How we manage climate-related risks and opportunities to the Scheme

A report for members
by the Trustee of the Baptist Pension Scheme
for the Scheme year ending 31 December 2022

Why have we written this report?

We are pleased to share with you the second TCFD report by the Trustee of the Baptist Pension Scheme. The report provides an opportunity for you to learn more about our work in relation to climate change.

We recognise that many of our members are interested to understand how we manage climate-related financial risks and opportunities. This report highlights our efforts in identifying and mitigating such risks and taking advantage of opportunities in the Scheme's investments. It also outlines our engagement with our fund managers to encourage the investee companies to adopt sustainable business practices and reduce their carbon footprint.

The UK has become the first G20 country to make it mandatory for Britain's largest companies and financial organisations to disclose their climate-related risks and opportunities.

We are proud to be part of a nation that has taken a significant step forward towards its commitment to make its financial system the greenest in the world.

As part of the Baptist Family we have long held the view that investments should be made ethically and our Ethical Policy includes environmental and climate-change issues. We welcome this initiative and the additional focus it has brought in this area.

We hope you find it informative and would welcome any feedback.

[Signature]

Chris Maggs

Moderator for Baptist Pension Trust Limited

Overview

The Trustee of the Baptist Pension Scheme views climate change as a risk to society, the economy and the financial system, but also recognises that reducing carbon emissions throughout the economy presents opportunities.

These risks and opportunities may impact the Scheme's financial position, for example by impacting the businesses the Scheme invests in. The Trustee monitors this potential impact and takes steps to reduce climate-related risks for members.

This report describes how the Trustee has identified, assessed and managed climate-related risks and opportunities to the Scheme during the Scheme year to 31 December 2022.

In June 2022, the defined benefit assets and liabilities were transferred to an insurer, with only residual assets remaining in the Scheme, which were in the process of being redeemed and passed to the insurer at the time of writing. Therefore, these assets are not included in this year's TCFD report.

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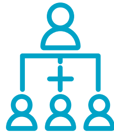
Published alongside the Scheme's annual report and accounts for the Scheme year to 31 December 2022 and available online [with link].

Key findings

1. **Governance – the Trustee has a robust framework for managing the Scheme, including setting clear expectations and responsibilities in relation to climate change.**

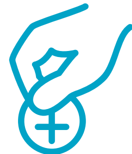


A Climate Governance Statement defines responsibilities of everyone involved

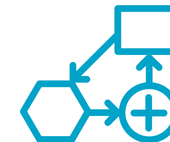
Climate-related risks and opportunities are reviewed regularly at Investment Committee meetings in light of the Trustee's ethical policy

The Scheme's advisers support the Trustee on climate-related matters

2. **Strategy and Risk Management – the Trustee has taken steps to understand how climate change might affect the Scheme and to control the risks it has identified. Based on the analysis carried out, the Trustee expects climate change to potentially impact the Scheme more significantly over the longer term. It aims to reduce the risks to the Scheme in several ways:**



Investing responsibly, in line with the Trustee's Ethical Investment Policy



Regularly reviewing the Scheme's investment managers' climate practices

3. **Metrics and Target – the Trustee has collected and reviewed information about the greenhouse gas emissions, carbon footprint and emissions reductions targets for the assets the Scheme invests in, to help it understand the Scheme's exposure to climate risks. It has set a target to increase the proportion of companies it invests in with science-based emissions reductions targets.**

Collected and reviewed greenhouse gas emissions data for the Scheme's investments

Reported proportion of investments with no data or estimated data

Agreed to use data quality as an additional climate-related metric to help it monitor climate-related risks

Monitored progress against the target for 80% of investee companies to have emissions reduction targets by 2030

Detailed report

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Section 1 – Governance

The roles of those undertaking, advising on or assisting with Scheme governance activities in identifying, assessing, and managing relevant climate-related risks and opportunities

The Trustee maintains a Climate Governance Statement (also known as "Roles and Responsibilities" document) which clearly lays out the distribution of responsibilities between the Trustee, Investment Committee and investment adviser in order to maintain appropriate oversight of the climate-related risks and opportunities relevant to the Scheme and so that the Trustee can be confident that its obligations are being met. This section reflects how the Scheme is currently governed, however, following the buy-in of the Defined Benefit Section, the Trustee is currently considering the future governance structure of the Scheme to ensure it remains appropriate and proportionate.

The Trustee uses outputs from TCFD-related activities to determine areas of focus for their climate-related governance activities.

The role of the Trustee

The Trustee of the Scheme has ultimate responsibility for ensuring effective governance of climate change risks and opportunities in relation to the Scheme. This is done by the Trustee Board and Investment Committee, with support from the Pensions Manager and the Trustee's external advisers.

As the Trustee has ultimate responsibility for scheme governance activities, its role is to review and discuss any information, decisions and proposals that have been made by the Investment Committee, the Governance and Risk Committee and/or its advisers. Having done so, the Trustee Directors will then confirm or amend any decisions or proposals made, and ensure the decisions are implemented appropriately. All decisions are ratified by the Trustee Board, including but not limited to decisions relating to climate change.

The Trustee role also includes:

- Agreeing training requirements and scheduling them into the business plan;
- Ensuring the climate governance arrangements remain appropriate and effective;
- Signing off the Trustee's investment beliefs, investment policies and risk register, including appropriate climate-related wording;
- Communicating with Scheme members and other stakeholders on climate change where appropriate.

The role of the Investment Committee

The Investment Committee provides the Trustee with regular updates and guidance following the reviews it has carried out and sets out any decisions that are required. It does this by:

- Reviewing and discussing all investment advice received, including ensuring appropriate consideration of climate change;
- Reporting back significant pieces of investment advice and recommendations to the Trustee, including any advice and recommendations relating to climate change;
- Ensuring any advice from the investment advisers is requested and carried out appropriately;
- Providing recommendations in respect of the investment advisers' competency;
- Meeting with the investment managers regularly and receiving updates on the managers' approaches to climate risk and opportunities;
- Reviewing the metrics and targets to assess climate-related risks and opportunities in relation to the Scheme's investment managers.

The role of the Pensions Manager

The Pensions Manager's role is to ensure that the Trustee Board, Investment Committee and its advisers have full access to all the information needed on the Scheme and to help implement any decisions made. The Pensions Manager attends the Trustee's climate-related training sessions and other opportunities for similar training from investment specialists in the pensions industry.

How the Trustee maintains oversight of climate-related risks and opportunities relevant to the Scheme

The Trustee Board and Investment Committee meet each quarter to discuss and make decisions regarding various topics related to the Scheme. As part of the work surrounding these meetings, the Trustee allocates significant time and resources to meeting its obligations on climate change governance and reporting. TCFD-related activities, such as monitoring climate metrics and reviewing the climate practices of the Scheme's investment managers, regularly represent substantive agenda items.

This structure allows third parties with climate-related responsibilities, such as investment advisers and investment managers, to have clear monitoring and review frameworks of how and when they inform trustees of their work. The oversight structure therefore provides clear lines of communication between the Trustee and those working on climate-related risks and opportunities relevant to the Scheme. From time to time, the Trustee will review the climate competency of its advisers and take appropriate action if any concerns are identified.

With appropriate advisers in place, the Trustee ensures that climate-related risks and opportunities are considered as part of any relevant advice, such as the investment strategy review.

The Trustee also ensures that the Investments and Governance and Risk Committees have suitable experience in considering climate risk, to ensure that risks are suitably considered, documented, reviewed and kept up to date.

Oversight activity – at the regular Trustee Board meeting

At its regular Board meeting each quarter, the Trustee receives and reviews:

- An update from the Governance and Risk Committee which includes any recent review of the Scheme's risk register. Where appropriate, this includes updates in relation to the climate-related risks and opportunities identified in the risk register.
- An update from the Investment Committee on the Scheme's investments. Where appropriate, these include updates in relation to the investment managers' climate policies, and their assessment of relevant climate-related risks and opportunities.

Oversight activity – by the Investment Committee

The Investment Committee considers climate-related risks and opportunities within each investment topic and individual mandates as and when they arise at quarterly meetings. The Investment Committee also reviews (at least annually):

- A responsible investment report from the Scheme's investment adviser that reviews the Scheme's investment managers in relation to environmental, social and governance (ESG) factors and climate change;
- Data on climate-related metrics and progress against the target set in relation to these metrics;
- Whether it is appropriate to update the climate scenario analysis that illustrates how the Scheme's assets might be affected under various climate change scenarios;
- Their advisers' climate competency including assessing how they have performed against their climate responsibilities.

Oversight activity – other regular items

The Trustee also considers climate-related risks and opportunities whenever a review of the investment strategy is undertaken.

Oversight activity – appointments

Whenever it reviews its agreements with external advisers, or appoints new advisers, the Trustee also considers and documents the extent to which the advisers' climate-related responsibilities are included in the agreements and/or any adviser objectives set. In particular, the following objectives have been set for the investment adviser that are relevant to climate considerations:

- Take into account the Scheme's ethical policy, ESG and stewardship considerations in advising on the implementation of the Scheme's investment strategy;
- Help the Trustee understand climate risks within each investment mandate vs the Trustee's investment beliefs;
- Inform the Trustee of regulatory changes and assist the Scheme in becoming compliant.

Trustee training

The Trustee recognises the importance that the climate-related information provided by third parties is fully understood and can be critically challenged by the Trustee Board, where appropriate. In order to help with this, the Scheme's investment adviser delivers training to the Trustee and/or the Investment Committee on a range of climate risks and opportunities.

During 2022, the Trustee and Investment Committee allocated meeting time to climate-related topics and commissioned additional advice to be better placed to satisfy its regulatory obligations. Agenda items included the following:

- Training on the findings in the Scheme's first TCFD report (June 2022);
- Training on the new requirement for a fourth metric, and review of metrics and targets for TCFD reporting (November 2022);
- Stewardship priorities training, which identified climate change as a key priority for the Trustee (November 2022).

The processes by which the Trustee satisfies itself that the relevant third parties are taking adequate steps to identify, assess and manage those risks and opportunities

The Trustee seeks to ensure that any third parties assisting the Trustee in undertaking governance activities have suitable climate-related risk expertise and resources to carry out their role.

The Trustee considers and documents climate-related responsibilities in Scheme documents and agreements, such as the Statement of Investment Principles, the Ethical Investment Policy, the investment adviser's strategic objectives and service agreements.

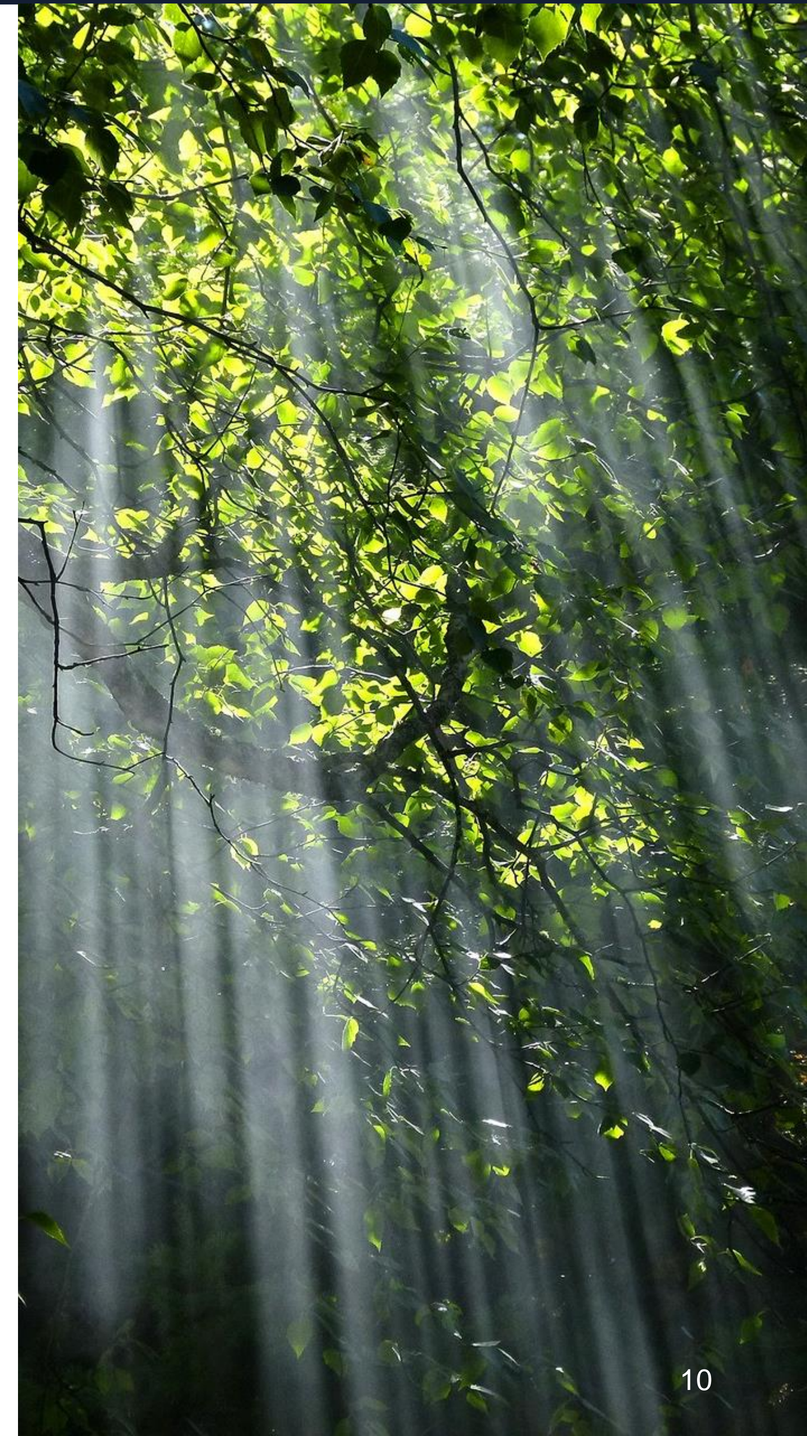
In particular, the Trustee incorporates its beliefs and policies on climate-related risks into its Statement of Investment Principles and Ethical Investment Policy, which help to define the investment strategy for the Scheme. This process allows the Trustee to engage with the relevant parties, either directly or through its investment adviser, to satisfy themselves that climate-related risk has been adequately prioritised.

Climate-related beliefs within the Statement of Investment Principles

- The Scheme's Statement of Investment Principles (SIP) is designed to reflect the Department for Work and Pensions (DWP)'s 2018 guidance on matters pertaining to environmental, social and governance (ESG), including climate change.
- The Trustee believes ESG factors are likely to be one area of market inefficiency and so managers may be able to improve risk-adjusted investment returns by taking account of ESG factors including factors relating to climate change. This is one of the Trustee's key investment beliefs, which influence the setting of the investment arrangements.
- The Trustee has considered how ESG considerations, including climate change, should be taken into account in the selection, retention and realisation of investments, given the time horizon of the Scheme and its members.
- The Trustee expects its investment managers to take account of financially material considerations, including climate change. The Trustee seeks to appoint managers that have appropriate skills and processes to do this, and from time to time reviews how its managers are taking account of these issues in practice. The Trustee recognises that it has limited influence over managers' investment practices where assets are held in pooled funds, but it encourages its managers to improve their practices where appropriate.
- The Trustee is responsible in respect of investment matters for formulating a policy in relation to financially material factors and exercise of rights and engagement activities in respect of the investments, such as those relating to ESG considerations, including climate change.
- The Trustee expects its investment managers to take account of financially material considerations, including climate change, as appropriate when managing the portfolios of assets.
- The Trustee expects its investment adviser to be responsible, in respect of investment matters, as requested by the Trustee, for advising on the selection, and review, of the investment managers, incorporating its assessment of the nature and effectiveness of the managers' approaches to financially material considerations, including climate change.

The Scheme's SIP explicitly identifies climate change as a source of risk, which could be financially material over both the short and longer term. This risk is defined as relating to the transition to a low carbon economy, and the physical risks associated with climate change, such as extreme weather events. The Trustee seeks to appoint investment managers who will manage this risk appropriately, and from time to time reviews how this risk is being managed in practice.

During the Scheme year, the Trustee set Stewardship Priorities for the Scheme, to provide a focus for monitoring investment managers' voting and engagement practices. Climate change was identified as a priority for the Scheme, alongside human rights. These priorities have been reflected in the Statement of Investment Principles following the end of the Scheme year and have been communicated to Legal and General, the Scheme's main DC investment manager. The Stewardship Priorities will also be considered when selecting new investments, as well as in the monitoring of existing investments.



Climate-related policies within the Ethical Investment Policy

The Trustee seeks to achieve an acceptable balance between risk, reward and ethical considerations in its Ethical Investment Policy that will satisfy this expectation and the conscience of the Baptist constituency. The Trustee must at all times satisfy itself that its action in applying an ethical investment policy will not involve significant financial detriment.

The Scheme invests in pooled funds and, in selecting which pooled funds to make available, the Trustee takes into account ethical issues. In particular, the Trustee seeks to select funds that comply as closely as possible with its Ethical Investment Policy, taking into account availability of suitable funds and their management cost but recognises the Trustee cannot dictate specific ethical requirements to the fund managers.

Through its Ethical Investment Policy, the Trustee seeks a constructive engagement with the corporate world, investing in companies that will successfully develop their business financially where responsible business practices and high standards of corporate behaviour are encouraged and supported. This policy includes the use of different approaches as described below:

- Investing in companies or sectors which reflect Christian values in areas including environmental protection, supporting sustainable development and health (including healthy food).
- Avoiding investment in companies or sectors undertaking a particular activity or operating in a way which may be harmful and inconsistent with the Scheme's Christian values and ethos. The Trustee will therefore avoid investment in companies with significant trading in certain areas, including the extraction, production and refining of fossil fuels. Significant trading or involvement is normally taken to mean greater than 10% of turnover.
- Stakeholder Activism, whereby the Trustee seeks to influence a company's policies towards those which better reflect the Scheme's values and ethos. The Trustee is in regular dialogues with the Scheme's investment managers to understand how they have exercised company voting rights, noting the Trustee's agreed stewardship priorities, climate change and human rights. These stewardship priorities are also considered on an ongoing basis in fund retention and selection.

Identification and assessment of climate-related risks and opportunities relevant to the Scheme

The Trustee recognises that climate change is likely to affect members differently depending on the investments held and the length of time considered. The Trustee has considered climate-related risks and opportunities over various time periods which it believes are most relevant to the Scheme.

The Trustee has selected short, medium and long-term time horizons over which to formally consider the impact of climate related risks and opportunities for the Scheme. These are shown in the table below, alongside the main reason why each period was chosen. Time horizons for the Defined Benefit section have not been included in the table as it entered into a bulk annuity contract to fully insure its liabilities in June 2022.

Time horizon	Years	Reason
Short term	Up to 5 years	Major improvements in climate data quality are expected over this period.
Medium term	5 to 10 years	Key period over which policy action will determine if Paris Agreement goals can be met.
Long term	10 to 27 years	Many developed economies are targeting to be net zero by this point

When selecting the above time horizons, the Trustee has considered the expected timeframe over which current members' monies will be invested to retirement and the actual investments members are expected to hold.

The Trustee recognises that members face risks and opportunities from both the physical effects of climate change, such as rising temperatures and more extreme weather events, as well as from the effect of transitioning to a lower carbon economy to help mitigate the impacts of climate change, such as government policies to reduce the use of fossil fuels, technological advantages in renewable energy, and shifts in consumer demand for "greener" products. Many of these climate-related risks and opportunities could impact the value of the Scheme's assets.

The Trustee has identified the following relevant climate-related risks and opportunities in relation to the Defined Contribution Section over the following time horizons:

Time horizon	Risks	Opportunities
Short term	Older members within 10 years of retirement will be most exposed to transition risks in the short term in the event of a Paris disorderly Pathway.	Low carbon investments can mitigate the impact of market shocks due to a market repricing event.
Medium term	Transition risks may still be heightened over the medium-term creating volatility. Market returns may be lower if disorderly transition harms economic performance.	Impact investments can take advantage of the shift to a low carbon economy and may provide an enhanced source of return over this period.
Long term	Physical risks are most prevalent in the failed transition pathway, impacting those members 20 years or more from retirement.	Engagement with investment managers to ensure they are exercising stewardship in support of net zero pathways is key to avoiding a failed transition.

The climate-related risk and opportunities feed into the Trustee's policies in various ways including the Scheme's Ethical Investment Policy. The investment managers are asked to disclose whether the funds they manage on behalf of the Scheme are in compliance with the Scheme's Ethical Investment Policy (the latest iteration of this policy shared with the managers is dated March 2023 at the time of writing). Whilst some of the investment managers are not able to report alignment with our specific criteria, our investment adviser considers this alignment in detail and reports any concerns to the Trustee on a regular basis. Overall, the investment managers' Responsible Investment practices were believed to be broadly in line with expectations following the most recent review in November 2022 (based on the version of the Ethical Investment Policy dated November 2022).

To capture the opportunities associated with the transition to a low carbon economy, the Trustee offers a Low Carbon UK Equity fund as an investment option for members. This fund invests in the UK equity market while on a de-carbonisation path to achieve net zero by 2050. The investment manager may exclude companies that fail to meet pre-defined minimum standards in low carbon transition and corporate governance standards.

The Trustee also offers an Ethical Global Equity fund as an option investments can choose. The fund follows an investment philosophy that aims to invest in companies demonstrating specific Environmental, Social and Governance ("ESG") practices. Minimum climate change score thresholds apply in assessing eligibility for both existing and new investments in this fund. These scores take into consideration the sector that particular company operates in.

The Trustee engages with current and prospective investment managers on matters including climate change but does not monitor or engage directly with issuers or other holders of bonds or equities.

1. Stewardship priorities

The Trustee has selected priority themes to provide a focus for the monitoring of investment managers' voting and engagement activities. The Trustee will review these regularly and update them if appropriate. The current priorities are climate change and human rights.

The Trustee chose these priorities because they are considered market-wide areas of risk that are financially material for the Scheme's investments, aligned with the interests of the Scheme's members and the Trustee believes they can be addressed by good stewardship. Therefore, the Trustee decided it is in members' best interests that the Scheme's managers adopt strong practices in these areas.

The Trustee has written and continues to write to Legal and General, its main Defined Contribution Section investment manager regularly to notify it of the Trustee's stewardship priorities and remind them of its expectations of them in relation to responsible investment, including climate change considerations in voting and engagement.

2. Manager selection

The Trustee seeks to appoint investment managers that have strong responsible investment skills and processes. The Trustee favours investment managers who are signatories to the Principles for Responsible Investment, UK Stewardship Code and Net Zero Asset Managers Initiative.

When selecting new managers, the Trustee considers its investment adviser's assessment of potential managers' capabilities in this area. If the Trustee meets prospective managers, the Trustee usually asks questions about responsible investment, focusing on the stewardship priorities discussed above.

3. Manager monitoring

The Investments Committee receives information regularly to enable them to monitor the Scheme's managers' responsible investment practices and check how effective these are.

This information includes metrics such as the investment adviser's responsible investment grades for each manager, whether they are signatories to the responsible investment initiatives listed above, and (where available) carbon emissions data for the Scheme's mandates.

4. Annual responsible investment review

Each year, the Investments Committee undertakes a more comprehensive review of its managers' responsible investment practices. This includes the investment adviser's qualitative responsible investment assessments for each manager, including how the manager mitigates climate change risk.

5. Ongoing cycle of manager engagement

Given that responsible investment is rapidly evolving, the Trustee expects most managers will have areas where they could improve. The Trustee therefore aims to have an ongoing dialogue with its managers to clarify its expectations and encourage improvements. In particular, investment managers have been routinely invited to meetings with the Investments Committee and the investment adviser, although the Trustee is reviewing if this along with its wider review of governance arrangements over the next year.

The Trustee reviews the information provided to them by its investment adviser to identify any concerns, for example where the managers' actions are not aligned with the Trustee's views. Where there are concerns, the Trustee typically seek further information through its investment adviser.

Climate scenario analysis

The Scheme's first climate scenario analysis was carried out in the Scheme year ending 31 December 2021. Further information regarding modelling approach and outcomes can be found in Appendix 2. The Trustee reviewed whether it is appropriate to update this analysis in November 2022. It was agreed that there have not been any material changes for the assets under scope, in the availability of data or investment strategy, industry practice or modelling capabilities which warrant updating the climate scenario analysis for this report. In June 2022, the defined benefit assets were bought in by an insurer and only held residual assets which are in the process of being redeemed and passed to the insurer. Therefore these assets have not been included in this year's TCFD report.

The Defined Contribution Section climate scenario analysis undertaken for the Scheme year ending 31 December 2021 looked at the retirement outcomes (in terms of the size of their retirement pot) for individual members of different ages who are invested in the default strategy. The analysis highlighted that members will be subject to climate risks to varying degrees depending on the climate scenario. In general, the default strategy has been designed in a way which reduces investment risk as members approach retirement. Climate risks are generally expected to have the greatest impact on return-seeking assets such as equities. In the default strategy, exposure to these assets is reduced as members approach retirement, which should help to reduce their exposure to climate risks.

The results of the climate scenario analysis are summarised in the table below. It shows how much lower expected pot sizes at retirement will be in different

Scenario	Member aged 25	Member aged 35	Member aged 45	Member aged 55
Paris Orderly outcome	-5.9%	-3.0%	-1.2%	-0.8%
Paris Disorderly outcome	-7.9%	-5.9%	-4.9%	-4.2%
Failed Transition outcome	-22.7%	-19.1%	-11.2%	-1.4%

The Trustee noted the following key conclusions from the modelling results:

- The Paris Orderly scenario leads to the best outcome for members as in this scenario the climate risks are relatively low.
- The Paris Disorderly scenario includes a market shock in the short term which impacts return-seeking assets the most. This has a muted impact on most members' retirement pots as they have time to recover through future investment returns and contributions. Members within 10 years of retirement hold a low and decreasing amount of return-seeking assets so they are impacted less than younger members under this scenario.
- The Failed Transition scenario has limited short term effects but larger long term effects as it assumes increasingly severe physical impacts of climate change emerge over time. This scenario particularly impacts younger members who remain invested in the Scheme for longer.
- The analysis confirmed the importance of managing climate-related risks to members' pots. The Trustee does this by: ensuring the Scheme's investment managers have strong climate practices; reducing members' exposure to return-seeking assets as they approach retirement; and using stewardship to encourage the companies the Scheme invests in to improve their climate practices.

Section 3 – Risk management

The Trustee has implemented a number of processes and tools for identifying, assessing and managing climate-related risks and opportunities, including:

- attending regular training on various climate-related topics, for example training on stewardship priorities and tools for integrating the trustee's climate change stewardship priority into Scheme policies;
- undertaking climate scenario analysis which shows how the Scheme's assets might be affected under a range of climate scenarios;
- reviewing its investment adviser's assessments of the Scheme's investment managers' climate practices;
- ensuring good stewardship practices are in place
- monitoring a range of climate-related metrics in relation to the Scheme's assets; and
- ensuring its advisers have processes in place to help it research its investment managers' climate-related practices.

In addition, the Trustee expects its investment managers to identify, assess and manager climate-related risks to the Scheme's assets on a day-to-day basis. The above processes are integrated into the overall risk management of the Scheme through the business plan, the risk register and regular support from its advisers. The Trustee's risk register is updated regularly to ensure all risks are being monitored and managed consistently and proportionately.

These processes and tools have helped the Trustee consider issues such as:

- Which climate change risks are most material to the Scheme;
- How to take account of transition and physical risks across different asset classes; and
- How climate change affects the Trustee's risk appetite.

The processes and tools are used to identify the key risks and opportunities that the Trustee should focus on and should be considered in the investment decision processes.

The Trustee has used the climate scenario analysis as a key tool for identifying, assessing and managing climate-related risks and opportunities. In particular, the analysis was used to identify the time horizons over which the physical risks and transition risks could materialise (see page 11). The Trustee has considered what the possible impacts of climate change could be over each of these time horizons and whether its investment strategies are likely to be robust against these risks (or able to take advantage of any opportunities).

Ethical Investment Policy

The Trustee has an Ethical Investment Policy which was most recently updated in March 2023, to focus more on the DC assets of the Scheme following the buy-in of DB assets in June 2022. The Investment Committee is also responsible for monitoring how well the Scheme's investment managers are aligning to this policy. The purpose of the policy is to encourage companies to act responsibly in the interests of their shareholders, employees and other stakeholders.

The policy specifically addresses climate risks by excluding fossil fuel extraction companies, unless a company is deemed to be moving significantly to sustainable energy policies. The Ethical Policy was expanded from 9 December 2021 to exclude companies with significant trading in all extraction, production and refining of fossil fuels. The policy specifically addresses climate opportunities by allocating to companies involved in environmental protection and supporting sustainable development. As stated in the policy, the Trustee regards itself as "stewards of the world" and will avoid investment in companies that act without proper regard to the environment.

The Trustee, with help from its Investment Committee and advisers, has sought to align all funds with its ethical and climate beliefs, where possible, but notes this is challenging for a scheme of our size which requires the use of pooled funds.

Annual Responsible Investment Review - Process

The latest Annual Responsible Investment Review was produced by the Scheme's investment advisers in November 2022 and includes:

- a summary of each of the Scheme's investment manager's Responsible Investment processes, including the Scheme's investment adviser's view of their ESG practices;
- a summary of the Scheme's investment manager's climate approaches, including the Scheme's investment adviser's view on how climate considerations apply to each asset class; and
- any recommended action.

The Annual Responsible Investment Review identified which of the Scheme's funds have strong climate policies and the funds for which there are opportunities to consider taking action, noting any action would need to be proportionate based on the expected benefit for members (for example, the cost associated with taking action may outweigh the potential benefits for funds that only represent a very small proportion of members' assets).

Annual Responsible Investment Review - Findings

Overall, the investment managers were believed to be broadly in line with their peers in terms of managing ESG and climate risks.

The report identified the funds for which climate-related risks are an important part of the investment process. These funds have lower carbon exposure compared to the average fund with similar characteristics. In particular, one active equity fund and one passive equity fund were identified as having strong climate policies (which was expected given ESG factors, including climate risk, are an important part of the Trustee's manager selection process).

Some of the funds have an ethical focus which include policies that reduce the exposure to climate-related risks. The review noted that other funds are available, such as low carbon equity funds, that have lower carbon exposure than these ethical funds. However, these alternative funds were less well aligned with other parts of the Trustee's Ethical Investment Policy. This compromise, along with the potential transaction costs to change, meant the Investment Committee did not believe lower carbon funds were appropriate at this time.

Investment monitoring

In addition to the Annual Responsible Investment Review referenced above, the Scheme's investment advisers provide quarterly investment performance monitoring reports to the Investment Committee for discussion. Any concerns in relation to the investment managers are being monitored as part of this process.

The Investment Committee is responsible for carrying out an annual responsible investment review.

The Investment Committee also receives and reviews detailed climate metrics data from its investment adviser and investment managers, on an annual basis. In November 2022, the Trustee agreed to add Data Quality as an additional climate change metric to the previously agreed three metrics, which was included in this year's annual reporting. The calculations and reporting of these metrics, along with other climate risk exposures, were discussed at the November 2022 meeting. The reporting included a comparison of the climate characteristics of each fund with the climate characteristics of a suitable index. Climate metrics are reported in the next section of this report.

Risk register

The Trustee maintains a risk register covering the wide range of risks run in the Scheme. The Governance and Risk Committee maintains and updates the risk register, with any amendments notified to the Trustee Board.

Climate risk areas included in the risk register include:

- Knowledge and understanding of climate risks
- Compliance with climate risk legislation
- Regular review of climate risks relevant to the investment strategy
- Reputational risks of not tackling climate risk appropriately
- Inadequate communication with members on climate risk.

These are reviewed regularly to consider if any further risks need adding or amending, to assess any significant priority risks to manage and to ensure regular action is maintained in monitoring and mitigating these risks.

The Trustee's current assessment, based on consideration of their impact and likelihood, is that climate-related risks are fairly low risk for the Scheme and therefore should continue to be monitored in accordance with the current monitoring processes.

Stewardship

The Trustee expects the Scheme's investment managers to engage with investee companies on climate-related (and other) matters. The Trustee generally believes that engaging with companies is more effective at encouraging change than selling the Scheme's investments in those companies. Stewardship is therefore used to help manage climate-related risks. Voting and engagement activities are delegated to the individual investment managers. Each manager has its own ESG policy, which includes assessment of climate-related risks and policies on voting on climate-related resolutions.

More information on the Trustee's stewardship activities can be found in its Implementation Statement.

In November 2022, the Trustee selected priority themes to provide a focus for its monitoring of investment managers' voting and engagement activities. The Trustee will review these priorities regularly and update them if appropriate. The Scheme's current priorities are climate change and human rights. The Trustee chose these priorities because they are market-wide areas of risk that are financially material for the Scheme's investments, aligned with the interests of the Scheme's members and can be addressed by good stewardship. Therefore, the Trustee believes it is in members' best interests that managers adopt strong practices in these areas. The Trustee has written to the Scheme's investment managers notify them of the Scheme's stewardship priorities and remind them of the Trustee's expectations of them in relation to responsible investment – including ESG considerations, climate change, voting and engagement.

In order to monitor how the individual investment managers are exercising their voting rights and undertaking engagement on behalf of the Trustee, the Investment Committee:

- periodically meets with the Scheme's investment managers, to engage with them on how they have considered **climate change** and human rights (the Scheme's stewardship priorities) within their stewardship activities and will seek to challenge the investment managers on these matters where they think this is in the best interests of members; and
- further monitors the investment managers by receiving stewardship and governance reports from the investment managers on a quarterly basis.

Section 4 – Metrics and Targets

Metrics

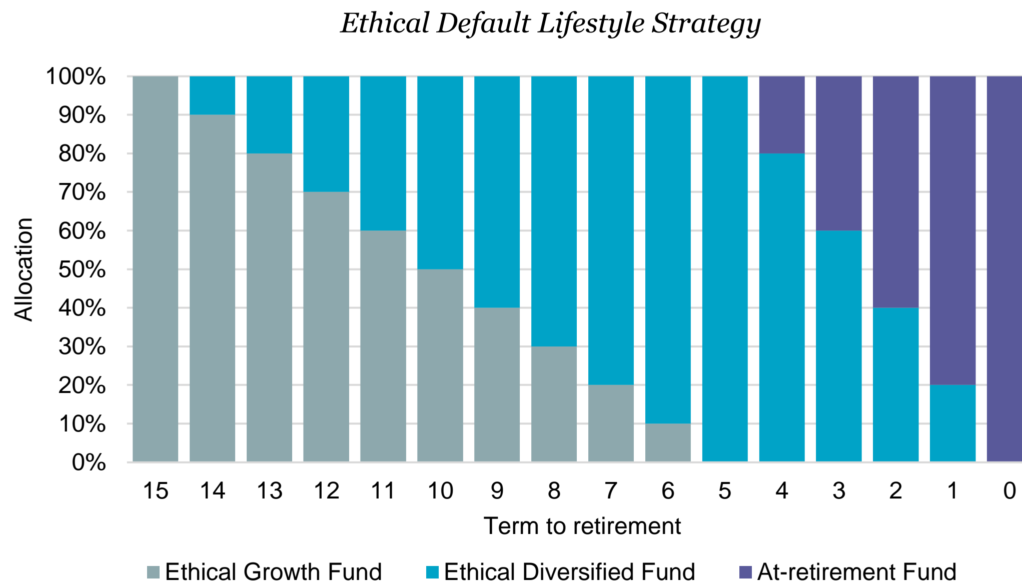
The Trustee has chosen four climate-related metrics to help it monitor climate-related risks and opportunities relevant to the Scheme. These are listed below and reported overleaf (as far as the Trustee was able to obtain the data).

Metric	High-level methodology
Absolute emissions: Total greenhouse gas emissions	The sum of each company's most recent reported or estimated greenhouse gas emissions attributable to the Scheme's investment in the company, where data is available. Emissions are attributed evenly across equity and debt investors. Reported in tonnes of CO_2 equivalent. This methodology was chosen because it is in line with the statutory guidance.
Emissions intensity: Carbon footprint	The total greenhouse gas emissions described above, divided by the value of the invested portfolio in £m, adjusted for data availability. Emissions are attributed evenly across equity and debt investors. Reported in tonnes of CO_2 equivalent per £1m invested. This methodology was chosen because it is in line with the statutory guidance.
Portfolio alignment: Science-based targets	The proportion of the portfolio by weight of companies that are aligned with a Net Zero, demonstrated by a target approved Science Based Targets initiative (SBTi) or equivalent. Reported in percentage terms. The Trustee chose this "binary target" measure because it is considered the simplest and most robust of the various portfolio alignment metrics available.
Data quality	This is the proportion of the portfolio for which each of Scope 1-2 emissions and Scope 3 emissions are **verified, reported, estimated or unavailable**.

The data has been calculated using portfolio holdings as at 30 September 2022, using the most recent data available in November 2022, from the investment adviser's appointed climate metrics provider, MSCI. The Trustee was unable to source data on the cash fund.

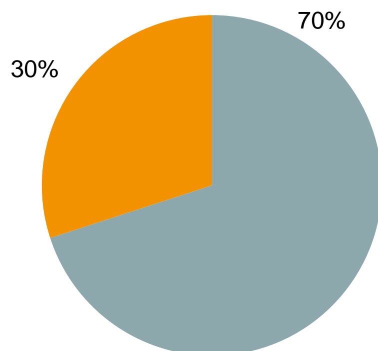
The majority of assets are invested in the default strategy, with the assets allocated depending on members' expected retirement dates, as shown in the charts overleaf. As at 30 September 2022, 88.5% of assets were invested this strategy. The remaining assets are invested in a range of self-select funds, the largest self-select fund allocation being c3.5% (£2.2m). The Trustee has not collected metrics for the self-select funds as it did not feel it was proportionate to do so. This is in line with the guidance issued by the Department for Work and Pensions.

The default investment strategy allocations are shown on the next page. The first chart shows the allocation to the three default funds for members of different ages (based on time to retirement). The following pie charts show the allocations to the various asset classes within each of the three funds used in the default strategy.

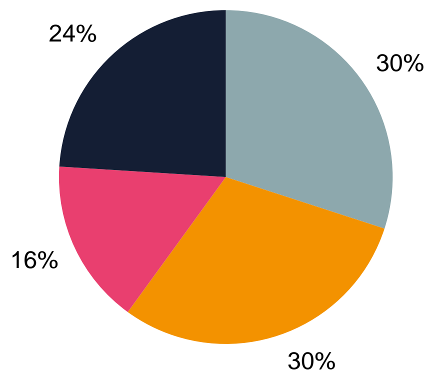


Each of the funds in the chart above invests across a number of asset classes. The pie charts below show the allocation for each fund. The remainder of this section reports climate metrics for the Scheme's default strategy, split by the same asset class categories.

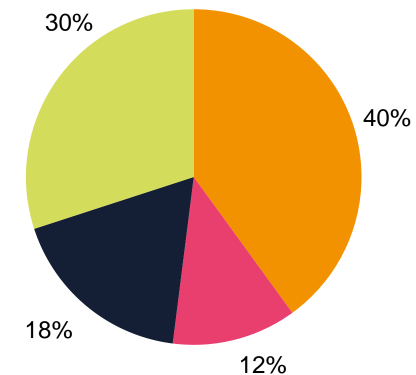
Ethical Growth Fund



Ethical Diversified Fund



At-retirement Fund



Ethical global equities   Diversified Fund   Corporate Bonds   Government Bonds   Cash Fund

Total Scheme coverage of 82%

Asset class (% assets)	High-level methodology
Ethical Global Equities (50%)	See Appendix 3.
Corporate bonds (6%)	
Diversified Fund (33%)	
Government bonds (9%)	The carbon emissions and SBTi alignment are not directly reported by the UK government. The Scheme's investment adviser, LCP, has estimated these figures based on a number of assumptions including: the greenhouse gas emissions produced in the UK; the value of the UK's public debt; the value of the Scheme's investments; and the Net Zero commitments made by the UK government. Different estimates of emissions data may differ materially from those calculated by LCP due to differences in methodologies, sources of data and/or dates of calculation.
Cash (2%)	There are significant gaps in reporting climate data for this asset classes. The Trustee, through its investment adviser, continues to work with its investment managers to improve data reporting over time.

Metrics collected

Manager, asset class and valuation (£m)		Scope 1 and 2 emissions (for holdings with data)			Scope 3 emissions (for holdings with data)			Emissions targets	Data source	Date of portfolio value and holdings
		Coverage (%)	Total GHG emissions (tCO_2e)	Carbon footprint (tCO_2e/£m)	Coverage (%)	Total GHG emissions (tCO_2e)	Carbon footprint (tCO_2e/£m)	Proportion with science-based target (%)		
Ethical Global Equities	28.2	99.7	1,286	46	99.5	8,856	317	48.7	MSCI	30/09/22
Corporate bonds	3.5	36.5	27	21	36.3	404	322	13.0	MSCI	30/09/22
Diversified Fund – equities and corporate bonds	18.7	87.7	876	84	87.1	4,902	474	25.5	MSCI	30/09/22
Diversified Fund – government bonds, specialist asset classes*		Not available	Not available	Not available	Not available	Not available	Not available	Not available	-	30/09/22
Government bonds	5.9	100.0	1063	181	100	914	156	100.0**	LCP	30/09/22
Cash	1.1	Not available	Not available	Not available	Not available	Not available	Not available	Not available	-	30/09/22

The carbon footprint of Ethical Global Equities is higher than that of corporate bonds but lower than for the equities and corporate bonds held in the Diversified Fund (lower is better). The Ethical Global Equities index is most effective in reducing the carbon footprint of the fund. Nevertheless, the majority of the Scheme's total emissions come from the allocation in the Ethical Global Equities because of the large proportion of the Scheme's assets invested in it.

Scope 1, 2 and 3 emissions of the Ethical Global Equities and corporate bonds are significantly reduced over the year to 30 September 2022. Whilst the total GHG emissions of the diversified funds (equities and corporate bonds) increased over the year to 30 September 2022, their Scope 1 and 2 carbon footprint is reduced over the same period.

The proportion of holdings with SBTi portfolio alignment targets is also highest for Ethical Global Equities (excluding the government bonds) (higher is better). The Trustee has a long-term target related to this metric which is shown on page 24.

The Trustee, with help from its investment adviser, continues to work with the Scheme's investment managers to improve data reporting over time. The Trustee considers both risks and opportunities related to carbon metrics when reviewing its investments.

Source: Investment managers, MSCI, LCP.
Certain data ©2022 MSCI ESG Research LLC. Reported by permission. See Appendix 3 for more details, including how to interpret data where coverage is less than 100%.
*Such as property, commodities, and alternative credit.
**The UK has a net zero by 2050 target written into law, with carbon budgets based on advice from the independent Committee on Climate Change, so UK government bond exposure has been treated as having a credible science-based target.

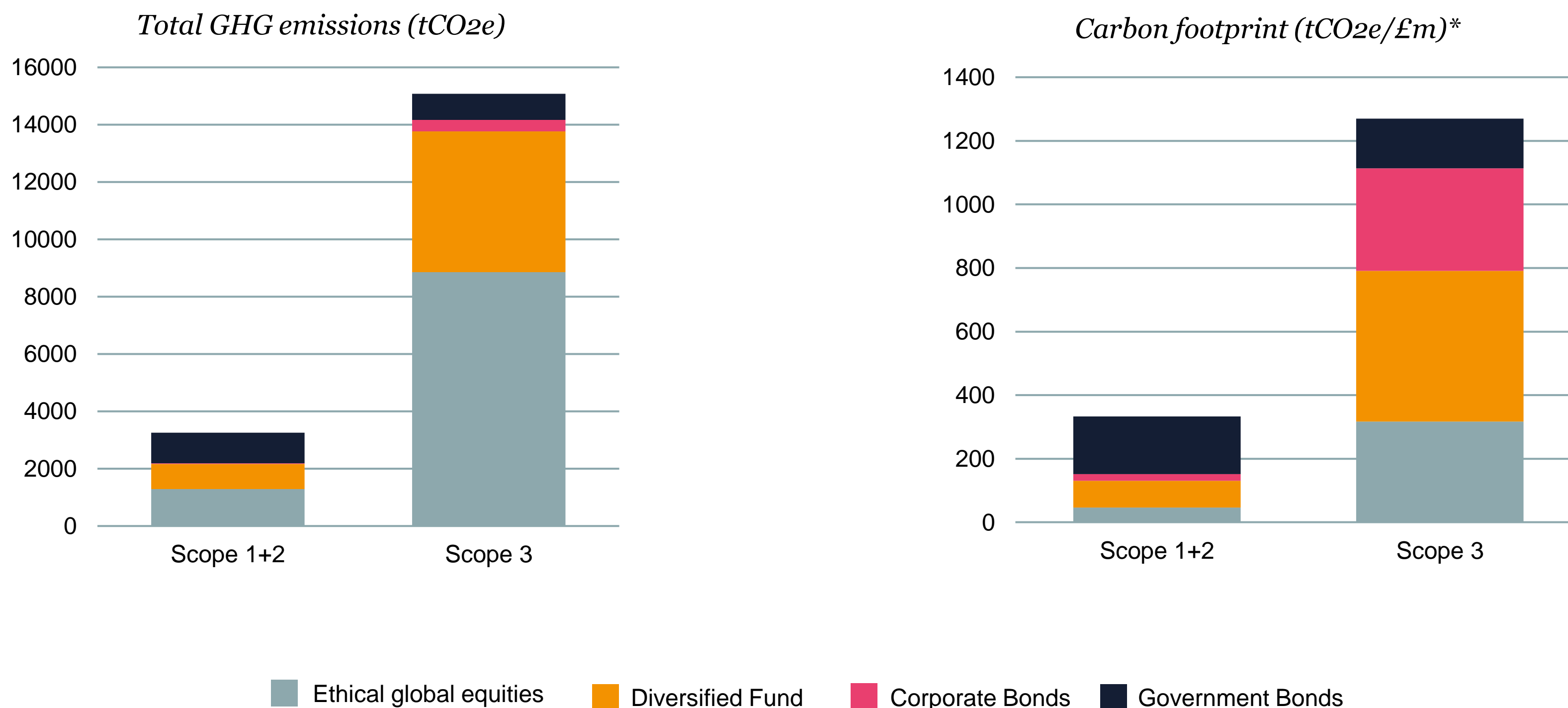
The charts on the next three pages summarise the data shown on the previous page.

The main emissions data gaps relate to the cash and specialist asset classes. The coverage is reasonable but still leaves significant gaps in greenhouse gas emissions metrics. The Trustee encouraged the investment manager to engage with portfolio companies that do not yet disclose information on greenhouse gas emissions.

Emissions coverage is high for Ethical Global Equities, the listed passive equity fund used in the default strategy.

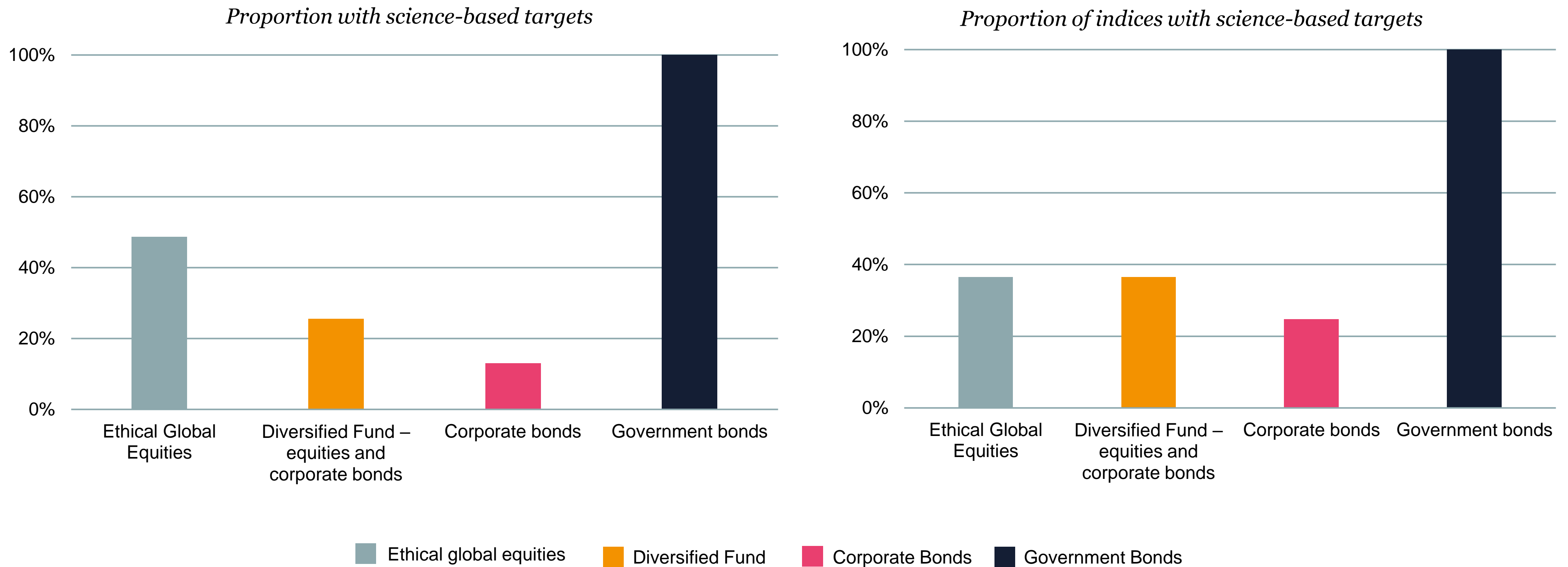
All Scope 3 emissions data is estimated by MSCI, even where reported emissions are available. This provides greater consistency than using a mixture of reported and estimated emissions. Analysis of reported Scope 3 emissions suggests that the data quality is currently low: data is volatile and often out of date, with relatively few companies reporting on all types of Scope 3 emissions. In contrast, MSCI estimates all types of Scope 3 emissions for most companies in its database, for a recent reporting year and using a consistent approach.

MSCI's data does not distinguish between companies which do not have an SBTi target and companies for which the SBTi status is not known. The Trustee's investment adviser continue to engage with MSCI to address this.



Source: Investment managers, MSCI, LCP.
Certain data ©2022 MSCI ESG Research LLC. Reported by permission. See Appendix 3 for more details, including how to interpret data where coverage is less than 100%.
*Such as property, commodities, and alternative credit.
**The UK has a net zero by 2050 target written into law, with carbon budgets based on advice from the independent Committee on Climate Change, so UK government bond exposure has been treated as having a credible science-based target.

Section 4 – Metrics and Targets

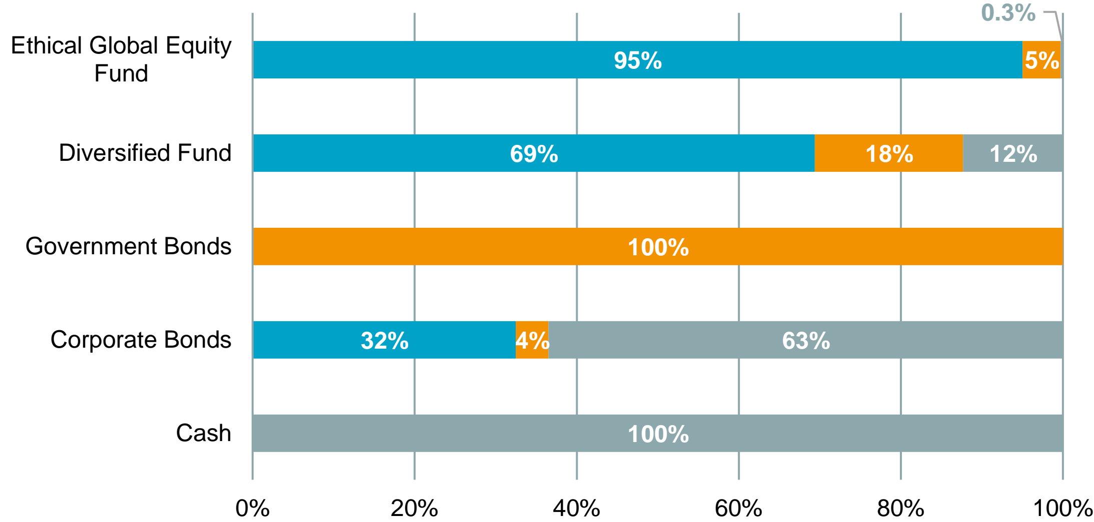


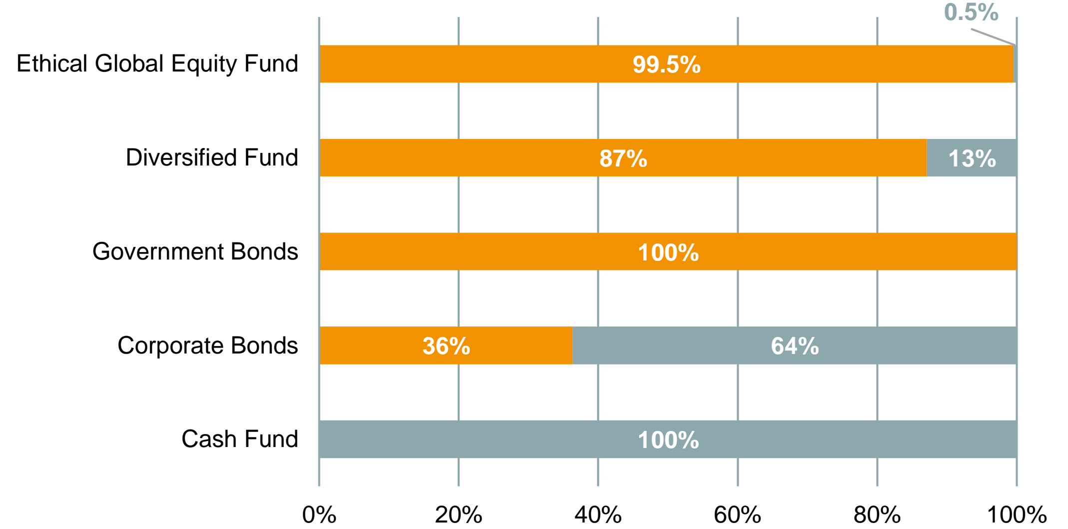
Source: Investment managers, MSCI, LCP. *Based on £1m invested in proportion to the Scheme's assets for which data is available.

Certain data ©2022 MSCI ESG Research LLC. Reported by permission. See Appendix 3 for more details.

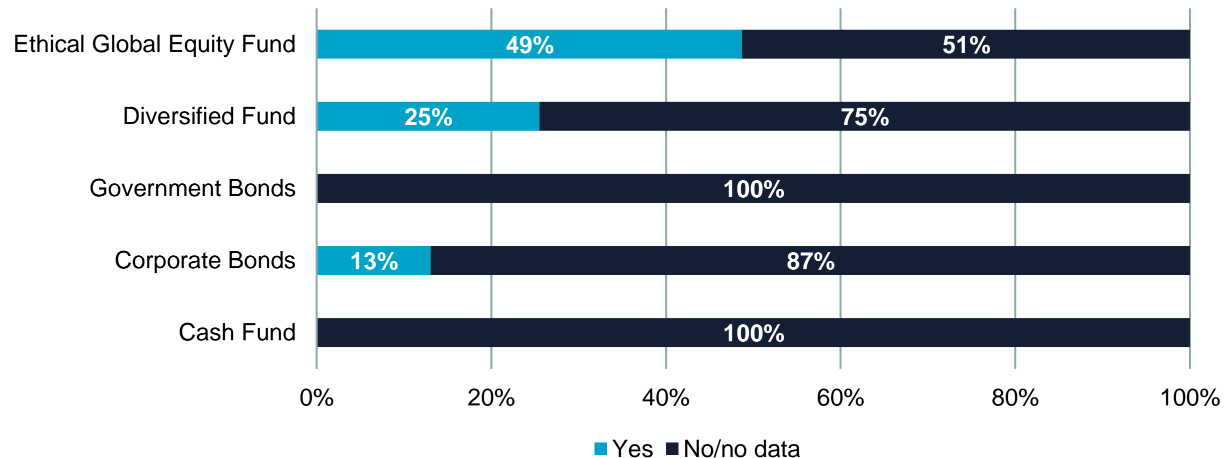
Breakdown of data coverage

This is shown as the split of portfolio value (not the split of the emissions figures).





Reported Estimated Unavailable



Source: Investment managers, MSCI, LCP. Certain data ©2022 MSCI ESG Research LLC. Reported by permission. See Appendix 3 for more details.

Section 4 – Metrics and Targets

Metrics

The Trustee has set the following target:

Target	Coverage	Reference base year
80% of listed equity and corporate bond investments to have set SBTi targets by 2030	Listed equities and corporate bonds within the default investment strategy (c89% of total DC assets).	2021

Initial performance against the target

The climate reporting carried out for the Scheme during the year included an assessment of the current alignment with the above target. Broadly 39% of the Scheme's listed equity and corporate bond investments within the default investment strategy have set SBTi targets by 2022, based on information held on the MSCI database. This is an increase from the 35% SBTi alignment from last year, showing companies are taking actions in setting SBTi targets, however further action is needed in order to meet the Scheme's 80% target by 2030. For the portion of the portfolio for which SBTi alignment data is not available, this analysis assumes that no other portfolio companies have set SBTi targets. The figures presented in this section are therefore a cautious assessment of the current position. The SBTi alignment may be higher in practice.

The proportion of each fund with set SBTi targets was compared with the corresponding figure for a relevant market index with similar characteristics. Overall, the current proportion is considered to be broadly in line with the wider market. The analysis enabled the Trustee to identify the most appropriate funds and managers to focus their engagement on, which would result in the most significant improvement in the Scheme's alignment with its target.

The following steps are being taken to achieve the target:

The Trustee, with help from its investment adviser, has communicated the target to each investment manager.

Investment managers are routinely invited to present at Trustee meetings as part of the existing monitoring process. When meeting with any of the Scheme's investment managers, the Trustee will ask the manager how they expect the proportion of portfolio companies with SBTi targets to change over time and encourage the manager to engage with portfolio companies about setting SBTi targets, prioritising those with the highest carbon footprint.

The investment adviser encourages managers to support the goal of net zero emissions by 2050 or earlier and has published its expectations for investment managers in relation to net zero. This includes the use of effective voting (where applicable) and engagement with portfolio companies to encourage achievement of net zero. The investment adviser continues to engage with managers on this topic and will encourage them to use their influence with portfolio companies to increase the use of SBTi targets.

The Trustee will review progress towards the target each year and consider whether additional steps are needed to increase their chance of meeting the target.

Appendix

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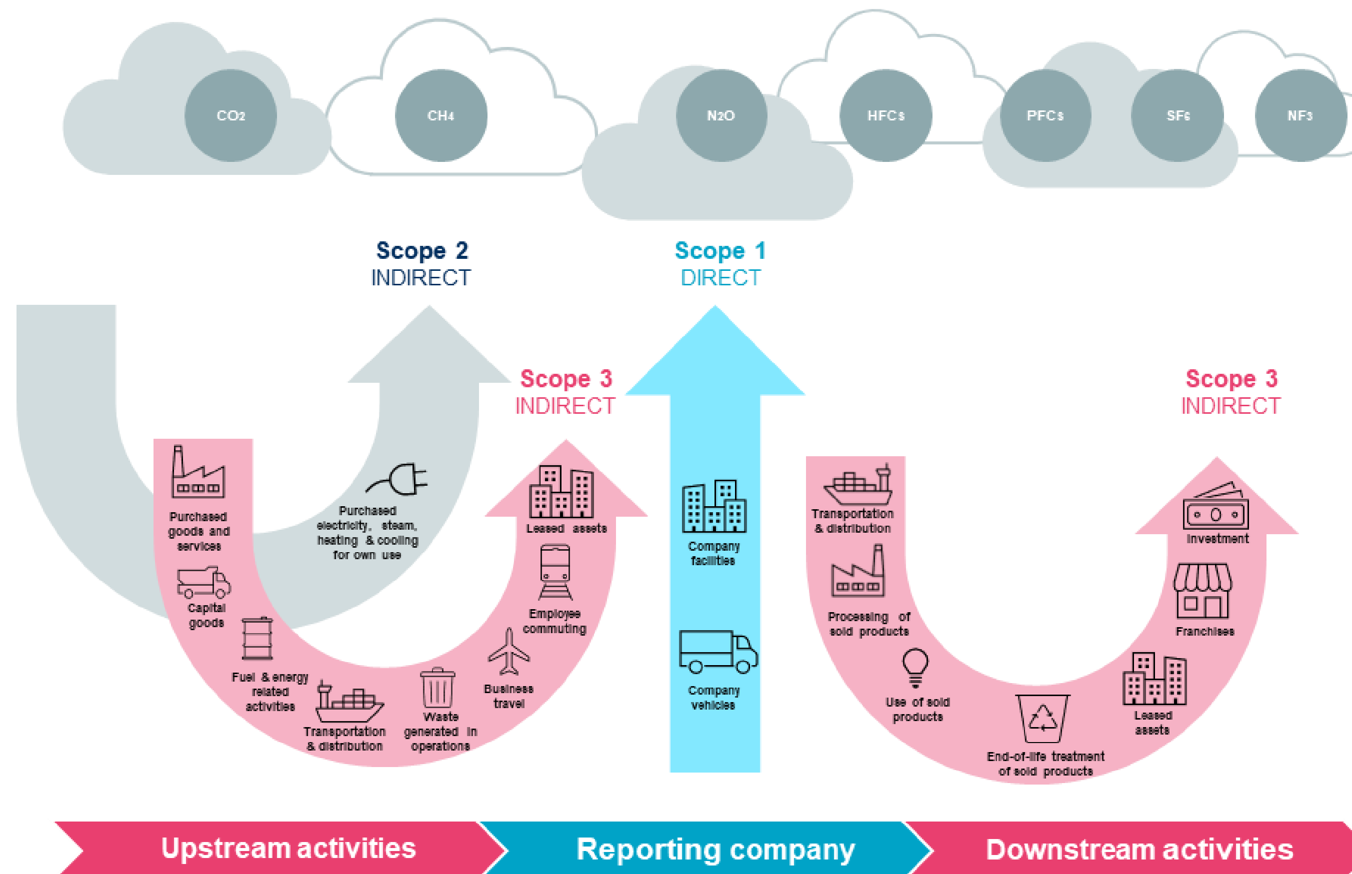
Appendix 1 – Greenhouse gas emissions

Within the 'metrics and targets' section of the report, the emissions metrics relate to seven greenhouse gases – carbon dioxide (CO2), methane (CH4), nitrous oxide (N2O), hydrofluorocarbons (HFCs), perfluorocarbons (PFCs), sulphur hexafluoride (SF6) and nitrogen trifluoride (NF3). The figures are shown as "CO2 equivalent" (CO2e) which is the amount of carbon dioxide that would be equivalent to the excess energy being stored by, and heating, the earth due to the presence in the atmosphere of these seven greenhouse gases.

The metrics related to greenhouse gas emissions are split into the following three categories: Scope 1, 2 and 3. These categories describe how directly the emissions are related to an entity's operations, with Scope 1 emissions being most directly related to an entity's everyday activities and Scope 3 referring to indirect emissions in an entity's value chain. Scope 3 emissions often form the largest share of an entity's total emissions, but are also the ones that the entity has least control over.

- Scope 1 greenhouse gas emissions are all direct emissions from the activities of an entity or activities under its control.
- Scope 2 greenhouse gas emissions are indirect emissions from electricity purchased and used by an entity which are created during the production of energy which the entity uses.
- Scope 3 greenhouse gas emissions are all indirect emissions from activities of the entity, other than scope 2 emissions, which occur from sources that the entity does not directly control.



Source: GHG Protocol

Appendix 2 – Climate scenario analysis

Scenarios considered and why the Trustee chose them

The Trustee carried out climate scenario analysis during the previous Scheme year, with the support of their investment adviser, LCP. The analysis looked at three possible scenarios:

Transition	Description	Why the Trustee chose it
Failed Transition	Paris Agreement goals not met; only existing climate policies are implemented	Physical risks (such as extreme weather events) have a significant negative impact on the global market value of goods and products. Investors are expected to price in further impacts from physical risks, which will affect asset prices, including for our Scheme's investments.
Paris Orderly	Paris Agreement goals met; rapid and effective climate action, with smooth market reaction	To consider the expected impact on the Scheme assets of a material shift towards low carbon by 2030. The transition to a low carbon economy has limited positive effects on the global market value of goods and products and is more than offset by negative physical impacts.
Paris Disorderly	Same policy, climate and emissions outcomes as the Paris Orderly Transition, but financial markets are initially slow to react and then over-react	The key difference to the Paris Orderly scenario is that financial markets react slower to the significant changes in government policy and corporate and consumer behaviour. There is an abrupt market reaction causing a worse outcome than the Paris Orderly scenario.

The Trustee acknowledges that many alternative plausible scenarios exist but found these were a helpful set of scenarios to explore how climate change might affect the Scheme in future.

The scenarios' key features are summarised on the next page.

These scenarios show that equity markets could be significantly impacted by climate change with lesser but still noticeable impacts in bond markets. All three scenarios envisage, on average, lower investment returns and these result in lower retirement outcomes for members.

Appendix 2 – Climate scenario analysis

The climate scenarios considered by the Trustee (as at 31 December 2020)

Scenarios:	Failed Transition	Paris Orderly Transition	Paris Disorderly Transition
Low carbon policies	Continuation of current low carbon policies and technology trends.	Ambitious low carbon policies, high investment in low-carbon technologies and substitution away from fossil fuels to cleaner energy sources and biofuel.	
Paris Agreement outcome	Paris Agreement goals not met.	Paris Agreement goals met.	
Global warming	Average global warming is about 2°C by 2050 and 4°C by 2100, compared to pre-industrial levels.	Average global warming stabilises at around 1.5°C above pre-industrial levels.	
Physical impacts	Severe physical impacts.	Moderate physical impacts.	
Impact on GDP	Global GDP is significantly lower than the climate-uninformed scenario in 2100. For example, UK GDP in 2100 predicted to be 55% lower than in the climate uninformed scenario.	Global GDP is lower than the climate-uninformed scenario in 2100. For example, UK GDP in 2100 predicted to be about 10% lower than in the climate-uninformed scenario.	In the long term, global GDP is slightly worse than in the Paris Orderly scenario due to the impacts of financial markets volatility.
Financial market impacts	Physical risks priced in over the period 2025-2030. A second repricing occurs in the period 2035-2040 as investors factor in the severe physical risks.	Transition and physical risks priced in smoothly over the period of 2021-2025.	Abrupt repricing of assets causes financial market volatility in 2025.

Source: Ortec Finance. Figures quoted are medians.

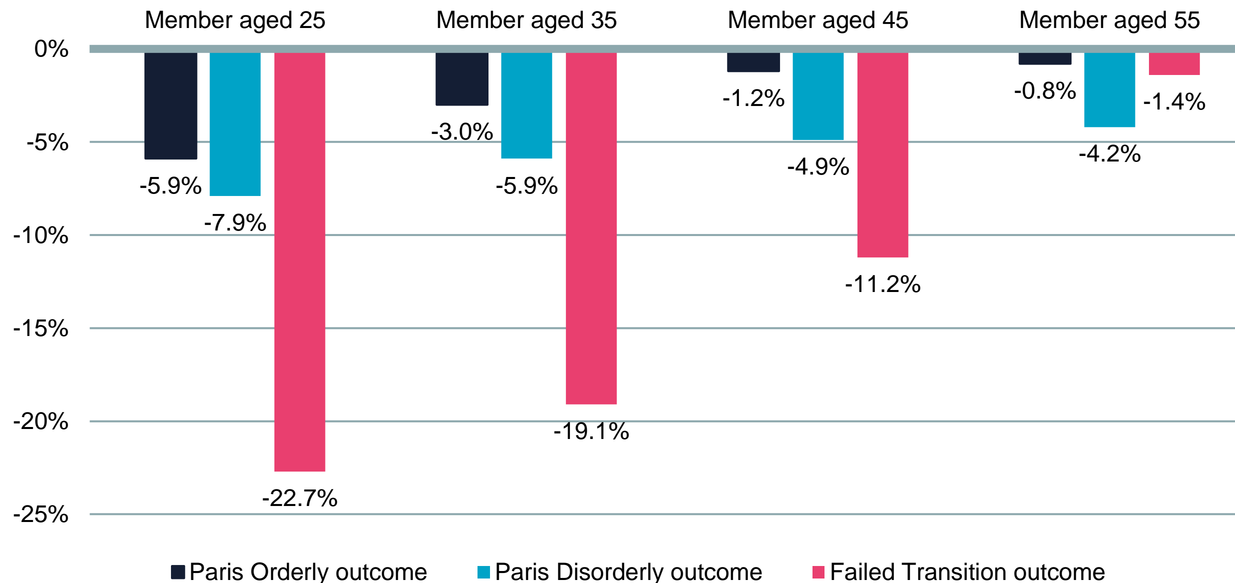
Potential Scheme impacts under each scenario

The scenario analysis looked at the retirement outcomes (in terms of the size of their retirement pot) for individual members of different ages who are invested in the default strategy. The analysis highlighted that members will be subject to climate risks to varying degrees depending on the climate scenario. In general, the default strategy has been designed in a way which reduces investment risk as members approach retirement. Climate risks are generally expected to have the greatest impact on return-seeking assets such as equities. In the default strategy, exposure to these assets is reduced as members approach retirement, which should help to reduce their exposure to climate risks.

- The Paris Orderly scenario leads to the best outcome for members as in this scenario the climate risks are relatively low.
- The Paris Disorderly scenario includes a market shock in the short term which impacts return-seeking assets the most. This has a muted impact on most members' retirement pots as they have time to recover through future investment returns and contributions. Members within 10 years of retirement hold a low and decreasing amount of return-seeking assets so they are impacted less than younger members under this scenario.
- The Failed Transition scenario has limited short term effects but larger long term effects as it assumes increasingly severe physical impacts of climate change emerge over time. This scenario particularly impacts younger members who remain invested in the Scheme for longer.

The analysis confirmed the importance of managing climate-related risks to members' pots. The Trustee does this by: ensuring the Scheme's investment managers have strong climate practices (see pages 6-7); reducing members' exposure to return-seeking assets as they approach retirement (see chart on page 15); and using stewardship to encourage the companies the Scheme invests in to improve their climate practices (see page 13-14).

Chart showing the impact on member pots at retirement with different scenarios and starting ages



Appendix 2 – Climate scenario analysis

Modelling approach – more details

- The scenario analysis is based on the ClimateMAPS model developed by Ortec Finance and Cambridge Econometrics, and was then applied to the Scheme's assets by LCP. The three climate scenarios were projected year by year, over the next 40 years.
- The three climate scenarios chosen are intended to be plausible, not "worst case". Only three scenarios out of countless others which have been considered. Other scenarios could give better or worse outcomes for the Scheme.
- The results discussed in this report have been based on macro-economic data at 31 December 2020, calibrated to market conditions at 31 March 2021.
- ClimateMAPS uses Cambridge Econometrics' macroeconomic model which integrates a range of social and environmental processes, including carbon emissions and the energy transition. It is one of the most comprehensive models of the global economy and is widely used for policy assessment, forecasting and research purposes. The outputs from this macroeconomic modelling – primarily the impacts on country/regional GDP – are then translated into impacts on financial markets by Ortec Finance using assumed relationships between the macroeconomic and financial parameters.
- Ortec Finance runs the projections many times using stochastic modelling to illustrate the wide range of climate impacts that may be possible, under each scenario's climate pathway. LCP takes the median (ie the middle outcome) of this range of impacts, for each relevant financial parameter, and adjusts it to improve its alignment with LCP's standard financial assumptions.
- Members' starting pots values were assumed to equal the average value for Scheme members of their age, and member and employer contributions were assumed to be paid in line with the current contribution structure. No allowance was made for changes to the investment strategy or contributions in response to the climate impacts modelled.
- As this is a "top-down" approach, investment market impacts were modelled as the average projected impacts for each asset class, ie assuming that the Scheme's investments are affected by climate risk in line with the market-average portfolio for the asset class. This contrasts with a "bottom up" approach that would model the impact on each individual investment held in the Scheme's investment portfolio. As such, it does not require extensive scheme-specific data and so the Trustee was able to consider the potential impacts of the three climate scenarios for all of the Scheme's assets.
- In practice, the Scheme's investment portfolio may not experience climate impacts in line with the market average. The Trustee considers, on an ongoing basis, how the Scheme's climate risk exposure differs from the market average using climate metrics (which are compared with an appropriate market benchmark) and its annual responsible investment review which considers the investment managers' climate approaches (see page 15).
- The Trustee notes that the three climate scenarios chosen are intended to be plausible, not "worst case", and the modelling is based on median outcomes. It therefore illustrates how the centre of the "funnel of doubt" surrounding asset projections might be affected by climate change. It does not consider tail risks within that funnel, nor does it consider how the funnel might be widened by the additional uncertainties arising from climate change. In addition, only three scenarios out of infinitely many have been considered. Other scenarios could give better or worse outcomes for the Scheme.
- Uncertainty in climate modelling is inevitable. In this case, key areas of uncertainty relating to the financial impacts include how climate change might affect interest rates and inflation, and the timing of market responses to climate change. ClimateMAPS, like most modelling of this type, does not allow for all climate-related impacts and therefore, in aggregate, is quite likely to underestimate the potential impacts of climate-related risks, especially for the Failed Transition scenario. For example, tipping points (which could cause runaway physical climate impacts) are not modelled and no allowance is made for knock-on effects, such as climate-related migration and conflicts.

Appendix 3 – MSCI data

Notes for data sourced from MSCI (shown on pages 19-22)

Emissions are attributed to investors using “enterprise value including cash” (ie EVIC, the value of equity plus outstanding debt plus cash).

The total GHG emissions figures omit any companies for which data was not available. For example, if the portfolio was worth £200m and emissions data was available for 70% of the portfolio by value, the total GHG emissions figure shown relates to £140m of assets and the portfolio’s carbon footprint equals total GHG emissions divided by 140. In other words, no assumption is made about the emissions for companies without data.

The emissions targets metric refers to the % of portfolio by weight of companies that have a near-term carbon emissions reduction target that has been approved by the Science Based Targets initiative (SBTi). Science-based targets provide a clearly defined pathway for companies to reduce greenhouse gas emissions which is in line with what the latest climate science deems necessary to meet the goals of the Paris Agreement – limiting global warming to well below 2°C above pre-industrial levels and pursuing efforts to limit warming to 1.5°C. The MSCI database does not distinguish between companies which do not have an SBTi target and companies for which MSCI does not check the SBTi status, so the coverage for this metric is equal to the % of the portfolio with an SBTI target.

Emissions data coverage and quality

Where coverage of the portfolio analysed is less than 100%, this is because the MSCI database:

- Does not cover some holdings (eg cash, sovereign bonds, bonds that have recently matured, shares in companies no longer listed when the analysis was undertaken);
- Does not hold emissions data for some portfolio companies because the company does not report it and MSCI does not estimate it; and/or
- Does not hold EVIC data for some portfolio companies, so emissions cannot be attributed between equity and debt investors.

The last of these reasons is usually the main explanation for the fairly low coverage of bond portfolios.

Where emissions data is estimated, MSCI uses one of three methods.

- For electric utilities, MSCI’s estimate of Scope 1 emissions is of direct emissions due to power generation, calculated using power generation fuel-mix data.
- For companies not involved in power generation, which have previously reported emissions data, MSCI starts with a company-specific carbon intensity model.
- For other companies, MSCI uses an industry segment-specific carbon intensity model, which is based on the estimated carbon intensities for 1,000+ industry segments.

For Scope 3 emissions, we have chosen to use MSCI’s estimated emissions even where reported emissions are available. This provides greater consistency than using a mixture of reported and estimated emissions. Analysis of reported Scope 3 emissions suggests that the data quality is currently low: data is volatile and often out of date, with relatively few companies reporting on all types of Scope 3 emissions. In contrast, MSCI estimates all types of Scope 3 emissions for most companies in its database, for a recent reporting year and using a consistent approach.

MSCI is a leading provider of climate-related data, so we would expect the coverage to compare favourably with other data sources. Our investment adviser is engaging with MSCI to encourage them to improve EVIC coverage for debt issuers and to distinguish between companies which do not have an SBTi target and companies for which it does not check the SBTi status.

Appendix 3 – MSCI data

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Appendix 4 – Glossary

Alignment – in a climate change context, alignment is the process of bringing greenhouse gas emissions in line with 1.5°C temperature rise targets. It can be applied to individual companies, investment portfolios and the global economy.

Asset class – a group of securities which exhibit broadly similar characteristics. Examples include equities and bonds.

Bond – a bond is a security issued to investors by companies, governments and other organisations. In exchange for an upfront payment, an investor normally expects to receive a series of regular interest payments plus, at maturity, a final lump sum payment, typically equal to the amount invested originally, or this amount increased by reference to some index.

Carbon emissions - These refer to the release of carbon dioxide, or greenhouse gases more generally, into the atmosphere, for example from the burning of fossil fuels for power or transport purposes.

Carbon footprint – In an investment context, the total carbon dioxide or greenhouse gas emissions generated per amount invested (eg in £m) by an investment fund. Related definitions are used to apply the term to organisations, countries and individuals.

Climate change adaptation – steps taken to adapt to the physical effects of climate change such as improving flood defences and installing air conditioning.

Climate change mitigation – steps taken to limit climate change by reducing greenhouse gas emissions, for example by shifting to renewable sources of energy – such as solar and wind – and by using less energy and using it more efficiently.

Credit – long-term debt issued by a company, also known as corporate bonds. Corporate bonds carry different levels of credit risk which is indicated by their rating and credit spread.

Defined Contribution (DC) – a pension scheme in which the sponsor stipulates how much it will contribute to the arrangement which will depend upon the level of contributions the member is prepared to make. The resultant pension for each member is a function of the investment returns achieved (net of expenses) on the contributions and the terms for purchasing a pension at retirement. In contrast to a defined benefit scheme, the individual member bears the risk that the investments held are insufficient to meet the desired benefits.

Debt – money borrowed by a company or government which normally must be repaid at some specified point in the future.

Default strategy – the fund or mix of funds in which contributions in respect of a DC member will be invested in the absence of any explicit fund choice(s) of that member.

Environmental, social and governance (ESG) – an umbrella term that encompasses a wide range of factors that may have been overlooked in traditional investment approaches. Environmental considerations might include physical resource management, pollution prevention and greenhouse gas emissions. Social factors are likely to include workplace diversity, health and safety, and the company's impact on its local community. Governance-related matters include executive compensation, board accountability and shareholder rights.

Equity – through purchase on either the primary market or the secondary market, company equity gives the purchaser part-ownership in that company and hence a share of its profits, typically received through the payment of dividends. Equity also entitles the holder to vote at shareholder meetings. Note that equity holders are entitled to dividends only after other obligations, such as interest payments to debt holders, are first paid. Unlike debt, equity is not normally contractually repayable.

Ethical investment – an approach that selects investments on the basis of an agreed set of environmental, social and governance (ESG) criteria that are motivated by ethical considerations. These can be positive – eg choosing companies involved in water conservation or negative – eg not choosing companies involved in the arms trade.

Fossil fuels – fuels made from decomposing plants and animals, which are found in the Earth's crust. They contain carbon and hydrogen, which can be burned for energy. Coal, oil, and natural gas are examples of fossil fuels.

Gilts – bonds issued by the UK government. They are called gilts as the bond certificates originally had a gilt edge to indicate their high quality and thus very low probability of default.

Greenhouse gas (GHG) emissions (scopes 1, 2 and 3) – gases that have been and continue to be released into the Earth's atmosphere. Greenhouse gases trap radiation from the sun which subsequently heats the planet's surface (giving rise to the "greenhouse effect"). Carbon dioxide and methane are two of the most important greenhouse gases. See also Appendix 1.

Investment mandate – see pooled mandate and segregated mandate

Net zero – this describes the situation in which total greenhouse gas emissions released into the atmosphere are equal to those removed. This can be considered at different levels, eg company, investor, country or global.

Offsetting – the process of paying someone else to avoid emitting, or to remove from the atmosphere, a specified quantity of greenhouse gases, for example through planting trees or installing wind turbines. It is sometimes used to meet net zero and other emission reduction targets.

Appendix 4 – Glossary

Paris Agreement – the Paris Agreement is an international treaty on climate change, adopted in 2015. It covers climate change mitigation, adaptation and finance. Its primary goal is to limit global warming to well below 2°C, preferably to 1.5°C, compared to pre-industrial levels.

Physical risk – these are climate-related risks that arise from changes in the climate itself. They include risks from more extreme storms and flooding, as well as rising temperatures and changing rainfall pattens.

Pooled mandate – a feature of a collective investment vehicle whereby an investor's money is aggregated (ie "pooled") with that of other investors to purchase assets. Investors are allotted a share of those assets in proportion to their contribution. Ownership is represented by the number of "units" allocated – eg if the asset pool is worth £1m and there are 1m units then each unit is worth £1. Pooled funds offer smaller investors an easy way to gain exposure to a wide range of investments, both within markets (eg by buying units in a UK equity fund) as well as across markets (eg by buying units in both a UK equity fund and a UK corporate bond fund).

Responsible Investment (RI) – the process by which environmental, social and governance (ESG) issues are incorporated into the investment analysis and decision-making process, and into the oversight of investments companies through stewardship activities. It is motivated by financial considerations aiming to improve risk-adjusted returns.

Science-based targets – targets to reduce greenhouse gas emissions that are in line with what the latest climate science deems necessary to meet the goals of the Paris Agreement.

Science-Based Targets initiative (SBTi) – an organisation that sets standards and provides accreditation for science-based targets set by companies and investors.

Scenario analysis – a tool for examining and evaluating different ways in which the future may unfold.

Scope 1, 2 and 3 – a classification of greenhouse gas emissions. See Appendix 1.

Segregated mandate – a segregated investment approach ensures that an investor's investments are held separately from those of other investors. This approach offers great flexibility – for example, the investor can stipulate the precise investment objective to be followed and can dictate which securities can or cannot be held.

Self-select – in contrast with a default fund, a self-select fund within a DC scheme is one of a range of funds that members can choose to invest in.

Stakeholder – an individual or group that has an interest in any decision or activity of an organisation. The stakeholders of a company include its employees, customers, suppliers and shareholders.

Statutory obligations – statutory obligations are those obligations that do not arise out of a contract, but are imposed by law.

Stewardship – stewardship is the responsible allocation, management and oversight of capital to create long-term value for clients and beneficiaries leading to sustainable benefits for the economy, the environment and society. It is often implemented via engagement with investee companies and exercising voting rights.

Taskforce on Climate-related Financial Disclosures (TCFD) – a group of senior preparers and users of financial disclosures from G20 countries, established by the international Financial Stability Board in 2015. The TCFD has developed a set of recommendations for climate-related financial risk disclosures for use by companies, financial institutions and other organisations to inform investors and other parties about the climate-related risks they face.

Transition risk – these are climate-related risks that arise from the transition to a low-carbon economy and can include changes in regulation, technology and consumer demand.