

HAMPSHIRE COUNTY COUNCIL

Decision Report

Decision Maker:	Pension Fund Responsible Investment Sub-Committee
Date:	7 September 2021
Title:	Climate Change scenario analysis
Report From:	<i>Director of Corporate Operations</i>

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Purpose of this Report

1. This report provides the Responsible Investment Sub-Committee with an update of the Fund's progress engaging with its investment managers on scenario analysis on the impact of Climate Change on the Pension Fund's investments.

Recommendations

2. That the Pension Fund Responsible Investment Sub-Committee notes that :
 - i) the Task Force on Climate Related Disclosures (TCFD) includes a requirement to "*describe the resilience of the organisation's strategy, taking into consideration different climate related scenarios*".
 - ii) the TCFD's 'Inevitable Policy Response' outlines the policies that are expected by the PRI by 2025 to begin meeting Governments' net zero carbon emission targets.
 - iii) the Pension Fund has engaged with its Investment Managers to undertake its first 'Climate Change scenario analysis', based on asking Investment Managers to assess the impact of the 'Inevitable Policy Response' on their Hampshire portfolio, in order to test the resilience of the Hampshire Pension Fund's investments.
 - iv) whilst engagement for this first assessment has been positive, further work will be undertaken to develop and embed the Climate Change scenario analysis impact assessment and reporting with Investment Managers.

Executive Summary

- The Pension Fund is a signatory to the Principles for Responsible Investment (PRI) developed by the United Nations, and has adopted the reporting principles of the Taskforce on Climate Related Financial Disclosures (TCFD). The TCFD framework includes the requirement to *'describe the resilience of the organisation's strategy, taking into consideration different climate related scenarios'*. Having discussed with its consultants MJ Hudson Spring the Pension Fund has decided that for its first climate related scenario it would ask its investment managers to consider the impact of the *Inevitable Policy Response* policy forecasts developed by the PRI.

Inevitable Policy Response

- The Inevitable Policy Response outlines the policies that are expected by the PRI by 2025 to begin meeting Governments' net zero carbon emission targets. The PRI says *'it offers markets the crucial next layer of detail on when, where and how these commitments will start to shift the macroeconomic context through forceful policy implementation across a range of key policy levers'*.
- The PRI's forecast policies are based on developments to eight key policy levers.

 Carbon pricing <ul style="list-style-type: none"> Carbon taxes Emissions trading systems Border carbon adjustments 	 Coal phase-out <ul style="list-style-type: none"> Prohibiting regulations Emissions performance standards Electricity market reforms 	 100% clean power <ul style="list-style-type: none"> 100% clean power targets Renewables capacity auctions and other support policies 	 Zero emission vehicles <ul style="list-style-type: none"> 100% zero emission vehicle (ZEV) sales legislation Manufacturer ZEV obligations ZEV consumer subsidies
 Low-carbon buildings <ul style="list-style-type: none"> Prohibiting regulations for fossil heating systems Purchase subsidies for low-carbon heating systems Thermal efficiency regulations for new build and retrofit Minimum energy performance standards for new appliances 	 Clean industry <ul style="list-style-type: none"> Emissions performance standards for industrial plant Subsidy for new or retrofit clean industrial process 	 Low-emissions agriculture <ul style="list-style-type: none"> Methane or nitrous oxide emissions tax or cap-and-trade system Subsidy for low-emissions agricultural practices and technologies Farmer education and technical assistance programmes 	 Forestry <ul style="list-style-type: none"> Strong policy action against deforestation, such as monitoring and penalties, supported by consumer pressure Incentives for reforestation and afforestation via domestic action and carbon markets


'Just Transition' lens to ensure social and political feasibility

- The PRI's 2021 top-ten policy forecasts are:

- Carbon Border Adjustments Mechanisms (CBAMs) for carbon will become increasingly a policy option. This could lead the United States to announce a national carbon pricing system as early as 2023, and we forecast by 2025, and signal a strong carbon price path to reach a backstop of \$65 by 2030.
- The European Union's evolving commitments will deliver substantial carbon prices. By 2030, we expect EU policy to backstop an EU Emissions Trading System (ETS) carbon price of \$75/tCO₂ to ensure long term action toward decarbonisation in heavy emitting sectors.
- In India, rapidly evolving Indian policy and prospects for market reforms and pricing has already ended further investment in new coal.
- China will end construction of new coal fired power production after 2025, driven by new policies to facilitate its 2060 net zero target and ongoing market liberalisation.
- The United States will end all coal-fired power generation by 2030, through a combination of emission performance standards and carbon pricing at the Federal and State levels, combined with market forces.
- The United States will implement a binding and credible 100% clean power standard for 2040, ending unabated fossil electricity generation.
- China, France, Germany, Italy and Korea will end the sale of fossil fuel cars and vans in 2035. Jointly these large markets will accelerate the auto industry transition to electric drive, and precipitate further policy action internationally.
- All major industrial economies including the US, Germany, Japan and China will require all new industrial plants, led by steel and cement, to be low-carbon by 2040, through a combination of emissions performance standards and carbon pricing.
- The US, Canada, Australia and other major agricultural producers will have comprehensive mitigation policy in place by 2025 to reduce emissions from production of crops and livestock pricing.
- Major tropical forest countries will end deforestation by 2030, with domestic policy responding to international climate finance and corporate supply chain pressures.

7. For the purpose of the Hampshire Pension Fund's first Climate Change scenario analysis the details of the policy forecasts in the *Inevitable Policy Response* are less important than their use as a tool to give the Fund's investment managers a common starting point for considering the impact of Climate Change of their portfolios.

Scenario Analysis

8. The Fund has received a variety of responses from its investment managers, ranging from those where further work would be required to be able to fully assess impact, to those that have undertaken their own detailed modelling in producing their response. The engagement exercise between the officers and the investment managers has gone well, and on the whole, the Fund's investment managers have taken this seriously. Although the responses received have varied, this is partly due to this sort of exercise being fairly new to the sector, and as time passes it is expected that an improved level of information will be received, as it becomes more commonplace for investors to adopt the reporting principles of the TCFD. Therefore at this point it is too early to report on findings due to the range of depth in which investment managers are currently able to respond.
9. Undertaking its first Climate Change scenario analysis provides a number of learning points for the Pension Fund:
 - Experience of asking this type of question of its investment manager, which can be used for future iterations of the exercise to ask more precise and well defined questions.
 - Showing the Pension Fund's investment managers' capability in considering the impact of Climate Change in terms of their ability to engage with the question and use their resources and expertise to provide an answer. This can be used by the Pension Fund to challenge its investment managers and work with them to better develop their ability to manage Environmental, Social and Governance (ESG) investment issues.
 - Providing an indication of how Climate Change could effect the Pension Fund's investments and what the higher risk areas may be.
10. Officers will report further updates to the Responsible Investment Sub-Committee following further engagement with the Fund's investment managers on this area.

Climate Change Impact Assessments

11. Hampshire County Council utilises two decision-making tools to assess the carbon emissions and resilience of its projects and decisions. These tools provide a clear, robust, and transparent way of assessing how projects, policies and initiatives contribute towards the County Council's climate change targets of being carbon neutral and resilient to the impacts of a 2°C temperature rise by 2050. This process ensures that climate change considerations are built into everything the Authority does.
12. The Pension Fund itself has a negligible carbon footprint, but it recognises that the companies and other organisations that it invests in will have their own carbon footprint and a significant role to play in the transition to a lower carbon economy. Therefore the Pension Fund recognises the risk that environmental, social and governance (ESG) factors including the impact of climate change can materially reduce long-term returns. The Pension Fund has a role to play as an investor, in ensuring that its investment managers are suitably considering the impact and contribution to climate change in their investment decisions and acting as a good steward to encourage these companies to play their part in reducing climate change. This is explained further in the Pension Fund's RI policy [InvestmentStrategyStatementincludingRIpolicy.pdf](#) (hants.gov.uk).
13. This paper specifically seeks to address the impact of Climate Change on the value of the Pension Fund's investments through the use of a scenario analysis based on the PRI's *Inevitable Policy Response*.

REQUIRED CORPORATE AND LEGAL INFORMATION:**Links to the Strategic Plan**

Hampshire maintains strong and sustainable economic growth and prosperity:	No
People in Hampshire live safe, healthy and independent lives:	No
People in Hampshire enjoy a rich and diverse environment:	No
People in Hampshire enjoy being part of strong, inclusive communities:	No
OR	
This proposal does not link to the Strategic Plan but, nevertheless, requires a decision because: For the ongoing management of the Hampshire Pension Fund.	

Section 100 D - Local Government Act 1972 - background documents

The following documents discuss facts or matters on which this report, or an important part of it, is based and have been relied upon to a material extent in the preparation of this report. (NB: the list excludes published works and any documents which disclose exempt or confidential information as defined in the Act.)

DocumentLocation

None

EQUALITIES IMPACT ASSESSMENT:

1. Equality Duty

The County Council has a duty under Section 149 of the Equality Act 2010 ('the Act') to have due regard in the exercise of its functions to the need to:

- Eliminate discrimination, harassment and victimisation and any other conduct prohibited by or under the Act with regard to the protected characteristics as set out in section 4 of the Act (age, disability, gender reassignment, marriage and civil partnership, pregnancy and maternity, race, religion or belief, sex and sexual orientation);
- Advance equality of opportunity between persons who share a relevant protected characteristic within section 149(7) of the Act (age, disability, gender reassignment, pregnancy and maternity, race, religion or belief, sex and sexual orientation) and those who do not share it;
- Foster good relations between persons who share a relevant protected characteristic within section 149(7) of the Act (see above) and persons who do not share it.

Due regard in this context involves having due regard in particular to:

- The need to remove or minimise disadvantages suffered by persons sharing a relevant protected characteristic that are connected to that characteristic;
- Take steps to meet the needs of persons sharing a relevant protected characteristic that are different from the needs of persons who do not share it;
- Encourage persons sharing a relevant protected characteristic to participate in public life or in any other activity in which participation by such persons is disproportionately low.

2. Equalities Impact Assessment:

Equality objectives are not considered to be adversely affected by the proposals in this report as the proposals do not directly affect scheme members