

This report has been prepared by LPPI for Lancashire County Pension Fund (LCPF) as a professional client.

1. Introduction

This report on Responsible Investment (RI) is a companion to the LPPI RI Dashboard (Appendix 1) and the Quarterly Active Ownership Report (Appendix 2 – available from the online Pensions Library).

It covers stewardship in the period 1st July - 30th September 2021 plus insights on current and emerging issues for client pension funds.

^R This symbol indicates a term explained in the reference section at the end of this report.

Key takeaways for the period:

- In Q3 2021 LPPI voted on 100% of company proposals, supporting 89% of these.
- Investments in brown sectors (extraction, transportation, storage, supply, and generation of energy from fossil fuels) are 2.38% of the portfolio.
- Investments in green sectors (renewable energy generation, clean technology, and decarbonising activities) are 3.08% of the portfolio.
- LPPI has joined the Occupational Pensions Stewardship Council (OPSC), a new industry peer group set up by the Department for Work and Pensions (DWP) to promote and facilitate high standards of stewardship for pensions assets.
- The Responsible Investment Team, in cooperation with the Equities team, has developed Shareholder Voting Guidelines for the LPPI Global Equities Fund (GEF).
- LPPI has submitted its Annual Report on Stewardship and Responsible Investment (2020/21) to the Financial Reporting Council (FRC).

2. RI Dashboard – portfolio characteristics

This section of the report shares key takeaways from the RI Dashboard at Appendix 1.

Asset class metrics (*Dashboard pages 1 & 2*) offer insights on the composition of the portfolio and its general characteristics. See the summary for Q3 2021 outlined below.

Listed equities (Dashboard p1)

Sector Breakdown

Categorised by GICS^R the largest sectoral exposures for the GEF are Information Technology (26%), Consumer Staples (15%), and Financials (12%).

Comparing the GEF with its benchmark (MSCI ACWI)^R gives insight into how sector exposures for the fund differ from a global market index. The length of each horizontal bar

indicates by how much exposures differ in total (+ or –) compared with the benchmark, which is the outcome of active managers making stock selection decisions rather than passively buying an index.

Top 10 Positions

The top 10 companies (10 largest positions) make up 24% of the total LPPI GEF.

In Q3 2021 Microsoft remains the largest holding in the GEF, Nestlé has overtaken Visa to become the second largest holding in the GEF, and Visa remains in the top 3 as the third largest holding. Below the top 3 holdings, Accenture moved above Colgate-Palmolive, becoming the 4th largest holding, with Colgate-Palmolive becoming 5th largest holding. There were also changes to the bottom 2 positions. Nike and Waters Corporation (9th and 10th in Q2) have been replaced by Experian and Costco respectively. Starbucks, Pepsi, and Alphabet's positions remain unchanged (6th, 7th, and 8th respectively) between Q2 and Q3.

Portfolio ESG Score

The GEF's Portfolio ESG score increased from 5.2 to 5.3 between Q2 and Q3. In the same period the equivalent score for the benchmark remained unchanged at 5.1.

Transition Pathway Initiative (TPI)

Monitoring against TPI^R Management Quality ratings confirms the GEF continues its relatively low exposure to highly carbon intensive activities with minimal changes in ratings since Q2. By value, the coverage of the GEF represented within the globally high emitting companies under TPI assessment remains unchanged from Q2, at 12%.

The number of GEF companies in scope of TPI scoring has not changed since Q2 2021, remaining at 24.

Of the 24 companies in TPI scope:

- 90% (by value) are rated TPI 3 and above – demonstrably integrating climate change into their operational planning (TPI3) and into their strategic planning (TPI 4). This is unchanged from Q2 2021.
- 7 companies are scored below TPI 3 and under monitoring.

Other asset classes (Dashboard p2)

Private Equity

Sectoral and geographical exposures remained similar to those reported in Q2 2021. The portfolio continued to have a strong presence in the United States (47%) and the largest sectoral exposure continued to be Information Technology (31%).

The Real-World Outcomes section of the dashboard features examples of socially positive investments and this quarter the focus is on Private Equity. Pages 6-8 share information on a selection of investments within the Lancashire Fund portfolio which are developing solutions for sustainable consumption, production, and development.

Infrastructure

The geographical exposure to UK based infrastructure continued to increase, moving from 43% exposure in Q2 to 47% in Q3. The largest sectoral exposure remained in Traditional Energy, Renewable Energy, Waste, which makes up 37% of the portfolio. Please note, we continue to use updated categorisation from Q2, which reflects amendment made by the Infrastructure Team to align with the ACM limits applied to LPPI Infrastructure.

Real Estate

Sectoral and geographical exposures remained similar to those reported in Q2 2021. The portfolio continued to be largely deployed in the UK, with 74% of assets here. The largest sectoral exposure continued to be in Industrial assets, making up 31% of the portfolio.

Green & Brown Exposures

Calculation of the Fund's exposure to Green and Brown activities focusses specifically on equity assets (listed equity, private equity, and infrastructure) plus corporate bonds within fixed income. Figures give an indication, rather than a precise measure, as an assistance to reviewing the overall position.

Green activities are those directly contributing to real world decarbonisation, principally through renewable energy generation, but include other activities supporting lower emissions including district heating, and waste management. Brown activities are those directly involved with extracting, transporting, storing, and otherwise supplying fossil fuels, or using them to generate energy.

The dashboard presents information on the trend in green and brown exposures (commencing in Q4 2019). Quarterly changes in Green and Brown exposure reflect multiple factors at play including funds reaching maturity, assets being revalued, and investments being made and sold. The total value of the LCPF portfolio (as the denominator) also affects brown and green % shares quarterly.

Compared with Q2 2021, brown exposure has decreased from 2.66% to 2.38%. The change reflects a net reduction in the total value of brown infrastructure assets (including the sale of an asset within one of the Infrastructure funds). Whilst the value of brown assets fell slightly, the biggest influence on the proportion of brown was growth in the value of Lancashire Fund (as the denominator) between Q2 and Q3.

Compared with Q2 2021, green exposure has decreased from 3.22% to 3.08%. This decrease results from changes in the overall value of assets identified as green (predominantly resulting from a small net reduction in infrastructure asset valuations) but in total green assets are a smaller proportion of the total Fund in Q3 due to the increase in the value of the Lancashire Fund (as the denominator) between Q2 and Q3.

Investments in renewable energy generation from wind, solar, hydro, and waste make up 78% of total green exposure, and 97% of green exposure comes from Infrastructure assets.

3. Core Stewardship

This section of the report gives an overview of stewardship activities in the last quarter. Client pension funds delegate day to day implementation of the Partnership's approach to RI to Local Pensions Partnership Investments Ltd (LPPI). Ongoing stewardship activities by LPPI include portfolio and manager monitoring and the exercise of ownership responsibilities via shareholder voting, and engagement.

Shareholder Voting - LPPI Global Equity Fund (GEF) (Dashboard page 3)

Shareholder voting is overseen centrally by LPPI rather than by individual asset managers. LPPI receives analysis and recommendations from an external provider of proxy voting and governance research. We follow Sustainability Voting Guidelines focussed on material ESG considerations and liaise with providers and asset managers as needed to reach final voting decisions.

Full details of all shareholder voting by LPPI are publicly available from the LPP website within quarterly [shareholder voting reports](#).

The period 1st July - 30th September 2021 encompassed 48 meetings and 383 proposals voted. LPPI voted at 100% meetings where GEF shares entitled participation.

a) Company Proposals

LPPI supported 89% of company proposals in the period.

Opposition voting concentrated on:

- non-salary compensation (addressing inadequate disclosure of underlying performance criteria, use of discretion, and the quantum of proposed rewards), 47% of votes against company proposals.
- the election of directors (addressing individual director issues, overall board independence, and over-boarding), 42% of votes against company proposals.

Case study – Election of directors

LPPI voted against 11 directors across eight companies due to a lack of Board independence. At AARTI Industries Limited (India: Specialty Chemicals) for example, LPPI voted against two executive directors who served on the majority non-independent Audit Committee (results not disclosed).

At Titan Company Limited (India: Apparel, Accessories & Luxury Goods), LPPI voted against one director due to poor attendance without satisfactory explanation. Result: 17.5% Against.

At Berkeley Group Holdings (UK: Homebuilding), LPPI voted against the Chair of the Nomination Committee due to the lack of gender diversity on the Board. Result: 12.8% Against.

Case study – Non-salary compensation

LPPI voted against 18 out of 49 (37%) compensation votes across 23 companies.

At Prosus NV (Netherlands: Internet & Direct Marketing Retail), LPPI voted against the remuneration policy and report. This was due to factors including a significant portion of long-term incentives that were not performance related, early vesting of the long-term performance grant, and excessive remuneration from an insufficiently transparent incentive plan. Results: 15.0-16.0% Against.

At Godrej Properties Limited (India: Real Estate Development), LPPI voted against the CEO's remuneration plan. This was due to a lack of transparency in the context of weak financial performance. Result: 11.1% Against.

Shareholder proposals

There were no shareholder proposals at companies in the global equities fund during the quarter.

Shareholder Engagement

Company and manager engagements are underway on an ongoing basis, directly through board seats and Limited Partner Advisory Committees (LPAC) for private market assets, and more conventionally through shareholder engagement with listed companies.

LPPI's engagement partner Robeco has completed a fifth full quarter of engagement activity. The RI Dashboard (page 4) presents engagement headlines for the quarter which confirm the Robeco Active Ownership Team undertook 36 activities in total, and the predominant focus (by topic) was Human Rights.

Page 5 of the Dashboard summarises the status of each live engagement theme (as it stood at the end of Q3 2021).

The Active Ownership Report at Appendix 2 (a copy of which is available for Committee members to view in the online Pensions Library) provides detailed narrative on thematic engagements underway with listed companies (representing shares held by the Global Equities Fund, or corporate bonds held by the LPPI Fixed Income Fund).

Each quarter, we provide further insights into one of the live themes underway by the Robeco Active Ownership Team.

Robeco Active Ownership case study – Food Security

Food insecurity stems from economic and social conditions that hinder sufficient availability of and access to food. This differentiates food insecurity from the personal state of hunger and creates an important link to investors. Agricultural input providers and food companies play an important role in shaping the circumstances that could foster food security. Therefore, investors in these companies have a significant opportunity to contribute to SDG^R 2: End Hunger, achieve food security and improved nutrition and promote sustainable agriculture.

The persistent concern for food insecurity in civil society is reflected in an increased awareness of the issue among regulators. There is widespread recognition of food security as a defining development challenge for the 21st century. With that in mind, agricultural

policy is being stretched in new dimensions. New factors and challenges that need to be considered by policymakers are as diverse as poverty, food price volatility, climate change, the role of gender in rural areas, and developing agricultural technology. All of these strands make concerted action for food security an imperative. Regulators will expect international agricultural companies to make valuable contributions to retain their social, or even legal, license to operate.

Progress so far for LPPI's companies under engagement has been positive. An agricultural machinery producer managed to adapt its conventional tractors to service the needs of smallholder farmers. India constitutes a hub for the company's small tractor business, which manufactures tractors of 20-35 horsepower. Sales of tractors with lower horsepower represent 10-15% of global tractor sales. The same company has been allocating research and development (R&D) expenditures for developing products tailored to low- and middle-income countries. Our engagement objective focused on 'innovation management' was successfully closed due to evidence of the company's efforts to support farmer productivity and incomes in food-insecure region.

Robeco Active Ownership case study – Cyber Security

At theme launch in 2018, the significance of cybersecurity had come of age: research showed the annual cost of cybercrime had reached approximately \$500bn. Furthermore, an increasing body of evidence pointed to the materiality of cybersecurity in relation to stock prices. One study found an average negative stock price reaction of 5% as a result of companies' cyber breaches, with the negative impact in the cases of 'mega breaches' reaching far higher levels. The growing number of cyberattacks has prompted companies to dramatically increase spending on products to counter the threat among governments, corporations, and individuals alike. The scale of the recent SolarWinds breach suggests this is a trend that will not be reversing soon.

One company in our engagement group scored well on most engagement objectives, showing an exemplary approach to cyber governance & oversight. This approach is embodied in the Audit & Risk committee overseeing related risks and the significant technology experience on the board. Over the course of our engagement, the company committed to improve its reporting on how cyber risks are addressed throughout the company, including details on how cybersecurity is included in the executive compensation criteria. Another best practice is that the company holds third party assessments on the maturity of its program, with high scores compared to its peers.

4. Collaborations and Partnerships

LPPI participates in a range of investor groups and partnerships which provide opportunities for shared learning and a platform for collective action. The following are headlines for 2021 Q3 2021.

IIGCC Net Zero Announcement

LPPI was confirmed as a new signatory to the Institutional Investor Group on Climate Change (IIGCC) Net Zero Asset Manager Commitment within [announcements](#) made by IIGCC on the first day of COP26 (1st November 2021). The Net Zero Asset Manager commitment forms part of the IIGCC's Net Zero Investment Framework, which sets a range of requirements for the development and disclosure of net zero strategy, targets and activities. LPPI will continue to keep client funds updated as our work on net zero evolves.

Stewardship Code Submission

LPPI has submitted its Annual Report on Stewardship and Responsible Investment (2020/21) to the Financial Reporting Council, ahead of the October 2021 deadline. The report is our submission to be a signatory to the revised UK Stewardship Code (2020) and reflects LPPI's commitment to high standards of stewardship defined as the responsible allocation, management, and oversight of capital.

The Code comprises a set of 12 'apply and explain' Principles for asset managers and asset owners. The Principles are supported by reporting expectations which indicate the extensive information organisations must publicly disclose.

The Code has four main sections:

- Purpose and Governance
- Investment Approach
- Engagement
- Exercising Rights and Responsibilities

The FRC will assess LPPI's Report and confirm (in early 2022) whether it meets the standard required for gaining signatory status.

PRI Reporting – Update

For the 2021 reporting cycle, PRI piloted a new reporting system for signatories, which resulted in issues with specific areas in the reporting system. These issues resulted in some investor and service provider signatories not being able to submit a full and complete dataset, affecting the 2021 data quality.

As a result of this, PRI have decided to take a staged approach to release the 2021 outputs.

The first stage commenced in October 2021, with the release of the Private Transparency Reports. Given the issues with the submission, signatories (including LPPI) have a period of

four weeks to communicate any changes needed to the indicators affected by the issues. The PRI will then make the changes.

The second stage will be the release of the Public Transparency Reports and the Private Assessment Reports in the summer of 2022.

Finally, they have also delayed the next reporting cycle until 2023, to allow for improvements to be made to the process and reduce the occurrence of issues in the future.

For more information, please see [here](#).

Local Authority Pension Fund Forum (LAPFF) Annual Holdings Exercise Completion

LPPI has supported client funds to share information on listed equity holdings with LAPFF. This exercise is completed annually to support the planning of engagement activities by the Forum. LAPFF's engagement activity on behalf of LGPS pension funds is summarised in 'Quarterly Engagement Reports', available [here](#).

Occupational Pensions Stewardship Council (OPSC)

LPPI has become a member of the newly launched OPSC (the Council). The Council is a new industry peer group set up to promote and facilitate high standards of stewardship of pensions assets.

The Council has been created by the Department for Work and Pensions (DWP) to provide schemes with a forum for sharing experience, best practice, research, and providing practical support. Through this, the DWP aim to develop a stronger overall voice of trustees within the market, especially in relation to service providers. It also hopes to enable opportunities for schemes to collaborate on stewardship activities such as shareholder resolutions, climate change, corporate governance and other topics.

For more information, please see [here](#).

CDP Non-disclosure Campaign

LPPI participated in the 2021 CDP (formerly Carbon Disclosure Project) non-disclosure campaign which targets persistent non-respondents to their questionnaires in industries the CDP has identified as high impact across the themes of climate, water, and forests. At the headline level, LPPI was one of 168 investors participating (a 56% increase in the year before). LPPI co-signed letters to nine companies requesting their participation in the 2021 cycle. The results of this engagement can be found below.

	Total engaged		
	Total engaged	Total disclosed	%
Distinct companies	9	3	33%
Climate change	5	2	40%
Forests	3	0	0%
Water security	4	1	25%

5. Other News and Insights

Shareholder Voting Guidelines

The Responsible Investment Team, in cooperation with the Equities team, have drafted [Shareholder Voting Guidelines](#) for the LPPI Global Equities Fund. Recognising evolving market practices and the desire for additional detail and colour from a range of stakeholders (such as clients, beneficiaries, and asset managers) on how we approach shareholder voting, we have produced a public document that can be shared with all interested parties. The Guidelines have been approved by the LPPI Stewardship Committee and are now in operation.

Creation of the TPI Global Climate Transition Centre

From early 2022 the Transition Pathway Initiative (TPI), of which LPPI is a supporter and Steering Committee member, will begin to dramatically scale up its work through the creation of a [TPI Global Climate Transition Centre](#). This change will allow a significant increase in the number of companies being assessed, moving from 400 to 10,000 over time. It will also enable TPI to begin assessing corporate and sovereign bonds.

The centre will support investors in:

- Aligning their portfolios with net zero targets covering three major asset classes (listed equities, corporate bonds and sovereign bonds)
- Support global investor engagement initiatives such as Climate Action 100+ (which targets real world emissions reductions by the 167 most carbon intensive companies).
- Enable much more detailed analysis of the most carbon intensive companies and sectors as demonstrated by the recently launched Net Zero Standard for the Oil and Gas Sector that details exacting standards of disclosure intended to create a level playing field in corporate reporting.
- Place transparency and independent analysis at the heart of investor decision making within public equity, corporate debt and sovereign debt markets.

The increase in coverage will enhance and strengthen LPPI's responsible investment practices and considerably expand the amount of data available for reviewing transition planning by investee companies and presenting an objective evaluation of this to clients.

For Reference

CDP (formerly Carbon Disclosure Project) – A not-for-profit charity that runs the global disclosure system for investors, companies, cities, states, and regions to manage their environmental impacts. The world's economy looks to CDP as the gold standard of environmental reporting with the richest and most comprehensive dataset on corporate and city action.

GICS - Global Industry Classification System

The most widely used approach to categorising activities into industry sectors. The main standard in use for public markets with growing use for other asset classes.

For more information on GICS and the activities that fall into each sector see:

https://www.spglobal.com/marketintelligence/en/documents/112727-gics-mapbook_2018_v3_letter_digitalspreads.pdf

GRESB – Global Real Estate Sustainability Benchmark. GRESB Assessments capture information on ESG performance and sustainability best practices for real estate and infrastructure funds, companies, and assets worldwide, based on detailed information submitted by organisations applying to be assessed.

IIGCC – Institutional Investor Group on Climate Change. LPPI is a member.

INVESTOR AGENDA – The Investor Agenda is a common leadership agenda on the climate crisis that is unifying, comprehensive, and focused on accelerating investor action for a net-zero emissions economy. It draws expertise from across the investor landscape to clearly set out joint expectations. The founding partners are seven major groups working with investors: Asia Investor Group on Climate Change, CDP, Ceres, Investor Group on Climate Change, Institutional Investors Group on Climate Change, Principles for Responsible Investment and UNEP Finance Initiative. <https://theinvestoragenda.org/>

LONG-TERM INCENTIVE PLAN (LTIP) – A company policy that rewards employees for reaching specific goals that lead to increased shareholder value.

MSCI ACWI - MSCI All Country World Index

A stock index designed to track broad global equity-market performance.

The LPPI Global Equity Fund's benchmark.

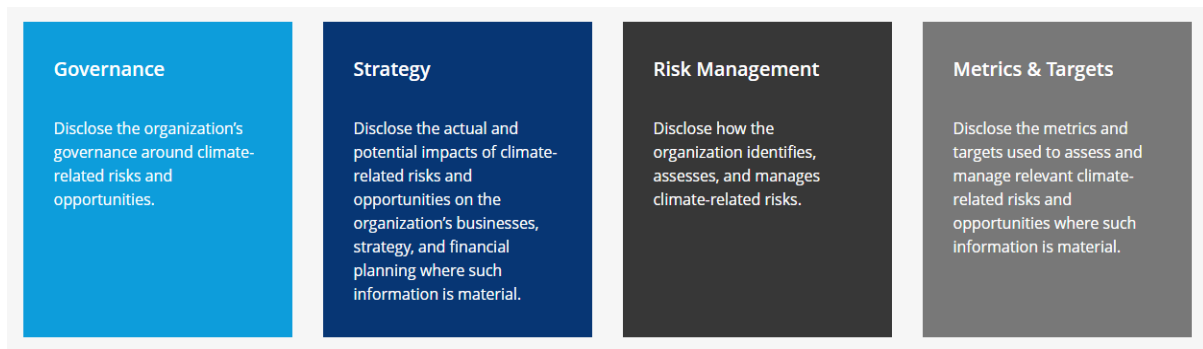
MSCI - Morgan Stanley Capital International A global index provider.

SHARE BLOCKING – The share-blocking system requires investors who intend to vote at a company meeting to surrender the right to dispose of their shares for a period in advance of the meeting. LPPI submit a DNV (Do Not Vote) where share-blocking is in place, to maintain control, flexibility, and liquidity.

TCFD - Taskforce on Climate Related Financial Disclosure

The Financial Stability Board created the Task Force on Climate-related Financial Disclosure (TCFD) to improve and increase reporting of climate-related financial information by companies and investors.

Recommendations include annual disclosure under 4 pillars:



TOTAL SHAREHOLDER RETURN (TSR) – (or simply total return) is a measure of the performance of a company's stocks and shares over time.

TPI - Transition Pathway Initiative <https://www.transitionpathwayinitiative.org/>

The TPI assesses highest emitting companies globally on their preparedness for transition to a low carbon economy. 368 companies are rated TPI 0-4* for Management Quality based on 19 separate datapoints. TPI Management Quality scores provide an objective external measure of corporate transition readiness.

UNITED NATIONS SUSTAINABLE DEVELOPMENT GOALS (SDG) – The 2030 Agenda for Sustainable Development, adopted by all United Nations Member States in 2015, provides a shared blueprint for peace and prosperity for people and the planet, now and into the future. At its heart are the 17 Sustainable Development Goals (SDGs), which are an urgent call for action by all countries - developed and developing - in a global partnership. They recognize that ending poverty and other deprivations must go hand-in-hand with strategies that improve health and education, reduce inequality, and spur economic growth – all while tackling climate change and working to preserve our oceans and forests.