HYMANS ROBERTSON

London Borough of Havering Pension Fund

Embedding climate risk management into the Fund

November 2022

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Executive Summary: Key actions over 2023 to embed climate risk management into the Fund

By 31 March 2023

- Completed the climate metrics baseline assessment
- Undertaken an education session on climate metrics
- Drafted a climate risk management policy

By 30 June 2023

- Agreed a net-zero target date and agreed the key climate metrics to be assessed
- Completed a gap analysis against the finalised LGPS TCFD requirements
- Finalised a climate risk management policy

By 30 September 2023

- Agree targets for individual metrics that will be set and developed actions to achieve the targets
- Completed the TCFD report for year to 31 March 2023
- Understood what strategy changes can be considered quickly to achieve the targets

By 31 December 2023

- Completed climate related engagement with at least two managers (LCIV + non-equity manager)
- Documented actions and expected outcomes for both managers
- Consider the form of ongoing monitoring that can be implemented for the Fund during 2024

The proposed overall budget for work over 2023 is [redacted]. Committee is asked to discuss and agree the proposed actions for 2023.

Introduction

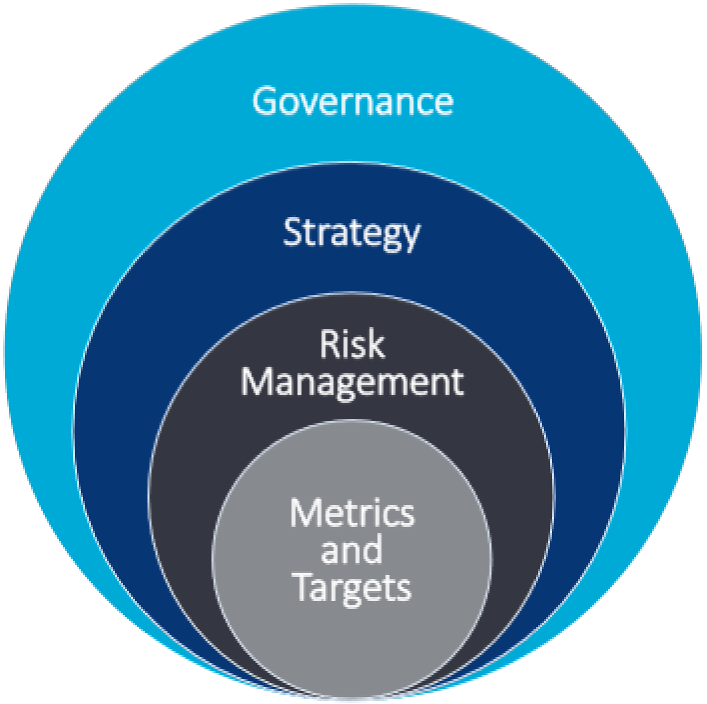
- This paper is addressed to the Pensions Committee (“the Committee”) of the London Borough of Havering Pension Fund (“the Fund”). The purpose of this paper is to summarise the next steps with regard to developing the Fund’s Climate Plan, building on the actions already taken by the Fund to address climate risk.
- This paper should not be released or otherwise disclosed to any third party except as required by law or regulatory obligation without our prior written consent. We accept no liability where this note is used by, or released or otherwise disclosed to, a third party unless we have expressly accepted such liability in writing. Where this is permitted, the note may only be released or otherwise disclosed in a complete form which fully discloses our advice and the basis on which it is given.
- Committee has previously set a belief stating that: “Climate change and the expected transition to a low carbon economy represents a long-term financial risk to Fund outcomes and should be considered as part of the Committee’s fiduciary duty.”
- Over the last two years, the Fund has addressed climate risk in a number of manners:
  - Changes have been made to several equity portfolios to incorporate climate factors
  - A commitment has been made to invest in renewable energy infrastructure
  - Dialogue with asset managers has incorporated climate factors
  - An initial baseline assessment of several carbon metrics has commenced
  - Climate scenario analysis has been incorporated within the actuarial valuation exercise
  - The Fund has prepared TCFD reporting over the last two years
- As the Committee both looks to develop and implement a climate risk commitment for the Fund, and becomes subject to TCFD, so it is appropriate to ensure that all related considerations are embedded in activity

The IIGCC net-zero framework defines a series of actions that asset owners can undertake to demonstrate compliance

Governance and strategy	❑ Commit to goal of net zero emissions by 2050 or sooner ❑ Define beliefs and set strategy/objectives for managers & others ❑ Undertake risk assessment in line with TCFD ❑ Publish clear action plan and disclose information in relation to net zero goal
Targets & Objectives	❑ Set medium term emissions reduction (<10 years) ❑ Set medium term climate solutions targets (<10 years) and define measurement basis ❑ Set asset class targets for % AUM in material sectors achieving or aligned to net zero ❑ Set engagement goal for % financed emissions in material sectors subject to stewardship
Implementation	❑ Use appropriate portfolio construction approaches to build climate aligned strategy ❑ Clear climate aligned engagement/voting plan with escalation ❑ Use of selective divestment based on climate related financial risks
Strategic Asset Allocation	❑ Update capital markets assumptions based on scenario analysis ❑ Use broader range of climate metrics to set objectives and strategy ❑ Set asset class mix with climate variants ❑ Review constraints to increasing alignment
Advocacy & Engagement	❑ Advocate for net zero policy, regulation, disclosure and shareholder rights ❑ Engagement with asset managers ❑ Engagement with other market actors

DLUHC is currently consulting on the implementation of TCFD for LGPS funds

- Proposals are expected to be effective from April 2023 with initial reporting due by end 2024
- Recommended approach largely follows the private sector framework although there are several key differences for the LGPS
  - Proposals establish the broad framework for TCFD although the detailed requirements will be embedded in statutory guidance which is yet to be published
  - Requirements will require monitoring of at least four metrics including absolute emissions, emissions intensity, data quality and a binary Paris Alignment metric
  - Reporting will be required annually with proposals for a Scheme wide report prepared by the SAB
- Committee's current approach to addressing climate risk will mean that the TCFD requirements will largely be met, but can test against final requirements once these are published in 2023
- Climate plan will need to ensure that all the requirements of TCFD are fully embedded in the Fund's processes



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Building on the previous outline plan and the actions taken to date, we can consider key deliverables over 2023/24

Build knowledge and understanding	Baseline position for change	Create focus areas and frame objectives / targets	Build and implement a plan	Monitor, evolve and report
November 2021 climate risk workshop and June 2022 Committee discussion	*Started at September 2022 Committee meeting*	*Areas of focus for 2023*	*Areas of focus for 2023*	*2024 onwards*

Key deliverables for 2023 include:

- Clearly articulated climate policy setting out baseline position, broad ambition and objectives for change. Policy should also frame approach to risk management and consideration of climate related opportunities
- Defined suite of metrics that will be periodically measured including a baseline measurement against which change will be assessed. Should also define rationale for the selection of metrics, expectations for improvement in the metrics and the actions that will be taken to achieve this
- Initial form of reporting covering how metrics will be calculated and reported to Committee and what actions will be taken
- Programme for more detailed, granular consideration of portfolios and the actions that can be taken

Areas of focus over 2023 will directly address some of the elements of the net zero framework and begin to consider others

Governance and strategy	✓ Commit to goal of net zero emissions by 2050 or sooner ✓ Define beliefs and set strategy/objectives for managers & others ✓ Undertake risk assessment in line with TCFD ✓ Publish clear action plan and disclose information in relation to net zero goal
Targets & Objectives	✓ Set medium term emissions reduction (<10 years) ? Set medium term climate solutions targets (<10 years) and define measurement basis ? Set asset class targets for % AUM in material sectors achieving or aligned to net zero ? Set engagement goal for % financed emissions in material sectors subject to stewardship
Implementation	? Use appropriate portfolio construction approaches to build climate aligned strategy ? Clear climate aligned engagement/voting plan with escalation × Use of selective divestment based on climate related financial risks
Strategic Asset Allocation	× Update capital markets assumptions based on scenario analysis × Use broader range of climate metrics to set objectives and strategy × Set asset class mix with climate variants × Review constraints to increasing alignment
Advocacy & Engagement	× Advocate for net zero policy, regulation, disclosure and shareholder rights ✓ Engagement with asset managers × Engagement with other market actors

H1 2023: Focus on defining vision, framing overall ambition and developing policy

Areas of activity

- Initial work to establish net-zero goals and objectives. Net-zero target to be used to inform discussion at subsequent stages of the climate plan
- Education on climate metrics, what they mean and why they matter in the implementation of a climate informed strategy. Consideration of the actions that can be taken to pursue a target linked to each climate metric
- Finalisation of the initial baseline assessment to give a benchmark against which progress can be measured
- Understand implications for the Fund of the change required to achieve net-zero target, including potential areas of cost and potential benefits that may arise
- Developing goals and objectives so we frame our overall ambition, consider what this means for the Fund in terms of the changes that are needed in relation to our starting point which we are now being bale to tie down a bit and plot something of a trajectory towards the goal.
- Consider the different actions that the Committee could consider and the metrics against which progress will be monitored, with particular reference to TCFD requirements

Key deliverables

- Completed climate baseline assessment (by Q1, 2023)
- Education session on climate metrics (Q1, 2023)
- Agreed net-zero target date and agreement on key climate metrics to be assessed (Q2, 2023)
- Gap analysis against LGPS TCFD requirements (completed following publication of guidance)
- Finalised climate risk management policy (draft in Q1, 2023 for finalisation in Q2, 2023

Expected budget

- [redacted]

H2 2023: Focus on developing and implementing climate action plan

Areas of activity

- Agree short, medium and long-term actions that will be taken to work towards overall ambition. Prioritise ‘quick wins’ with a focus on actions which will lead to tangible improvements in climate objectives
- Focus on stewardship and agree how Committee will engage with and hold asset managers accountable on climate, primarily focusing on LCIV. Agree climate KPIs for managers
- Undertake deep dive into at least one equity (LCIV) and one non-equity mandate to consider more granular goals on material sector exposures and engagement priorities. This will assist in framing ancillary climate targets
- Consider other areas of risk management activity that need to be addressed to ensure TCFD requirements are met
- Agree future reporting framework and agree approach for future collection of climate metrics
- Agree climate objectives and evaluation criteria for other service providers

Key deliverables

- Agree targets that will be set and actions to achieve the target (Q3, 2023)
- Plan for short term changes in strategy that can be explored in more detailed over period to end 2024, aligning this with broader strategy review
- Completed engagement with at least two managers and have documented actions and expected outcomes for both (Q4, 2023)
- Complete TCFD report for year to 31 March 2023 (Q3, 2023)

Expected budget

- [redacted]

2024: Focus on implementing the climate policy and monitoring and reporting progress

Areas of activity

- Continued implementation of changes to strategy
- Further deep dive evaluations of other managers to broaden understanding and build out activity and ensure KPIs in place for all managers
- Reporting to include agreed climate metrics to enable the Fund to monitor progress towards its net zero target - highlighting worst performing mandates to aid meaningful engagement with investment managers. ‘Deep dive’ review of key mandates carried out to further aid engagement process
- Annual assessment of climate metrics against baseline and evaluation of providers against KPIs
- Publication of first TCFD report under LGPS regulations
- Reassessment of initial progress against climate policy commitments

Summary of key deliverables for 2023

	Q1	Q2	Q3	Q4
Completed climate baseline assessment	Y			
Education session on climate metrics	Y			
Agreed net-zero target date and agreement on key climate metrics		Y		
TCFD gap analysis		Y		
Finalised climate risk management policy	Y	Y		
Agree targets that will be set and actions to achieve the target			Y	
Identify potential short term “quick wins”				Y
Deep dive with LCIV and agree expectations for manager			Y	
Deep dive with non-equity manager and agree expectations for manager				Y
Complete TCFD reporting for year to 31/3/23			Y	

Appendix: Climate Baseline

Baseline Metrics - Update

Mandate	WACI (tCO2e / £m)	% of Portfolio with Fossil Fuel Ties	Implied Temperature Rise	Exposure to Green Revenues / Climate Solutions	NZAMI Signatory
MSCI ACWI	163	12%	3.4°c	5%	N/A
Equity					
LGIM All World	177	4%**	3.0°c	4%	Yes
LGIM Emerging Markets	380	6%**	3.4°c	7%	Yes
LGIM Future World	146	2%**	2.7°c	5%	Yes
LCIV BG GAPA	107	0%	Available at separate cost.	Available at separate cost.	Yes*
LCIV PEPPA	120	1%	Available at separate cost.	Available at separate cost.	Yes*
Multi-Asset					
LCIV Ruffer	266	15%	Available at separate cost.	Available at separate cost.	Yes*
LCIV BG DGF	441	14%	Available at separate cost.	Available at separate cost.	Yes*
Real Assets					
UBS	41	0%	Expected Q1 2023.	Date not yet confirmed.	Yes
CBRE	Date not yet confirmed	0%	Date not yet confirmed	Date not yet confirmed	Yes
JP Morgan	51**	22%	Date not yet confirmed.	31%**	Yes
Stafford II	93**	21%	Date not yet confirmed.	35%	Yes
Stafford IV	19**	12%	Date not yet confirmed.	32%	Yes
LCIV Renewable Infrastructure	Available at separate cost.	Available at separate cost.	Available at separate cost.	Available at separate cost.	Yes*
Bonds					
RLAM MAC	127	2%	3.6°c	6%	Yes
RLAM Corporate Bonds	145	14%	2.7°c	20%	Yes
Churchill II	Expected 2023	0%	Date not yet confirmed.	Date not yet confirmed	No
Churchill V	Expected 2023	0%	Date not yet confirmed.	Date not yet confirmed	No
Permira	9	0%	Date not yet confirmed.	Date not yet confirmed.	No

**LCIV is not a signatory but each underlying manager is. Source: Investment managers.*
*** Previously not available in 'Climate Risk Plan – Baseline' paper produced in August 2022, now available following update from investment manager.*

Baseline Metrics

Weighted Average Carbon Intensity (“WACI”)
A measure of a portfolio’s exposure to carbon-intense companies. This is expressed in terms of tons of CO_2 equivalent emitted per million dollars of revenue, weighted by the size of the allocation to each company. Is measured using scope 1 + scope 2 emissions. Scope 1 emissions are those from sources owned or controlled by the company, typically direct combustion of fuel as in a furnace or vehicle. Scope 2 emissions are those caused by the generation of electricity purchased by the company.

% Of Portfolio With Ties to Fossil Fuels
The percentage of the portfolio invested in companies with an industry tie to fossil fuels (thermal coal, oil and gas), in particular reserve ownership, related revenues and power generation. It does not flag companies providing evidence of owning metallurgical coal reserves.

Implied Temperature Rise
The security's alignment temperature when referencing a combined approach which takes into account Scopes 1, 2, 3 and "cooling" potential (including emission reduction targets set by the firm). An ITR of 2°c suggested that the company’s current emission and management strategies are aligned with a 2°C climate change scenario.

Exposure to Green Revenues / Climate Solutions
The weighted average % of revenue for portfolio companies derived from revenue generated by economic activities relating to the transition to net zero, which typically meet the requirements of the EU Taxonomy on Sustainable Finance.

Net Zero Asset Managers Initiative (NZAMI)
The Net Zero Asset Managers initiative is an international group of asset managers committed to supporting the goal of net zero greenhouse gas emissions by 2050 or sooner, in line with global efforts to limit warming to 1.5 degrees Celsius; and to supporting investing aligned with net zero emissions by 2050 or sooner.

Paris Agreement
The Paris Agreement is a legally binding international treaty on climate change. It was adopted by 196 Parties at COP 21 in Paris, on 12 December 2015. Its goal is to limit global warming to well below 2, preferably to 1.5 degrees Celsius, compared to pre-industrial levels.

Risk Warning

Please note the value of investments, and income from them, may fall as well as rise. This includes equities, government or corporate bonds, and property, whether held directly or in a pooled or collective investment vehicle. Further, investments in developing or emerging markets may be more volatile and less marketable than in mature markets. Exchange rates may also affect the value of an overseas investment. As a result, an investor may not get back the amount originally invested. Past performance is not necessarily a guide to future performance.