

Draft Climate Policy and Action Plan

The Pensions Committee (“the Committee”) of the London Borough of Havering Pension Fund (“the Fund”) has developed this climate risk policy and action plan. This policy will be revised on an ongoing basis as the Fund’s action plan to achieve these objectives is developed and will be supported by ongoing quantitative analysis. This policy sets out the targets set by the Committee as well as the detail on the approaches that will be taken to achieve the net zero ambition included in the policy.

Introduction

The Committee considers that climate change represents a material financial risk with the potential to disrupt economic, financial and social systems. However, the potential impact on the Fund is unknown given policy uncertainty and the unknown physical feedbacks from environmental systems. Risks to the Fund arising from climate change include, but are not limited to:

- Economic risks: risks that the assumptions made in valuing the liabilities are inappropriate;
- Demographic risks: risks that demographic experience is different to that assumed as a consequence of climate related impacts;
- Asset risks: risks that the performance of the Fund’s assets is lower than assumed due to investments being affected directly by the physical impacts from climate change, the repricing or assets to reflect future physical risks or the transition to a lower carbon economy.

As a responsible asset owner, the Committee recognises the need to address the systemic risks posed by climate change, including the risks it poses to the Fund’s investments and its beneficiaries, thereby impacting the Committee’s fiduciary duties. The Committee has an ambition for the Fund to achieve net zero financed emissions by 2050 at the latest. This recognises that future improvements in the availability and quality of climate data (particularly for unlisted investments), and in the availability of available sustainable investment options, are factors in achieving progress. This ambition is made in the expectation that governments will follow through on their own commitments to ensure the objectives of the Paris Agreement are met.

To support the ambition, the Committee has developed this document as a framework for achieving net zero financed emissions, i.e. emissions produced by the investments held in the Fund. This framework is designed to guide as well as communicate the Committee’s investment decisions enabling the Fund to align with the goals of the Paris Agreement and contribute to real economy change.

A key objective is achieving positive real-world change and a significant reduction in emissions over time, whilst also maintaining a balance with the Fund’s wider risk / return objectives and its fiduciary duty to pay all member benefits.

This policy sets out the Committee’s approach to addressing climate related risks within the Fund and is intended to deliver strong long-term financial returns, in line with its overall funding objectives, as the impacts of climate change materialise. This document is designed to be dynamic and evolve as best practice changes. The Fund’s transition plan may be adjusted over time as new information emerges and circumstances change. By remaining open to new ideas and approaches, the Fund can strengthen its ability to reach its net zero goals.

Objectives and Actions

The Committee has determined that there are four There are four core elements associated with the action plan, split between portfolio level and asset level targets and actions. The key targets and actions within each element are summarised in the following table:

| Objective Area | Targets the Committee will assess | Actions the Committee will take |
|-------------------------------------|---|--|
| Portfolio emissions | <ul style="list-style-type: none"> Ambition to reduce financed emissions to net zero by 2050 at the latest Interim target to reduce scope 1 and 2 emissions on listed equities by 50% compared to the 2022 baseline level by 2030 | <ul style="list-style-type: none"> This will be achieved through a combination of capital allocation and engagement. Engagement with the London CIV will be a key focus, with the development of compelling decarbonisation solutions a priority. Strategies employed must have clear decarbonisation pathways. |
| Climate solutions and opportunities | <ul style="list-style-type: none"> 10% asset allocation by 2030, with potential to consider further increasing allocations past 2030 Positive impact to deforestation, biodiversity loss, social factors and climate adaptation are key factors included in decision-making | <ul style="list-style-type: none"> Consider extending allocation to renewable energy Consider local investment with positive social impact Emphasise climate solutions in new allocations to private market assets |
| Alignment | <ul style="list-style-type: none"> Minimum 50% alignment of listed assets aligned with an appropriate net zero pathway by 2030 At least 75% of heavy emitting sectors aligned with a net zero pathway by 2030 50% of real assets aligned with net-zero by 2030 | <ul style="list-style-type: none"> Focus on engagement with investment managers (including LCIV) initially. Mandate alignment will be considered alongside engagement; in particular any new commitments to unlisted assets |
| Engagement | <ul style="list-style-type: none"> Engage collaboratively, via the investment managers, with the most misaligned companies (at the portfolio level) in heavy emitting sectors. Deforestation, biodiversity loss, social factors and climate adaptation are key engagement topics Emissions data available and robust for all asset classes by 2025 | <ul style="list-style-type: none"> Identify key exposures through portfolio monitoring and raise issues with manager Engage to support improving data availability and quality |

Data, Asset Class Coverage and Emissions

The Fund's ambition is to be net zero by 2050 across the **entire** investment portfolio. However, existing limitations on data mean that only part of the strategy can be assessed quantitatively. Further, of the assets that can already be measured, estimates are heavily relied upon. Over time, it is expected that the coverage and quality of data will improve. The table below sets out the Committee's current assessment of data quality

| Mandate | Allocation | Comment on data coverage |
|--------------------|------------|---|
| Listed equities | 40.0% | Close to 100% coverage and data based on reported information from underlying companies |
| Multi-asset | 12.5% | As above for listed equity component. Estimates required across remaining assets |
| Property | 10.0% | c.40% coverage available and data reliant on estimates |
| Infrastructure | 12.5% | Data available of across all assets, though estimates necessary |
| Global credit | 5.0% | |
| Private debt | 7.5% | c.60% coverage available, though heavily reliant on estimates |
| Multi-asset credit | 7.5% | Data available covering the full investment, though heavily reliant on estimates |
| Gilts | 5.0% | Fully reliant on estimates |

Committee will engage with its investment managers, including the LCIV, to ensure that it obtains appropriate climate related data and reporting. Committee may also employ other third parties to provide additional reporting and analysis where necessary.

For the asset classes listed above there is a reasonable quality of data on scope 1 and 2 emissions and so the current targets and assessment of alignment will concentrate on these. However, given the significance of scope 3 emissions, Committee expects that consideration will be given to such emissions in reporting, analysis and the implementation of strategy.

While lack of data on other asset classes is an issue, it does not stop the Committee pursuing engagement activity and considering capital allocation into climate opportunities or solutions. Engaging with investment managers to develop good quality data is a primary goal for the Committee.

Baseline assessment

The Committee has collated data provided by each of its investment managers to establish a baseline position for the Fund against a series of initial metrics covering carbon emissions, exposure to fossil fuels and exposure to climate solutions. This position as at 31 March 2022 is set out in detail below.

| Mandate | WACI (tCO ₂ e / £m) | % of Portfolio with Fossil Fuel Ties | Exposure to Green Revenues / Climate Solutions |
|----------------|-----------------------------------|---|--|
| Equity | 153 | 2% | 2% |
| Multi-asset | 339 | 15% | 0% |
| Property | 41 | 0% | n/a |
| Infrastructure | 63 | 20% | 33% |
| Bonds | 132 | 5% | 10% |

*Asset class figures based on a weighted average of the underlying mandates for which data was available

The Committee will monitor progress against this baseline. Committee will also consider the introduction of additional metrics that align with its broader objectives.

Investment process

As an asset owner, there are two primary levers to move the investment portfolio towards a net zero emissions position - capital allocation and engagement. The Committee believes that a combination of both is likely to give the best chance of meeting their net zero goals although these considerations must be embedded within a broader investment process, with key considerations set out below.

Framing objectives

Committee will set objectives recognising that the broader goal is one of systemic change and the broader decarbonisation of global economic activities.

The Committee will be informed by an ongoing assessment of the Fund's exposure to climate related risks and opportunities and will use such assessments to frame appropriate goals or seeking additional information to allow the Committee to better understand how an objective may be set. When setting any objective, the Committee will also set out the actions it proposes to take in pursuit of the objective.

Objectives will be set on the understanding that there are gaps in the data, the likelihood that methodologies will change over time and on the understanding that the Committee's sphere of influence is limited to those it directly engages with. However, the Committee will seek to use its influence and that of its key stakeholders to push for change that will best allow it to achieve its goals.

Journey planning

The Committee will undertake analysis to assess the Fund's carbon position. This analysis will focus on the Fund's asset, sector, and regional allocations, comparing these to the levels required to reach the Fund's net-zero ambitions. This analysis will be built up to a portfolio level position. This approach is in line with the [IIGCC's Supplementary Guidance on Target Setting for a Net Zero Investment Framework](#), which recommends science-based net zero journeys at the portfolio level using a sectoral and regional approach.

The Committee recognises the importance of interlinked issues such as biodiversity loss and the social implications of transitioning to a low carbon economy. Considering this and building a nature positive investment strategy will be developed alongside the focus on reducing financed emissions.

Risk management

Committee will seek to understand exposure to physical and transition risks within portfolio, working with its managers to ensure that reporting on such exposures are provided.

Committee will work with its investment managers to define a set of acceptable standards with regard to how underlying managers account for and manage these risk exposures. Underlying managers will need to meet these standards on appointment and regular assessment will ensure that these standards are being upheld. Committee will managers compliance with these standards.

Identifying opportunities

The Committee considers two aspects to improving the current net zero pathway through capital allocation:

- **Reducing emissions** - Improve the current (and any future) mandates by allocating to more efficient companies within sectors and engagement relative to sector laggards or by engaging with laggards with the expectation of change. This includes recycling the proceeds of existing private assets into future products with better climate credentials
- **Remove emissions** - Increase allocations to assets that remove or avoid emissions with an initial focus on both natural capital and the displacement of emissions through technological advancement.

In both cases, Committee recognises that investment may be made in companies which are taking direct action (actors), or companies which support others in emissions removal (facilitators). The Committee will consider the following actions to better implement these options across the investment strategy:

- Ensuring that mandates have an aligned climate expectation, even where not formally stated as a mandate objective
- Setting minimum expectations around measurement and reporting of climate risk within mandates
- Considering allocating capital to mandates that emphasise climate solutions in line with the framework

The Committee will take an incremental approach to capital allocation changes as the data and opportunities evolves, balancing their fiduciary duties at all times.

The Committee intends to encourage LCIV to create compelling investment products that actively support the Fund's decarbonisation objective.

Active stewardship

Committee engagement with LCIV and investment managers

The Committee's primary means of engagement is with LCIV and its investment managers. Through this engagement, and using its influence to encourage LCIV and the investment managers in their own underlying engagement activities, the Committee believe that they have a significant influence on the decarbonisation actions of the organisations they finance.

The Committee will review the stewardship activity of LCIV and its investment managers on at least an annual basis. The Committee will establish clear expectations for its managers and LCIV and challenge any stewardship activity which falls below expectations. The Committee will report on this activity annually.

LCIV / investment manager engagement with underlying companies

LCIV and the Fund's investment managers have engagement programmes with the underlying companies in which they invest on the Fund's behalf. The Committee believe that through this engagement, portfolio companies can be encouraged to align to the decarbonisation pathways for the sectors in which they operate and set an appropriate strategy to align with these pathways. The goal being that cumulative emissions remain within the carbon budgets established for sectors and companies.

Stewardship is critical for investors to manage portfolio risk and real-world impact, especially in asset classes that are traded via secondary markets. Voting and engagement with companies enable investors to have significant influence on company strategy, operations, long-term sustainability and viability. The Committee believes that engagement is preferable to divestment, although the option to divest when engagement is unlikely to be effective or has failed should also be considered.

Measuring and accountability

A key part of the action needed to fulfil this plan is to measure, assess and report on the progress made against the targets set. The Committee has established the baseline by assessing the current investment strategy against across a range of climate related metrics. The Committee will ensure that such metrics are reassessed on at least an annual basis to support reporting on progress.

The Committee will undertake a periodic recalibration of its net zero journey plan and reassess its objectives and associated actions. To inform ongoing engagement activity the Committee will undertake at least one sector deep dive each year to inform engagement activity and monitor progress against targets.

Governance and reporting

The roles and expectations of the relevant stakeholders in relation to the Fund's climate ambitions are set out below.

| Stakeholder | Role | Expectations |
|--------------------|---|---|
| Committee | Ultimate responsibility to ensure the relevant actions are being taken to work towards the Fund's climate ambitions | <p>Ensure it has sufficient knowledge and skills to address climate considerations in its decision making</p> <p>Agree appropriate objectives based on discussion with other stakeholders and monitor progress against the key metrics on an annual basis</p> <p>Scrutinise and challenge the actions taken by others to ensure that the objectives are being met</p> <p>Report on the actions taken in line with regulatory requirements</p> |
| Officers | Support the Committee in ensuring that the Fund takes appropriate actions | <p>Ensure climate issues are being appropriately addressed throughout the investment process</p> <p>Ensure LGPS best practice is being captured and reflected in decision making, collaborating with others where possible</p> <p>Engage with managers, LCIV and advisers as necessary to ensure that climate ambitions are being achieved</p> |
| Investment adviser | Support the Committee/ Officers in developing and implementing the Fund's climate ambitions | <p>Provide education and advice to the Committee on the development of climate related objectives and an appropriate strategy to meet the objectives</p> <p>Provide analysis on climate related risks and opportunities, including in relation to both mandates and managers, and advise the Committee on any actions that can be taken in light of such analysis</p> <p>Support the Committee in its engagement and dialogue with other stakeholders</p> |
| London CIV/ | Primary pooling partner with responsibility for the development, implementation and oversight of appropriate asset strategies | <p>Embed the consideration of climate change into all product development, particularly the alignment of strategies with decarbonisation pathways</p> <p>Exercise active stewardship, including voting, over underlying assets to ensure that climate ambitions are appropriately communicated and challenged</p> <p>Provide the necessary information to allow the Committee to assess progress against its objectives</p> |

| | | |
|----------------------------------|---|--|
| <p>Other investment managers</p> | <p>Manage the Fund's assets in a manner aligned with Committee expectations</p> | <p>Ensure that climate considerations are embedded into product management</p> <p>Exercise active stewardship, including voting, over underlying assets to ensure that climate ambitions are appropriately communicated and challenged</p> <p>Provide the necessary information to allow the Committee to assess progress against its objectives</p> |
|----------------------------------|---|--|