LOTHIAN PENSION FUND
September 2020

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Highlights

- Lothian Pension Fund (LPF) is the Local Government Pension Scheme (LGPS) for Edinburgh and the Lothians and is Scotland's second largest LGPS with over £7.6bn in assets, 81,500 members and 80 employers.
- 85% of assets are managed in-house giving the Fund a unique ability to source data and ensure its values are articulated throughout the investment process and monitor impact.
- LPF has been a UNPRI signatory since 2008 and was scoring highly according to the PRI framework but in 2015 they realised they could be doing more.
- Since 2017, LPF has overhauled their responsible investment approach and now use ESG metrics on all fundamental equity funds.
- LPF have focused on climate change and carbon mapping in their newly launched Statement of Responsible Investment Principles and disclose carbon information in line with the Taskforce for Climate-related Financial Disclosure.
- LPF have made specific commitments to: measure the carbon intensity of 100% of their assets, including forestry, by 2022; cease any primary investment in companies that aren't aligned with the goals of the Paris agreement (via equities or bonds) and engage with those that don't up until 2025 (thereafter likely divesting).

Quotes

"If I'm giving 15 year money to a non-Paris aligned company now, I'm not convinced that's payable by 2035 given the way things are going....We don't want to say to our members we're providing new capital to these companies. That's a values-based decision but mostly a financial decision"

David Hickey, European Equity Manager, Lothian Pension Fund.

Introduction

From 2015 LPF, following a review of their UNPRI reporting and a number of questions from members and committee members around climate change and carbon emissions, decided to review how they were investing. Their first step was to review the data they held on their investments – made easier by the fact that 85% of LPF's assets are managed in house – and then embed ESG robustly within their investment process. This was achieved by including ESG metrics when making investment decisions and using EOS Federated to engage across the entire portfolio once invested. However, their review continued to evolve and they signed up to the TCFD, providing more information and data on the carbon footprint of the portfolio, as well as launching a new Statement of Responsible Investment Principles with clear climate action commitments.

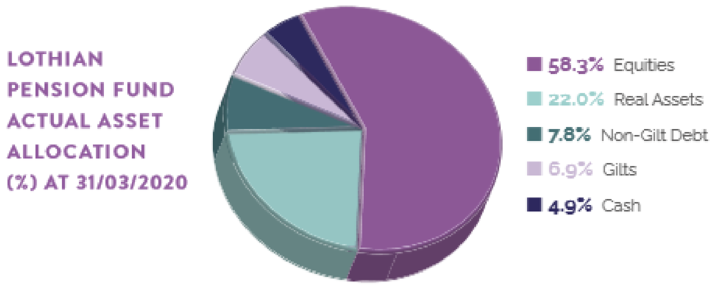
Climate Action Commitments

LPF's new Statement of Responsible Investment Principles is structured in line with the UNPRI principles and provides very specific goals around climate change. The targets and metrics include:

- To measure the carbon intensity of 100% of LPF's assets by 2022;
- To cease any primary investment in companies that aren't aligned with the goals of the Paris agreement – this includes the funding of any new equity or bond issuance;
- To continue engaging with non-Paris aligned companies until 2025, with any companies making little progress towards the goals likely being divested at this point.

Actions to date

Mapping 100% of Portfolio – equities mapped, more to do on other asset classes



Source: Lothian Pension Fund, Annual Report and Accounts 2019/2020

Since 2018, LPF have been measuring the carbon intensity of their equity portfolio and reporting in line with TCFD best practice. They use MSCI, Transition Pathway Initiative and Climate Action 100+ data which is continually developing and evolving. It is important to note that the data are purely used as outputs to inform the investment process rather than setting inputs which could easily be framed to ensure a certain outcome. LPF are not committing to specific carbon intensity targets for the overall portfolio and will use engagement to encourage change among the companies it holds. The following table is taken from LPF's annual report and accounts 2019/2020:

	2018 Weighted Average Carbon Intensity (tons CO2/$M sales)	2019 Weighted Average Carbon Intensity (tons CO2/$M sales)	Year on year change	2020 Weighted Average Carbon Intensity (tons CO2/$M sales)	Year on year change
LPF All Equities	328.6	325.2	-1.0%	294.9	-9.3%
MSCI ACWI	218.9	200.2	-8.5%	178.1	-11.1%

Source: MSCI

These numbers are presented on the basis of Scope 1 and 2 carbon emissions.

There is work currently being undertaken to map the real estate and infrastructure portfolios using GRESB data which LPF hope to publish in the near future and before 2022 when they are targeting the full mapping of the portfolio. At 31 March 2020, 89% of the Infrastructure portfolio value was invested in assets/funds which were also signatories of the PRI and 32% of funds participated in the 2019 GRESB Infrastructure Assessment.

Ceasing Primary Investment in Companies not Aligned with Paris Goals

In 2020, LPF announced plans to cease all primary investment in internal investments in equities and bonds where companies are not aligned with the Paris agreement. Where there are external funds, managers are encouraged to sign up to the PRI and LPF have an ambition that they will only appoint managers who commit to not providing new capital to non-Paris aligned companies.

Engaging with non-Paris Aligned Companies
LPF are clear that engagement with companies is always preferable to divestment which just shifts ownership to another asset owner who may not have the same values and goals. They participate in 100% of company resolutions and use their partners EOS at Federated Hermes and Climate Action 100+ to identify and engage with companies to encourage moves towards alignment with the Paris agreement.

In 2019, LPF co-filed a resolution for BP's May 2019 AGM calling for greater transparency and disclosure on the company's approach to carbon emission and low-carbon transition planning. The resolution was successfully backed, and BP have since committed to provide investors with a new strategy consistent with the goals of the Paris agreement.

LPF have also been engaged with Fortum, a Finnish utility company, which holds and is acquiring some carbon intensive businesses, including Uniper. The company is in open dialogue and Uniper has recently announced a commitment to net zero by 2035. Please see the full description of engagement below.

Next steps

LPF will be working hard to reach their targets over the coming years. The focus will continue to be on company engagement and disclosure, with reporting on the Stewardship Code 2020 being the focus from April next year. LPF are also working alongside a group of forestry asset owners, including the Church Commissioners, to set up a list of common carbon data requirements they will need from forestry managers in order to align with TCFD requirements. This will allow the asset owners to set the agenda and deliver the information they need in a coherent and efficient way for them to be able to publicly disclose.

"The mantra we'll follow from now on is very clearly 'Engage our Equities, Deny our Debt'. Lothian Pension Fund will no longer supply new funding to non-Paris aligned companies either through new bond issuance or through new equity issuance." David Hickey

About Pensions for Purpose

Pensions for Purpose is an online collaborative initiative to raise awareness of impact investment among pension funds. Our members consist of Influencers (eg. impact managers, trade bodies and consultants) who want to promote the understanding of, and discussion around, impact investment, and Affiliates (eg. asset owners, government bodies, independent advisers and journalists) who want to deepen their knowledge of this important topic. Affiliates are able to register for free, which allows them to access additional, Affiliate-only material and to receive monthly updates of new content posted on the platform. For more information see https://www.pensionsforpurpose.com/.