LOCAL PENSIONS PARTNERSHIP INVESTMENTS LTD

Responsible Investment Policy
Annex on Climate Change

1. Introduction

This annex to our Responsible Investment Policy explains our climate change beliefs and describes our approach to understanding and managing the risks and opportunities climate change presents for the portfolios we manage on behalf of clients.

2. Our Climate Change Beliefs

Climate change poses a long-term and material financial risk to client portfolios. It has the potential to impact value across all the asset classes we invest in globally, but the route scale and timing of this impact is both complex and uncertain.

Climate change is a systemic risk which arises from the physical effects of sustained changes in weather patterns due to global warming and from human interventions to mitigate and manage these changes by adapting to new circumstances through regulation, technological innovation, or other cultural shifts.

Climate change will impact companies globally. It has the potential to destroy value where business risks are not being recognised and integrated into effective strategic planning but also presents opportunities for value creation where products and services can be developed which solve problems and meet societal needs.

The scope, dimensions, materiality and long-term significance of climate change as an investment issue merit specific attention as part of our Responsible Investment approach and the processes we develop to implement this in practice.

3. Our Climate Change Beliefs Translated into Practice

Our ultimate objective is to be able to identify, quantify, measure, act, monitor and report to clients on our management of climate change risk on their behalf. This is a significant undertaking with numerous challenges and we recognise that we are at an early stage of an ongoing task to evolve our capabilities, access insightful data, set appropriate measures and monitor and report on our progress.

The steps we are already taking and areas we have identified for further development are briefly set out below.

Investment Selection & Portfolio Monitoring

Our approach to asset selection (for internally managed assets) and to manager selection and monitoring (for assets managed by external managers) is built around detailed risk analysis and an up-to-date understanding of context as part of due diligence. This approach suits the complexity and multi-dimensional nature of climate change and the challenge it poses for strategy integration.

Our starting point is to ensure managers share our beliefs and have the capabilities to meet our requirements. In appointing third party managers we routinely assess their approach to responsible investment and the integration of environmental, social and corporate governance factors. Our Responsible Investment Due Diligence Questionnaire includes specific questions on assessing, monitoring and reporting on climate change and questionnaire responses inform our detailed selection and appointment process.

Identifying the risks client portfolios face from climate change requires quantitative measurement. Measurement and monitoring require information. We are continually seeking data and tools to help us to assess the position of individual companies and support our evaluation of the aggregate position at headline level. Our focus to date has been on listed equities where information is most readily available, but our learning will inform the more challenging task of translating this analysis to wider asset classes.

We recognise that whilst all companies may ultimately be impacted by climate change, some sectors face greater risks due to their emissions intensity or involvement in traditional energy production based on fossil fuels which will need to be significantly curtailed to meet global emissions reduction targets. We are utilising data on greenhouse gas emissions to understand the position of sectors and companies and are exploring the alignment of our Global Equities Fund with a 2°c pathway in order to reference our position relative to the goals of the Paris Agreement.

We are using data from CDP and the Transition Pathway Initiative (TPI) toolkit to ensure our review of the position of our listed equities investments is referenced against external measures of corporate progress in the planning and management of climate-related business risks.

We are closely monitoring the companies in our portfolio engaged in the extraction of fossil fuels as part of evaluating the balance of risk to return for these assets and the likelihood of material asset stranding. Our assessment of companies informs an ongoing dialogue with managers around their own evaluation of the climate change risks their portfolios encompass.

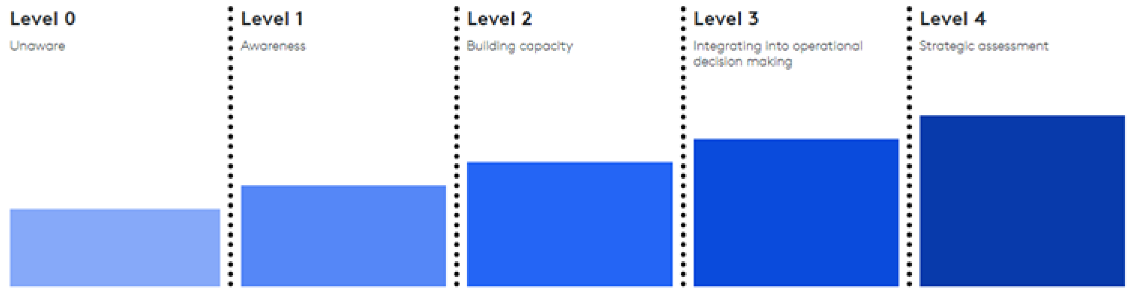
Our work has identified thermal coal extraction as a particular focus of risk. Coal is the most carbon intensive fossil fuel and the traditional energy source most likely to face declining demand in the face of rising renewable output at a reducing cost. As a consequence of this and an exception to our normal approach we have taken the decision to cease investing in thermal coal extraction through our Global Equities Fund by divesting existing holdings and placing an exclusion on further investment in this sector. This step reflects a commitment to protecting the long term financial interests of all clients invested in our Global Equities Fund. We acknowledge and are pragmatically managing the methodological challenges associated with thermal coal exclusion across other asset classes.

We have set qualitative targets around our investment in fossil fuel extraction. These reference the effectiveness of corporate governance by individual fossil fuel companies based on TPI Management Quality Scores. Setting targets is an exploratory step intended to maintain a clear focus on extractive companies and the investment risks they pose, the likelihood of value loss and the quality of corporate planning for climate related challenges.

Our target for the Global Equities Fund in 2018 is for all extractive fossil fuel companies within TPI coverage to be rated at TPI 2 or above. For 2019, the target is for companies to achieve a score of TPI 3 or above.

Transition Pathway Initiative (TPI) – Management Quality Stairway

Companies are assessed to one of 5 levels based on their position in relation to the recognition and management of transition risks. Standard questions are posed and are answered using publicly available data.



Targets apply on a comply or explain basis and Managers are required to provide a detailed justification for any alternative opinion on the preparedness of investee companies for the transition to a low carbon economy. Our focus in setting targets is to ensure we invest in companies which are addressing and assisting the transition to a lower carbon future and moving out of those which are not managing risk effectively on behalf of shareholders. This is facilitated by scrutiny and challenge based on a consistent measure. The TPI toolkit is publicly available, accessible to all managers without the need to subscribe to a proprietary data system and refreshed annually.

The efficacy of setting and monitoring to qualitative targets will be kept under review and considered in light of the availability of alternative measures and approaches for ensuring a consistent approach to corporate evaluation as part of manager monitoring.

Active Ownership (Voting and Engagement)

Our commitment to encouraging good corporate governance through our ownership activities includes a specific focus on climate related issues for investee companies.

Our shareholder voting approach explicitly identifies all upcoming resolutions on environmental themes. In appropriate circumstances we will support resolutions which encourage companies to recognise, evaluate, adapt to and report on climate related business risks and opportunities, or which urge them to evolve their current approach where further development is warranted. This is in line with our Shareholder Voting Policy which recognises the responsibility of asset owners to monitor and engage with investee companies in order to protect value.

As part of our engagement approach, LPPI is networked with a range of organisations working on climate related agendas. These include the Principles of Responsible Investment, the Institutional Investor Group on Climate Change, the Transition Pathway Initiative and Climate Action 100+. Our interactions with these groups inform our thinking and provide opportunities to support collective initiatives which encourage companies to address climate change related business risks and report transparently on their efforts.

We support the recommendations of the FSB's Taskforce on Climate Related Financial Disclosure which identified that inadequate corporate reporting creates significant information gaps which prevent investors from evaluating the quality of climate change governance by investee companies. We encourage investee companies to develop their reporting in line with the disclosures outlined by the TCFD.

We also recognise that TCFD recommendations on enhanced reporting extend to investors and Asset Managers and as part of the evolution of our approach to climate change we will be working towards alignment with the TCFD disclosure requirements.

To ensure the continuing effectiveness of our approach to addressing climate change as part of our commitment to Responsible Investment our Stewardship Committee will review this annex to our Responsible Investment Policy on an annual basis and will update it to reflect changes in approach and further progress.

This Annex was last reviewed and updated in August 2018.

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