided on page 1. The HGPS website at www.hermes-investment.com/hgps also contains helpful information about the Scheme.

Please also help us to keep in touch with you by telling us if you change address.

The position on 'winding up'

The funding position reported in this communication assumes that the Scheme will continue in operation in the future. However, sometimes pension schemes are wound up, which means that the accrued benefits for all members are bought out with an insurance company.

If the Scheme had started winding up on 31 December 2014 (the date of the last formal valuation), the estimated amount needed to ensure that all members' benefits could have been secured in full with an insurance company would have been about £297.4m. As the assets at that date were £138.6m there would have been a deficit on this basis of about £158.8m.

Inclusion of this information does not imply that the Employers are thinking of winding-up the Scheme and more details on the winding-up position are provided below.

What would happen if the Scheme started to wind up?

It is important to note that, whilst the Scheme continues (as it is now), even though funding may temporarily be below target from time to time, benefits continue to be paid in full. If the Scheme were to start to wind up, the Employers are required to pay enough into the Scheme to enable the members' benefits to be secured in full with an insurance company. It may be that it is not possible for this full amount to be paid, but this is very unlikely as HGPS has Employers who are financially very strong. In the unlikely event that there is a shortfall, the Pension Protection Fund may take over the Scheme and pay certain benefits to members. There are limits on the amounts paid by the Pension Protection Fund and this would not give exactly the same benefits as those provided by the Scheme.

Further information and guidance is available on the Pension Protection Fund's website at www.pensionprotectionfund.org.uk.
Alternatively, you can write to the Pension Protection Fund
at 12 Dingwall Road, Croydon, CR0 2NA.

Why does the Scheme not call for full winding up solvency at all times?

The full winding up solvency position assumes that benefits will be secured by buying insurance policies. Insurers are obliged to take a very cautious view of the future and need to make a profit. The cost of securing pensions in this way also incorporates the future expenses involved in administration. By contrast, our funding scheme assumes that the Employers will continue in business and support the Scheme.

Important: If you are thinking of leaving the Scheme for any reason, you should consult a professional advisor, such as an independent financial advisor, before taking any action.

The Trustee of the Hermes Group Pension Scheme

Additional documents available on request

The following documents are available to members. Many are available on the website www.hermes-investment.com/hgps , but if you want us to send you any of these documents please let the Scheme Secretary know.

Statement of Investment Principles. This explains how the Trustee invests the money paid into the Scheme.

Schedule of Contributions. This shows how much money is being paid into the Scheme.

Annual Report and Accounts. The report shows the Scheme's income and expenditure in the year to 31 December 2016.

Actuarial Valuation. The full report as at 31 December 2014.

Statement of Funding Principles. This sets out the policy of the Trustee in relation to scheme funding and other related matters.

Recovery Plan. This sets out the plan for eliminating the past service deficit in the valuation as at 31 December 2014.

Annual Benefit Statement – This statement will provide you with an illustration of your likely pension. The Scheme Administrator routinely provides Annual Benefit Statements. Alternatively, if you are an active or deferred member, you are able to request one for a particular date.