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 B) and the Quarterly Active Ownership Report (available from the online Pensions Library).

It covers stewardship in the period 1st October - 31st December 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 Q4 2021 LPPI voted on 96% company proposals, supporting 89% of these.
- Investments in Brown sectors (extraction, transportation, storage, supply, and generation of energy from fossil fuels) are 2.21% of the portfolio.
- Investments in Green sectors (renewable energy generation, clean technology, and decarbonising activities) are 2.84% of the portfolio.
- LPPI's first Net Zero update is to confirm the appointment of Chronos Sustainability as our Net Zero consultant.
- The annual emissions snapshot for the LPPI Global Equities Fund, has confirmed a further reduction in the carbon intensity for the portfolio, compared with the same point in 2020. The intensity is also well below that of the fund's benchmark (MSCI ACWI)[R].
- The Climate Change Annex to LPPI's Responsible Investment Policy has been updated and is available from the LPPI website.

2. RI Dashboard – Portfolio Characteristics

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

As an enhancement, LPPI has developed and added a new section to the end of the RI Dashboard this quarter. The new Client Guide aims to assist the interpretation of metrics presented and is in response to feedback from clients that readers would benefit from additional context and explanation. We welcome comments on the new section piloted in the Q4 2021 Dashboard and feedback on ways it can be further enhanced.

Asset class metrics (*Dashboard pages 1 & 2*) offer insights on the composition of the portfolio and its general characteristics. See the summary for Q4 2021 outlined below.

<u>Listed Equities (Dashboard p1)</u>

Sector Breakdown

Categorised by GICS[R] the largest sectoral exposures for the Global Equity Fund (GEF) are Information Tech. (27%), Consumer Staples (15%), and Industrials (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 Q4 2021 Microsoft remains the largest holding in the GEF. Nestlé and Visa remain in the top three as the second and third largest holdings in the GEF respectively. Accenture, Colgate-Palmolive, Starbucks, and Pepsi's positions remained unchanged (4th, 5th, 6th, and 7th respectively) between Q3 and Q4. Below the top 7 holdings, Costco moved up 2 positions, to 8th largest holding whilst Alphabet and Experian (8th and 9th in Q3) replaced by Apple and Adobe to become 9th and 10th.

Portfolio ESG Score

The GEF's Portfolio ESG score has increased from 5.3 to 5.4 between Q3 and Q4. In the same period the equivalent score for the benchmark increased from 5.1 to 5.2.

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 Q3. By value, the coverage of the GEF represented within the globally high emitting companies under TPI assessment remains unchanged from Q3, at 12%.

The number of GEF companies in scope of TPI scoring has decreased by 2 since Q3 2021, changing from 24 to 22.

Of the 22 companies in TPI scope:

- 97% (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 up from 90% in Q3 2021, which is a reflection of three companies TPI scores being re-evaluated and improving to TPI 3.
- 4 companies are scored below TPI 3 and are under monitoring.

The Real-World Outcomes section of the dashboard features examples of socially positive investments and this quarter the focus is on Listed Equity. Pages 6-8 share information on a selection of investments within the Lancashire Fund portfolio which are developing solutions in large, small and mid-cap companies.

Other asset classes (Dashboard p2)

Private Equity

Sector and geographical exposures remained unchanged to those reported in Q3 2021. The portfolio continued to have a strong presence in the United States (47%) and the largest sector exposure continued to be Information Technology (31%).

Infrastructure

The geographical exposures to UK based Infrastructure slightly decreased, moving from 47% exposure in Q3 to 43% in Q4. The largest sectoral exposure remained in Traditional Energy, Renewable Energy, Waste, which makes up 37% of the portfolio.

Real Estate

Sector and geographical exposures remained similar to those reported Q3 2021. The portfolio continued to be largely deployed in the UK, with 74% assets here. The largest sectoral exposure continued to be Industrial assets, increasing to 38% 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 Lancashire County Pension Fund (LCPF) portfolio (as the denominator) also affects Brown and Green % shares quarterly.

Compared with Q3 2021, Brown exposure has decreased from 2.38% to 2.21%. The biggest contributor was the removal of two extractive fossil fuel assets within the GEF. However, this was slightly offset by the addition of 'Brown' assets identified as part of a recent audit (Q4 2021), located within existing pooled funds (Infrastructure and Private Equity). Growth in the value of LCPF's Fund (as the denominator) between Q3 and Q4, led to further influences on the overall reduction to the proportion of Brown assets.

Compared with Q3 2021, Green exposure has decreased from 3.08% to 2.84% of the portfolio. The change reflects a reduction in the overall value of assets identified as Green, predominantly from an Infrastructure asset valuation update. Growth in the value of LCPF's Fund (as the denominator) between Q3 and Q4, also contributed to the overall reduction to the proportion of Green assets.

Investments in renewable energy generation from Wind, Solar, Hydro, and Waste make up 76% of total Green exposure, and 96% of Green exposure is via 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 at 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.

<u>Shareholder Voting - LPPI Global Equity Fund (GEF) *(Dashboard page 3)*</u>

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 October - 31st December 2021 encompassed 50 meetings and 337 resolutions voted. LPPI voted at 96% meetings where GEF shares entitled participation. The shortfall reflects an issue under investigation involving interactions in the voting chain between LPPI's proxy voting services provider and local sub-custodian regarding entitlement to vote.

Company Proposals
LPPI supported 89% of company proposals in the period.

Voting against management concentrated on:

- the election of directors (addressing individual director issues, overall board independence, and over-boarding), 43% of votes against company proposals.
- non-salary compensation (addressing inadequate disclosure of underlying performance criteria, use of discretion, and the quantum of proposed rewards), 27% of votes against company proposals.
- the support of shareholder resolutions, covering topics including climate change, human rights, diversity, and political lobbying (23%).

Case Study – Directors Related

- LPPI voted against eight directors across four companies due to a lack of Board independence. At Groupe Bruxelles Lambert (Belgium: Multi-Sector Holdings) for example, LPPI voted against one director nominee due to the lack of overall Board independence. Result: 33.8% Against. No other vote results disclosed.

- At The Estee Lauder Companies Inc. (USA: Personal Products), LPPI withheld support for one director nominee due to over-boarding. Result: 9.2% Against.

- At Guoco Group Limited (Hong Kong: Industrial Conglomerates), LPPI voted against the Chair of the Nomination Committee due to the lack of gender diversity on the Board. Result: 0.4% Against.

Case Study – Non-Salary Compensation

- At Nike (USA: Footwear), LPPI voted against the say on pay. This was due to factors including a significant portion of long-term incentives that were not performance-related (and undesirable metrics for the portion that was), and excessive awards. Result: 28.1% Against.

- At Medtronic (Ireland: Health Care Equipment), LPPI voted against the say on pay. This was due to changes in the long-term incentive plan (LTIP), alongside the additional complexity introduced. Result: 9.7% Against.

Shareholder Proposals

- At Autozone (USA: Automotive Retail), LPPI supported the shareholder resolution requesting the company introduce reporting on short and long-term greenhouse gas emissions reductions targets in line with the Paris Agreement[R]. The vote passed with 70.4% support.

- At Microsoft (USA: Systems Software), LPPI supported a shareholder resolution requesting the company release a transparency report detailing the effectiveness of workplace sexual harassment policies. The vote passed with 78.0% support.

- At Nike (USA: Footwear), LPPI supported a shareholder resolution requesting more comprehensive information regarding their political contributions. The vote resolution did not pass but received support of 30.5%. LPPI also supported a shareholder resolution at Nike requesting the company publish a human rights impact assessment examining the actual and potential impacts of its cotton sourcing. The resolution received support of 27.7%.

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 73 activities in total, and the predominant focus (by topic) was Environmental Management.

Page 5 of the Dashboard summarises the status of each live engagement theme (as it stood at the end of Q4 2021).

The Active Ownership Report 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 live themes underway by the Robeco Active Ownership Team, this quarter we share insights on focus themes in the year ahead.

Robeco Active Ownership: new engagement themes for 2022

Each year in Q4, Robeco clients submit engagement priorities and suggestions to inform new themes for the year ahead. These suggestions are aggregated and presented at the annual client panel for further discussion. The four new engagement themes for 2022 are below and will be rolled out across the year.

Net Zero Emissions
Net Zero commitments of asset owners and asset managers require increased climate coverage. This engagement theme will be an expansion of the Net Zero Emission engagement theme launched in 2020, focussing on high carbon emitting companies that are lagging in their transition to net zero.

Natural Resource Management
Water and waste are critical factors that influence environmental stability. Environmental regulation is rapidly increasing for both corporates and investors. This engagement theme will focus on companies that face environmental issues such as seabed and land mining, PFAS emissions, water scarcity, agrochemical waste and plastic waste.

Diversity, Equity, and Inclusion
Companies play a crucial role in creating diverse, equitable and inclusive (DEI) workplaces through their human capital strategy. The theme will aim to improve embedding DEI in companies' human capital strategies. Companies will be expected to set clear targets to strengthen DEI practices and outcomes. Further, companies will be expected to measure and disclose meaningful data and outcomes related to workforce composition, promotion, recruitment, retention rates and equity pay practices.

Nature Action 100
25% of all species on Earth are at risk of extinction by 2050. This engagement will be part of a global collaborative engagement program, building on the lessons learned from Climate Action 100[R]. The focus of the engagement will be on terrestrial, fresh water and marine biomes. Dependencies and potential impact on biodiversity, such as deforestation, overfishing and pollution will be assessed. The Nature Action 100 governance structure is currently under negotiation and aims to build on the Nature benchmark of the World Benchmarking Alliance.

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 Q4 2021.

Net Zero by 2050 Update

In partnership with our client pension funds, LPPI has set the goal of achieving Net Zero portfolio emissions by 2050. In November 2021 we signed the Institutional Investors Group on Climate Change (IIGCC)[R] Net Zero Asset Manager Commitment, which forms part of the IIGCC Net Zero (1.5°C) Investment Framework (NZIF). We will be collaborating with and are well placed to learn from partners, peers and industry leaders through our participation in this IIGCC initiative. More information about this is available from the LPPI website.

The IIGCC 1.5°C framework will inform LPPI's approach to aligning the portfolio we manage with the goals of the Paris Agreement whilst remaining focussed on sustainable investment outcomes for client pension funds. As our Net Zero analysis and planning evolve, we will keep client funds updated and share insights into the actions we are taking, and the progress being made.

Our first update is to confirm LPPI's appointment of Chronos Sustainability as our Net Zero consultant. Chronos will be providing advice, support, and practical assistance for developing LPPI's Net Zero route map and an implementation plan for the initial steps of a long-term pathway towards Net Zero portfolio emissions by 2050.

30% Club

During 2021, the 30% Club[R] expanded its focus to include ethnic diversity in addition to gender diversity. To mark the launch of the new approach, the 30% Club set out a statement on race equity which was originally intended for publication in November 2021. LPPI provided feedback during the drafting process and have been added as signatories to the final statement as members of the 30% Club. The statement will now be published in February 2022 and contains the following targets for 2023:

- *Beyond 30% representation of women on all FTSE 350 boards, including one person of colour.*
- *Beyond 30% representation of women on all FTSE 350 Executive Committees, including one person of colour.*
- *Beyond 30% of all new FTSE 350 Chair appointments to go to women between 2020 and 2023.*

The statement also advocates for a number of actions at UK listed companies including better data collection and disclosure of the ethnic make-up of workforces and action plans to reduce race based inequalities. Signatories to the letter commit to actively engage with board Chairs, nomination committees and executive teams on the issue of racial inequality. Additionally, where insufficient progress is made against targets, 30% Club members will consider voting against the re-election of board directors beginning in 2022.

These commitments are reflective of our existing engagement priorities outlined in our Shareholder Voting Guidelines and align with our ongoing work as investor signatories of the WDI and Asset Owner Diversity Charter.

Workforce Disclosure Initiative

LPPI is an investor signatory for the Workforce Disclosure Initiative (WDI), an investor collaboration platform which seeks to enhance corporate management of workforce issues through increased transparency. At the start of the 2021 engagement cycle, LPPI identified five target companies as priorities to respond to the WDI annual survey and coordinated with other investor signatories to lead a letter campaign to encourage participation for two of these targets. Following engagement, four out of the five target companies responded to the survey providing us with enhanced insights on their workforce management.

5. Other News and Insights

Letter to LGPS Chairs – Occupied Palestine

In December 2021 the LGPS Scheme Advisory Board (SAB) discussed a letter sent to all LGPS Pension Fund Chairs in November 2021 by Michael Lynk, United Nations Special Rapporteur on the Palestinian Territories, which asks a number of questions of LGPS funds regarding their investments. The minutes of the SAB meeting held on 13th December 2021 confirmed the Board was liaising with the Local Authority Pension Fund Forum (LAPFF) regarding a response and would organise a call with Mr Lynk to take place in the early new year.

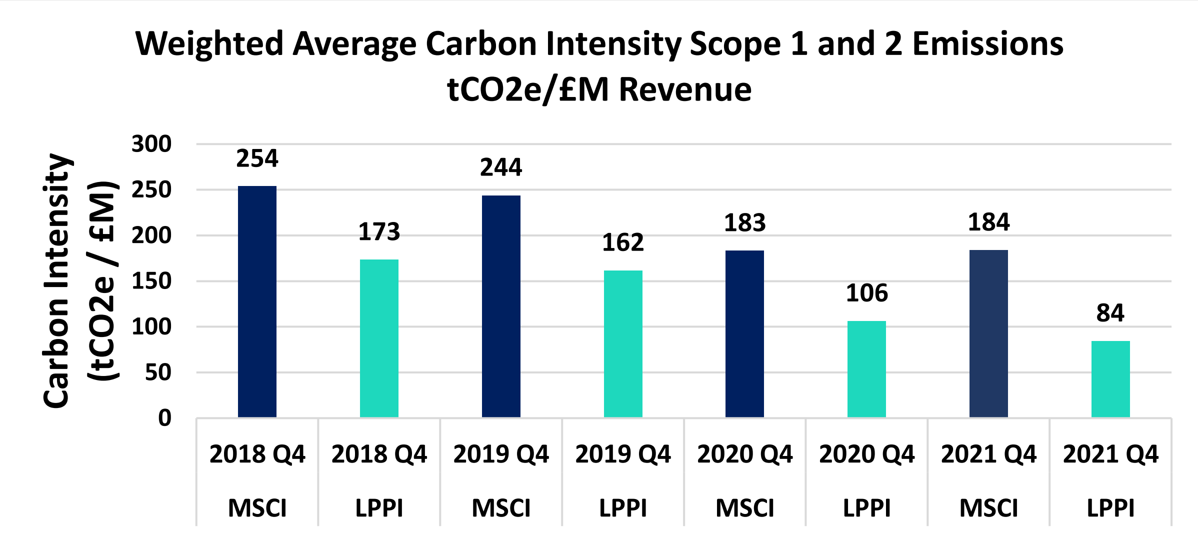
The involvement and mediation of the SAB and LAPFF are helpful given LPGS funds are facing targeted divestment lobbying whilst simultaneously awaiting details of new legislation from the UK Government "to stop public bodies from imposing their own approach or views about international relations, through preventing boycott, divestment or sanctions campaigns against foreign countries" (The Queens Speech 2021 - 11 May 2021, page 151).

GEF Carbon Footprint Analysis

LPPI reviews the carbon intensity of the Global Equity Fund at 31st December each year. The annual snapshot exercise, based on available and modelled data, has confirmed a further reduction in the carbon intensity of the fund compared with the same point in 2020 and an intensity well below that of the fund's benchmark (MSCI ACWI)[R].

Graph 1 below shows the position using a revenue measure (gross carbon emissions divided by total revenues for Global Equities Fund (GEF) companies) and includes scope 1 and 2 emissions[R].

Graph 1



Note: In calculating these numbers the following are to be considered when reconciling against other LPPI reporting:

- exclusion of cash,
- exclusion of a position in SPDR [Materials exposure] – a physical gold position, which the data provider currently is wrongly assuming as a traditional materials position from a carbon intensity point of view,
- potential rounding effects.

LPPI

Roughly 2/3 of LPPI's drop in scope 1 + 2 portfolio carbon intensity is from Utilities and Industrials sectors. For Industrials, the portfolio as at year end consisted of companies with 50% lower scope 1 + 2 intensity than the previous year. This was due to general churn of the portfolio, where three companies that collectively made up 45% of the previous years' sector carbon intensity were removed. For Utilities, it was a reduction of exposure by 1 percentage point, dropping from 2.5% in 2020 Q4 to 1.5% 2021 Q4.

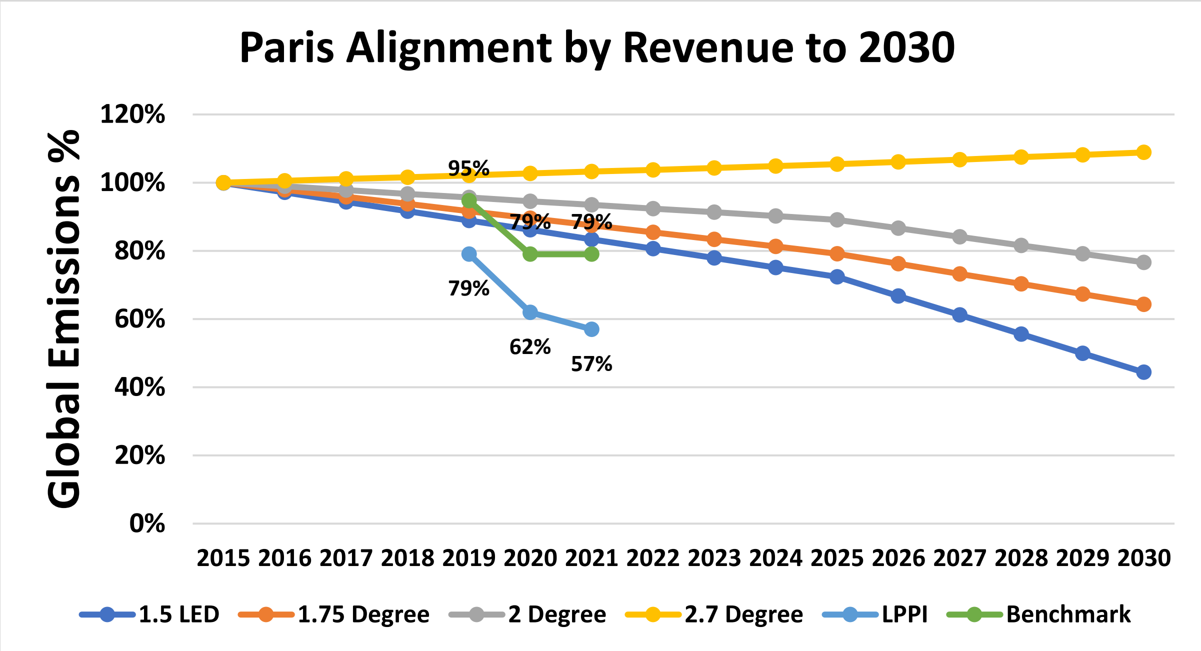
Other noteworthy drivers of the decreased portfolio carbon intensity were from Materials and Energy sectors. In both sectors there was a reduction in exposure; 0.5 percentage point drop to 1.2% overall for Materials and a 0.2 percentage point drop to 0.4% overall in Energy. The reduction of carbon intensity in Energy was due to the removal of two extractive fossil fuel companies from the portfolio, which previously made up 41% of the sector emissions.

MSCI

Our benchmark (MSCI ACWI) had a slight increase in scope 1 + 2 portfolio carbon intensity, which was mainly from Energy and Industrials. For Energy, it was the combination of an increase in sector intensity by 5.7% (an increase of 25 tCO2e / 1M USD revenue) and a sector weight increase of 0.4 percentage points, from 3.0% to 3.4%. For Industrials, it was the increase in sector carbon intensity by 17.5% (an increase of 18.3 tCO2e / 1M USD revenue). Utilities was the most noteworthy driver to a reduction in portfolio carbon intensity, with the sector weight reducing by 0.1 percentage points, a decrease from 3.0% to 2.9%.

In prior years we have shared an additional metric (from our provider of carbon metrics - Urgentem) which plots the GEF's carbon intensity against decarbonisation pathways for different global temperature outcomes by 2050. Graph 2 shows the latest position for this metric using a revenue intensity based measure (portfolio gross carbon emissions divided by portfolio revenue). It reflects scope 1, 2 and 3 emissions[R].

Graph 2



The graph observes that portfolio carbon intensity continued to fall between 2019, 2020 and 2021 for LPPI, indicating a current position beneath the trajectory for achieving the Paris Agreement goal of well below 2°c.

We caution that this complicated metric involves numerous assumptions and has material limitations we fully acknowledge.

In common with other investors, we await the development of robust market-standards for assessing portfolio alignment with the Paris Agreement, which are based on universally accepted, understandable, and decision-useful metrics.

Climate Change Annex Update

The Climate Change Annex to LPPI's Responsible Investment Policy has been updated. Available from the LPPI website, the refreshed document:

- records LPPI's commitment to the goal of Net Zero portfolio emission by 2050 in partnership with our client pension funds,
- confirms the exclusion of extractive fossil fuel companies from the LPPI Global Equities Fund (GEF) from 31 December 2021,
- reflects that climate change management is a priority theme within LPPI's Shareholder Voting Guidelines (published August 2021) and is considered in reaching voting decisions.

The decision to exclude extractive fossil fuels from the GEF is pragmatic. Our Net Zero commitment involves supporting real world decarbonisation by 2050 through encouraging all companies and sectors to transition over time. In practice, resource constraints impose limitations which will require engagement to be prioritised to financially material considerations and the likelihood for positive outcomes. Within the GEF, extractive fossil fuel companies are not a natural fit meaning small positions, conveying limited influence, but with challenging pathways to net zero.

TCFD Update

In previous reports we have highlighted the phased introduction of mandatory TCFD[R] reporting requirements for occupational pension schemes and asset managers. As it pertains to LPPI, the FCA has now issued its final rules for the implementation of climate change disclosure within an updated ESG Factbook. This commits LPPI to publish FCA aligned entity and, where relevant, product level TCFD reports by June 2024.

However, the consultation by the Department for Levelling up, Housing and Communities (previously MHCLG) on how these regulations will be translated for the LGPS has been delayed until the first half of 2022. On publication of the consultation, LPPI and its clients will still have 12 weeks to consider the proposals and provide a response if desired.

LPPI's Annual Report on RI and Stewardship 2020/21

As reported last quarter, LPPI has produced an Annual Report on Responsible Investment and Stewardship 2020/21 which offers a detailed account of our activities. Both the full report and a shorter highlights report are now available from the RI section of the LPPI website.

For Reference

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

Paris Agreement
The Agreement is a legally binding international treaty to tackle climate change and its negative impacts. The Agreement includes commitments from all countries to reduce their emissions and work together to adapt to the impacts of climate change. It entered into force on 4 November 2016.

The Agreement sets long-term goals to guide all nations to:

- substantially reduce global greenhouse gas emissions to limit the global temperature increase in this century to 2 degrees Celsius while pursuing efforts to limit the increase even further to 1.5 degrees,
- review countries' commitments every five years,

- provide financing to developing countries to mitigate climate change, strengthen resilience and enhance abilities to adapt to climate impacts.

https://www.un.org/en/climatechange/paris-agreement

Climate Action 100+
Climate Action 100+ is an investor-led initiative to ensure the world's largest corporate greenhouse gas emitters take necessary action on climate change.

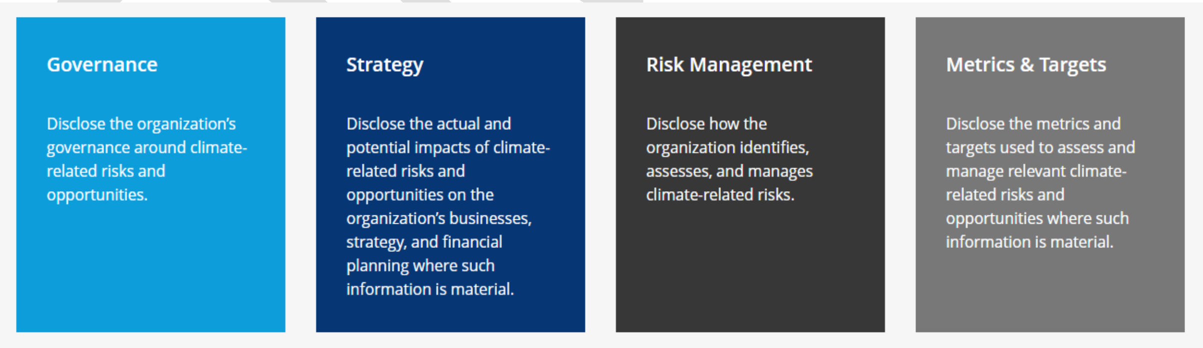
30% Club
The 30% Club is a campaign group of business chairpersons and CEOs taking action to increase gender diversity on boards and senior management teams. It was established in the United Kingdom in 2010 with the aim of achieving a minimum of 30% female representation on the boards of FTSE 100 companies.

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

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.

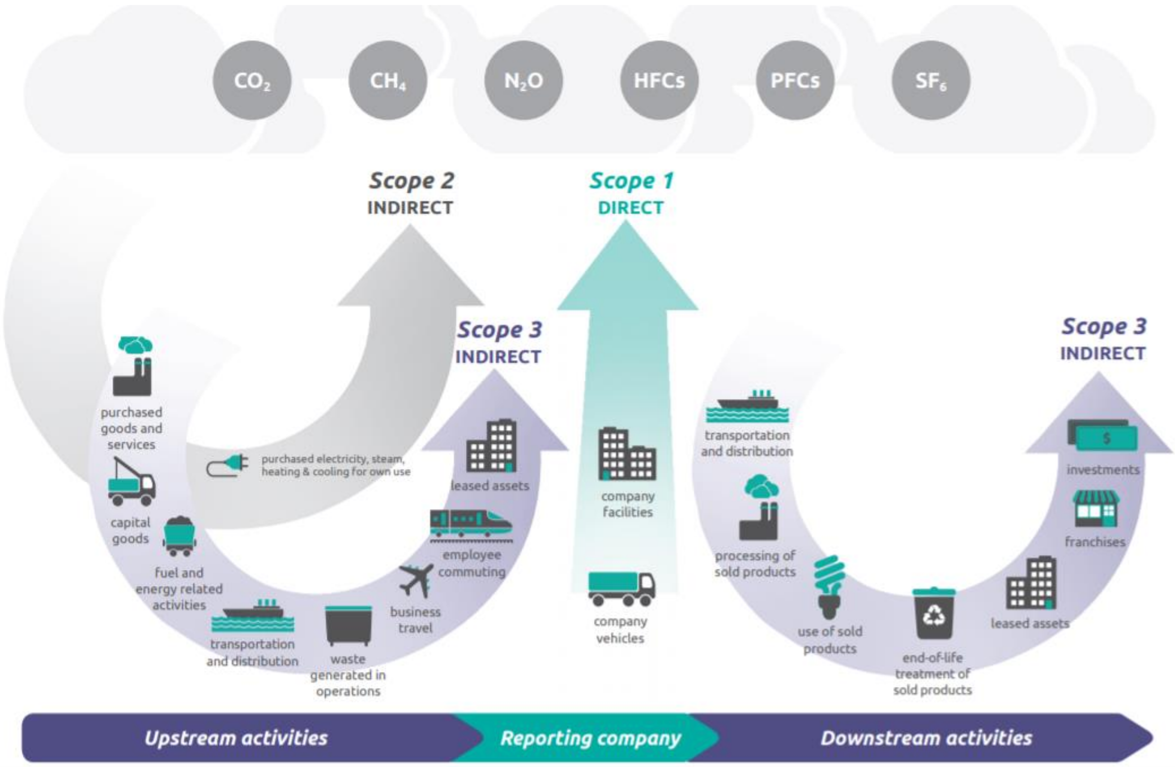
MSCI - **Morgan Stanley Capital International**
A global index provider.

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:



TPI - **Transition Pathway Initiative** https://www.transitionpathwayinitiative.org/
The TPI assesses the highest emitting companies globally on their preparedness for a 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.

Scope 1, 2 & 3 Emissions



Source: [GGH Protocol]

Scope 1 covers direct **emissions** from owned or controlled sources.
Scope 2 covers indirect **emissions** from the generation of purchased electricity, steam, heating and cooling consumed by the reporting company.
Scope 3 includes all other indirect **emissions** that occur in a company's value chain.