

Hampshire Pension Fund – Task Force on Climate-related Financial Disclosures – Draft disclosures 2021

Introduction

The Hampshire Pension Fund supports the recommendations of the Financial Stability Board's Task Force on Climate-related Financial Disclosures (TCFD). TCFD provides a global framework to enable stakeholders to understand the financial system's exposure to climate-related risks particularly affecting organisations most likely to experience climate-related financial impacts from transition and physical risks. The TCFD has been endorsed by over 1,000 companies and financial institutions representing a combined market capitalisation of over US\$12 trillion and nearly US\$118 trillion assets under management. The Fund has committed to reporting on its approach to climate risk using the TCFD framework for asset owners and sets out below its approach to managing climate risk within the TCFD's four thematic areas of Governance, Strategy, Risk Management and Metrics and Targets.

Governance

Recommended Disclosure (a)

Describe the board's oversight of climate-related risks and opportunities.

The Hampshire Pension Fund Panel and Board is responsible for agreeing investment objectives, strategy and structure and for developing and agreeing the Responsible Investment Policy. All of the Hampshire Pension Fund's investments are managed by specialist external investment managers. The Panel and Board receive regular reports from the Fund's investments managers, which includes their management of responsible investment.

To assist with managing the Pension Fund's Responsible Investment policy and monitoring its activities, the Panel and Board has created a specific Responsible Investment Sub-Committee.

Since 2019 Hampshire Pension Fund Panel and Board has considered 4 separate reports specifically addressing Climate Change risks. These are summarised as follows:

- July 2019 the Panel and Board considered a report concluding a review of the Fund's Responsible Investment strategy and the creation of the Responsible Investment Sub-Committee.
- March 2020 the Panel and Board agreed and published the Pension Fund's first annual update on Responsible Investment, including carbon footprint analysis of the Fund's listed equities.
- March 2020 the Panel and Board agreed to move the Fund's passive global equity portfolio to a *Climate Aware* strategy, reducing the carbon footprint of the portfolio.
- November 2020 the Panel and Board agreed to move one of the Fund's active global equity portfolios to a *Paris Aligned* strategy, reducing the carbon footprint of the portfolio.

Recommended Disclosure (b)

Describe management's role in assessing and managing climate related risks and opportunities.

The Deputy Chief Executive and Director of Corporate Resources is responsible for implementation of Pension Fund Panel and Board decisions. Day-to-day implementation of the Pension Fund's Responsible Investment policy is delegated to the external investment managers, who operate under the Pension Fund's policy on Responsible Investment and are responsible for:

- portfolio management including individual decisions on purchase, retention, and sale of investments,
- decisions on corporate actions and corporate governance (proxy voting),
- responsible investment activity including analysis and engagement with companies.

This is overseen by the Pension Fund's officers with oversight from the Deputy Chief Executive and Director of Corporate Resources.

An annual carbon footprinting exercise is used to assess both the risks from Climate Change and also areas of opportunity. In addition, the Hampshire Pension Fund has employed a specialist Responsible Investment (RI) advisor, MJ Hudson Spring, to assess and report on:

- i) The extent to which its external investment managers take account of Environmental, Social and Governance (ESG) risks in their investment process, including the extent to which they have a systematic process in place to assess the risks of the companies which it invests in, including consideration of Climate Change exposure.
- ii) Both a portfolio and individual company/stock analysis of carbon exposure, which includes relative carbon footprint, carbon intensity and an assessment of overall climate change exposure.

The Hampshire Pension Fund is a signatory of the UN PRI and will complete its asset owners survey for 2020 including those related to climate-change and will reflect on the results with a view to how it can incorporate the results in its future reporting.

Strategy

Recommended Disclosure a)

Describe the climate-related risks and opportunities the organisation has identified over the short, medium, and long term.

The Hampshire Pension Fund has a global investment strategy widely diversified by geography, asset class, sector and manager. Given the diversified nature of the Fund's strategy it will be exposed to all of the risks identified in the TCFD analysis, though the degree and timing of the impact cannot be accurately gauged.

The largest allocation in the Pension Fund's investment strategy is to equities, therefore the Fund's primary concern is that its investment managers and the management of the companies in which they invest have fully assessed climate-related risks and the potential impact on asset valuations, in particular from:

- obsolescence, impairment or stranding of assets;
- changing consumer demand patterns; and
- changing cost structures including increased emissions pricing, insurance and investment in new technologies.

The Fund also recognises that there is uncertainty over the direction and speed of policy changes in this area.

With respect to short term policy risk the Pension Fund monitors and discusses the status of its property investments with its appointed investment manager, who are now required to participate in the Global Real Estate Sustainability Benchmark (GRESB) annual assessment and report performance against the benchmark.

With respect to medium and longer term risk, the Fund ensures responsible investment considerations, including Climate Change, continue to be imbedded throughout the investment and management processes of all the external investment managers and that the managers continue to manage climate related risks and opportunities. As a public sector fund, reputational risk is also a particular concern, though not for financial reasons.

Recommended Disclosure b)

Describe the impact of climate related risks and opportunities on the organisation's businesses, strategy, and financial planning.

Responsible investment principles and considerations, including Climate Change and Sustainability are addressed in investment manager appointments.

As confirmed by the Pension Fund's specialist RI consultant, all but one of the Fund's investment managers are PRI signatories. The Pension Fund strongly encourages managers to become signatories and to adhere to the principles.

The Pension Fund has identified two of its portfolios (passive global equities and one global equity portfolio) that can be transitioned to lower carbon alternatives without compromising the investment return that the Fund requires to meet its Funding Strategy. The Fund will continue to discuss with its investment managers where there are opportunities to improve environmental outcomes that also correlate with positive investment performance.

Recommended Disclosure c)

Describe the resilience of the organisation's strategy, taking into consideration different climate related scenarios, including a 2°C or lower scenario.

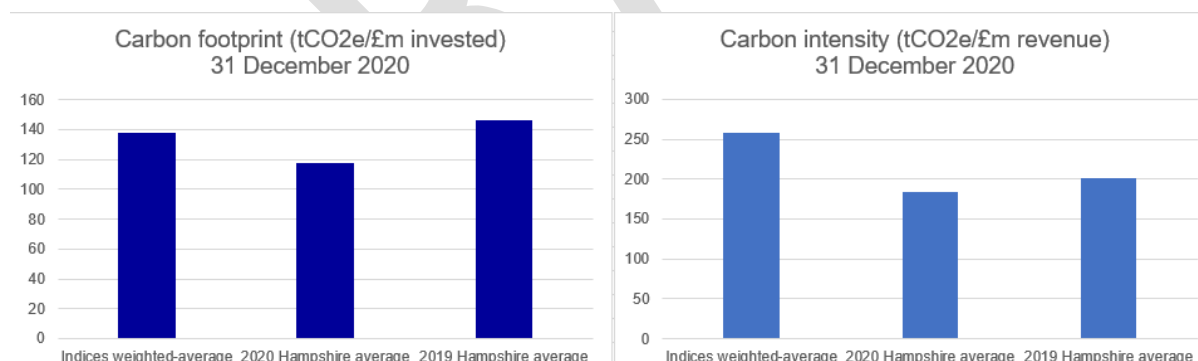
The Hampshire Pension Fund believes that Climate Change is a systemic risk and thus, a material long-term financial risk for any investor that must meet long-term obligations.

The Fund recognises that scenario testing is an inexact science due in part to inadequate disclosure from portfolio companies. The Fund continues to encourage greater levels of climate-related disclosures through its discussions with its investment managers and their engagement and voting with the companies they invest in to address this issue.

The Fund is well diversified and has allocations to real assets and through its infrastructure portfolio, the renewable energy sector, therefore Climate Change risks should have a relatively limited impact on returns.

The Fund has already taken steps to re-align its equity portfolio exposure in a managed way to continue to reduce carbon exposure, through moving to lower carbon funds for a number of the existing investment manager mandates, and anticipates that this will encompass further mandates within the next 12 months.

The Fund is well placed as its existing Portfolio already compares well to the weighted average of carbon output for the weighted average of the comparator indices for both Carbon Intensity and Carbon Footprint, and its current strategy is shown to be reducing carbon impact:



Risk Management

Recommended Disclosure a)

Describe the organisation's processes for identifying and assessing climate-related risks.

The Hampshire Pension Fund's external investment managers are responsible for identifying and managing all risks associated with their investments, and this includes Climate Change. This means that external investment managers take into account any climate-related risks when making their investment decisions.

The Pension Fund Panel and Board, supported by its independent advisor, the Pension Fund's officers and the consultants they have commissioned, monitor and scrutinise the Fund's investment managers to help ensure that climate risks are being assessed and addressed. The Fund's listed equity carbon footprinting is used to inform this process.

Recommended Disclosure b)

Describe the organisation's processes for managing climate related risks.

• Development of Specific Investment Strategies

The Pension Fund has put in place the following specific investment strategies:

- i) holding its portfolio of global passive shares (that track world stock markets) in a Climate Aware Fund, which skews its investments towards companies in each sector that have the best environmental credentials,
- ii) the largest active equity mandate is a strategy which already provides the lowest carbon footprint across the Fund's equity portfolios, and is a fund whose carbon footprint is only 6% of the average footprint of the 'FTSE All World' index,
- iii) has agreed to move its second largest equity portfolio to a Paris Aligned strategy,
- iv) the Pension Fund's allocation to global infrastructure includes 14% of commitments to renewable energy investments, which includes the production of wind, solar and other renewable energy, and
- v) has put in place specific benchmarking of its property portfolio against the Global Real Estate Sustainability Benchmark (GRESB) to ensure a focus on the environmental sustainability of the portfolio.

• Formal Advice

The Hampshire Pension Fund has taken formal advice from specialist responsible investment consultants MJ Hudson Spring, who reviewed the current Responsible Investment Strategy and suggested areas for development, provided training for the Pension Fund Panel and Board, recommended a roadmap of further responsible investment developments and reviewed the Fund's external investment managers' responsible investment approaches. The review of the Fund's investment managers is a key tool for the Pension Fund in analysing the comparative risks and opportunities from Climate Change across its portfolios, and highlighting areas to focus on with the investment managers.

• Exercise of Ownership Responsibilities

Ownership activity relating to Climate Change risk is carried out by the Fund's investment managers who are required to exercise the Fund's voting rights, to incorporate analysis of Environmental, Social and Governance (ESG) issues into their investment analysis and expected to engage on these issues with the

companies in which they invest. Voting activity is published on the Pension Fund's website and a summary of key issues are reported to the Responsible Investment Sub-Committee for the members to include in their scrutiny of the Fund's investment managers.

Recommended Disclosure c)

Describe how processes for identifying, assessing, and managing climate-related risks are integrated into the organisation's overall risk management.

The Hampshire Pension Fund's overall approach to risk management is described in its Risk Management Report, which is part of its Annual Report and published on the Fund's website at: <https://documents.hants.gov.uk/pensions/HPF-AnnualReport2020.pdf>. Climate Change is addressed as follows.

Risk	Description	Likelihood	Impact	Mitigation
Investment	Environmental, social and governance (ESG) factors including the impact of climate change – that these factors materially reduce long-term returns.	M	H	As set out in the Fund's Responsible Investment Policy, the Fund's external investment managers are required to consider ESG factors in their investment decisions, including any negative contribution to climate change and the overall risk from the impact of climate change, and to exercise the Fund's responsibility to vote on company resolutions wherever possible. They have also been instructed to intervene in companies that are failing, thus jeopardising the Fund's interests, by voting or by contacting company management directly.

The Pension Fund currently reports extensively on environmental, social and governance issues including Climate Change. This includes:

- reports for the Pension Fund Panel and Board and the Responsible Investment Sub-Committee.
- an annual report on Responsible Investment Activity which is considered by the Responsible Investment Sub-Committee and sent to pensioners and included in the Fund's Annual Report.
- a specific page on the Pension Fund's website <https://www.hants.gov.uk/hampshire-services/pensions/local-government/about-the-scheme/joint-pension-fund-panel/responsible-investment> containing further information.

The Pension Fund continues to pro-actively challenge all its investment managers to improve their reporting on carbon emissions and to justify their investment decisions.

Metrics and Targets

Recommended Disclosure a)

Disclose the metrics used by the organisation to assess climate related risks and opportunities in line with its strategy and risk management process.

The Hampshire Pension Fund monitors and publishes the shareholder voting of all its external Investment Managers on issues including Climate Change.

The Pension Fund annually reports the carbon footprint and carbon intensity (for Scope 1 and 2 emissions) for all of its equity investments and one of its multi-asset credit portfolios, and can currently measure the carbon emissions of 53% of its investments (50% last year). The Fund is committed to repeating the capture of this data on an annual basis, and is working with its other investment managers to extend the coverage of this information.

Following the analysis of its responsible investment consultants MJ Hudson Spring, the Pension Fund has a list of the investments it holds which are the highest ESG risks, including the risk of negatively contributing to Climate Change. This list is the basis of discussion with the Fund's external investment managers to ensure that they are aware of where their greatest exposures lie, and to seek their investment rationale for continuing to hold such stocks.

Recommended Disclosure b)

Disclose Scope 1, Scope 2, and, if appropriate, Scope 3 greenhouse gas (GHG) emissions, and the related risks.

The Hampshire Pension Reports on Scope 1 and 2 emissions in its analysis. Scope 3 data was not considered to be of a sufficiently robust standard and is not currently included in the disclosures of the companies that the Pension Fund invests in.

The TCFD recommendations call for asset owners to disclose a weighted average carbon footprint. As at 31 December 2020 the Fund's average carbon footprint was 117 tCO₂e/£ revenue, which is 15% lower than the weighted average of the comparator indices and 20% lower than it was at the end of December 2019. This data includes 53% of the Pension Fund's investments, up from 50% in the previous year.

Recommended Disclosure c)

Describe the targets used by the organisation to manage climate related risks and opportunities and performance against targets.

The Pension Fund is not currently using quantitative targets as part of its Responsible Investment Policy but is committed to continuing to monitor the carbon footprint and intensity of its investments and working with its investment managers to identify opportunities to improve environmental outcomes that also correlate with positive investment performance.