SOUTH YORKSHIRE
PENSIONS AUTHORITY

Action Plan for Delivering the Net Zero Goal

Update
March 2023

Contents

Introduction

At its meeting in March 2021 the Pensions Authority agreed its first Action Plan for Delivering the Net Zero Goal and agreed to update the Action Plan annually. This second annual update reflects on the progress that has been made and identifies a revised set of actions flowing from that progress and developments in the wider environment including the evolution of regulation.

The goal which the Authority has set for itself is ambitious, but that ambition is founded on the belief that institutions such as SYPA need to show leadership in order for the required change to be delivered with the overall degree of urgency required by the position in which the world finds itself. In that context this plan is simply the starting point. The climate challenge that the Authority wishes to address is urgent and in doing so we should not allow the perfect to be the enemy of the good, we need to make progress now so that we can begin the journey to net zero as quickly as possible.

This Action Plan has been developed using the Institutional Investors' Group on Climate Change (IIGCC) Net Zero Investment Framework. This recognises that there can be no "one size fits all" route to net zero, investors like SYPA need to focus on maximising efforts that achieve decarbonisation in the real economy, rather than simply creating portfolios with no emissions. This requires a comprehensive investment strategy led approach supported by concrete targets (at portfolio and asset class level) combined with smart capital allocation and engagement and advocacy activity. Such a strategy led approach must not just deliver emissions reductions, but also increase investment in the climate solutions which we need to achieve net zero. This approach will reduce the exposure of SYPA's investment portfolios to climate risk while increasing their exposure to climate opportunity, thus providing greater long-term protection for our scheme members' savings.

All of this does, of course, need to be seen in the context of our participation as one of 11 partner funds within the Border to Coast Pensions Partnership and we will continue to work with and gain the co-operation of the other partners and the operating company in order to achieve our goal.

There remain significant gaps in both our knowledge and the data available to us and while we will need to continue to address these. However, we will need to take specific actions in parallel with this so as to make full use of the relatively short time available to us to achieve net zero. We already report in line with the requirements of the Task Force on Climate Related Financial Disclosure and each year in our Annual Report we will present our progress both in delivering this action plan and towards achieving net zero.

This plan will continue to be developed further on at least an annual basis as we better understand our current position and the progress we are making.

Defining the Goal

It is important to understand what we mean by the goal of net zero and how it will be measured.

What we are seeking to achieve is that the net level of carbon emissions from the holdings in our investment portfolio equals zero. In itself this seems simple. However, there are a number of ways of defining carbon emissions and it is important that we understand which of these we are using so that we can pull the right levers in order to achieve our goal.

The accepted standard for defining (and measuring) carbon emissions has “3 scopes”.

Scope 1 emissions are direct emissions from company-owned and controlled resources. In other words, emissions released to the atmosphere as a direct result of a set of activities, at a firm level.

Scope 2 emissions are indirect emissions from the generation of purchased energy, from a utility provider. In other words, all GHG emissions released in the atmosphere, from the consumption of purchased electricity, steam, heat and cooling.

Scope 3 emissions are all indirect emissions – not included in scope 2 – that occur in the value chain of the reporting company, including both upstream and downstream emissions. In other words, emissions that are linked to the company’s operations.

Companies reporting in line with the requirements of the Task Force on Climate Related Financial Disclosure Standard (TCFD) must report on Scope 1 and 2 whereas reporting on Scope 3 is voluntary and as will be clear from the definition incredibly hard to measure with the significant risk of double counting as between direct producer and indirect consumer organisations. However, the data reported by fund managers to the Authority makes no distinction as to these different types of emission, and while a restricted definition might make a 2030 goal easier this is not practical and would leave the Authority open to the accusation of avoiding the key issues in emissions reduction.

Therefore, for the purpose of delivering the Authority’s Net Zero Goal the following definition will be used.

“The Authority’s goal is for the net carbon emissions from the totality of its investment portfolio to be zero by 2030.”

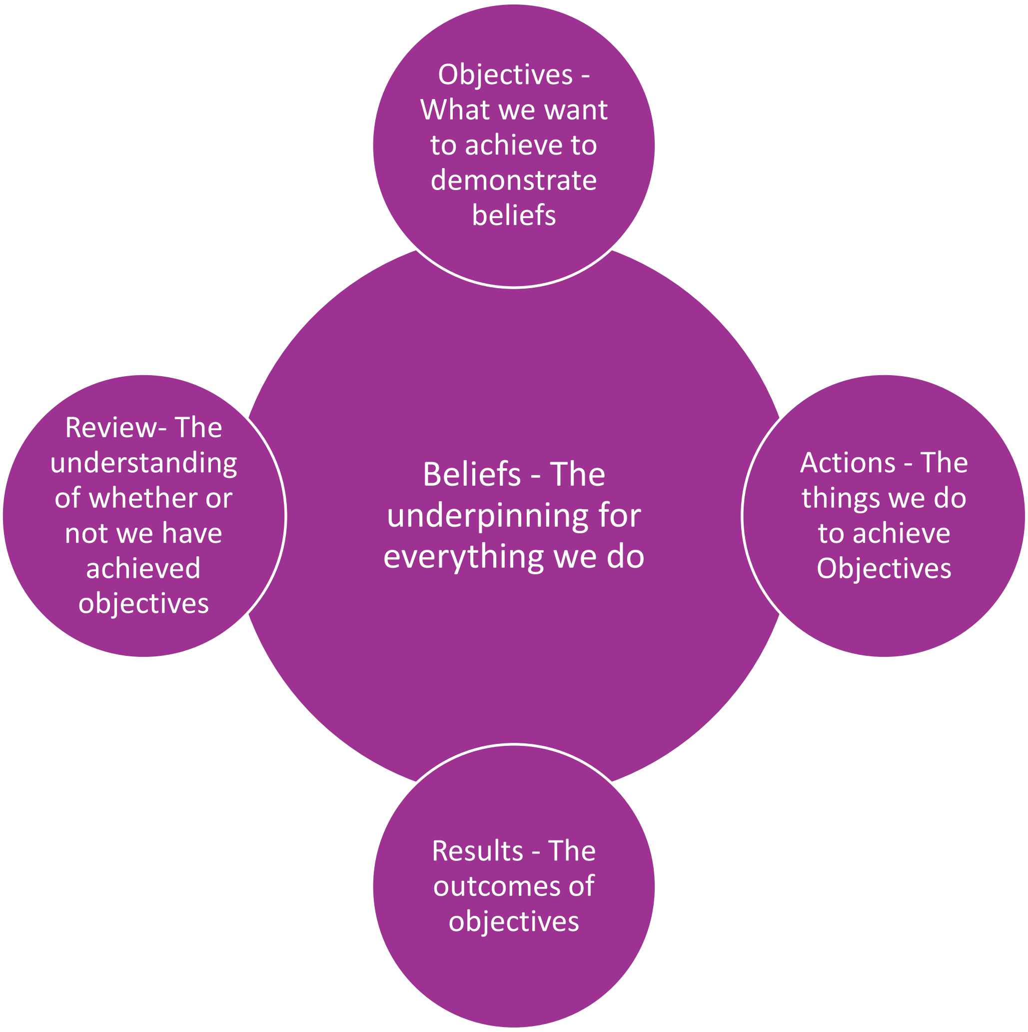
While concentrating on scope 1 and 2 emissions allows the Authority to set targets which are comprehensible and where data is likely to be available, this position will need to be kept under review as more data becomes available and the investment impacts of using specific measures becomes clear. Measurement and regulation are continually developing in this area and to a significant degree we are going to be trying to hit a moving target, particularly in the next few years when the pace of change in these areas is likely to be greatest.

In addition the Authority will separately seek to make the remainder of its operations carbon neutral over the same timescale with relevant actions included in future iterations of the corporate strategy, for example utilising renewable energy in our office, reducing the generation of waste and setting policies which promote the use of electric vehicles and/or public transport.

Governance and Strategy

Getting the governance and strategy right mean that the organisation will retain focus on specific goals and will have decision making processes which are able to receive understand and react to information on progress to specific goals as it comes through.

This is illustrated as a cycle in the graphic below



Everything we do needs to start with beliefs, they provide the framework within which we develop objectives which lead to us taking actions which lead to results which we then review to see whether we have achieved our objectives, and so the cycle goes on.

In making any decisions in relation to any of the stages of this cycle it is important to remember that the Authority is required by the LGPS Investment Regulations to ensure that it has taken proper advice. In most cases this will be provided by a combination of officers and the independent investment advisers, but in this area, there is likely to be a requirement at various points for additional specialist advice. Given the requirement to pool which is placed on LGPS funds there is also a need to ensure that Border to Coast are engaged with the Authority on this journey.

In the last 12 months we have continued to build from the foundations set out in our agreed beliefs statement continuing a dialogue with Border to Coast and the other partner funds to increase the focus on the move to Net Zero and deliver further opportunities for investment in climate positive assets.

Work has continued on the ongoing review of investment performance and on reporting progress towards Net Zero, and this will continue to be developed as data for more asset classes becomes available and the detailed requirements of new regulations become clear. This work is supported by the work undertaken by external consultants to support the review of the Investment Strategy during 2022.

The specific actions required to give effect to the structure outlined above are set out in the table below:

Ref	Action	Responsibility	By When
SG 1	Agree Investment Beliefs Reflecting the Commitment to Net Zero	Authority	Completed
SG 2	Revise Investment Strategy following 2022 Fund Valuation directly reflecting Net Zero Commitment, including further scenario and transition path analysis (to be repeated in each triennial strategy review).	Assistant Director - Investment Strategy	Completed alongside this update
SG 3	Review performance of all investments in the context of the Net Zero Commitment on a rolling basis.	Director	Ongoing
SG 4	Monitor the delivery of the Net Zero Commitment and the transition path on an annual basis	Director	Ongoing
SG 5	Create a forum to engage with Border to Coast to identify how they can assist and support the Authority on its Net Zero journey.	Director	Completed Now part of ongoing dialogue with Border to Coast

The work required to support the investment strategy review will provide a foundation for addressing the new reporting requirements. In addition we will be working with Border to Coast and their new data provider to develop the forward looking metrics that will be crucial to measuring progress towards the goal and informing future adjustments to the strategy.

Setting Targets Objectives and Reporting

Measurement and reporting are central to how we drive forward the changes that are required in order to achieve the net zero commitment. The detail of these will flow from some of the strategic work set out in the previous section and the establishment of a baseline position which enables us to understand how far we have to travel to achieve net zero.

In simple terms what we are seeking to do is establish a set of steps to reduce carbon in each element of the portfolio over a given time. How this will be achieved for individual asset classes is the subject of the next section of this plan.

This section of the framework deals with the four outer circles in the diagram on page 5, which can be described as the "plan do review" cycle.

At this stage we have some idea for around 50% of the Fund's assets by value of the distance to travel and fund managers have set targets for a number of portfolios, although these relate to their own targets for achieving Net Zero rather than the Authority's own more ambitious target. The key consideration here is that we are not the only investor in the products in which we are invested and while in terms of the Border to Coast internally managed funds we can seek to influence we cannot dictate. Nor are we able to simply switch into a carbon neutral fund because the pool does not offer one, and to do so would require a fundamental change in the Authority's longstanding investment approach (either in terms of active v passive management, or in terms of internal management v much more expensive external management) which we do not believe is justified. These issues are dealt with in more detail in the next section of this document.

For other asset classes (such as Property) we are in the process of agreeing a trajectory of emissions reduction with investment managers which will be incorporated in the next round of updates to targets under the Paris Aligned Asset Owner Initiative, and we have made some significant improvements in the availability of data over the last 12 months. At the same time setting targets will continue to be difficult and on the basis of not letting the perfect be the enemy of the good we will be looking to set emissions from all portfolios on a downward trajectory as soon as practically possible.

Setting targets alone is not enough. We need to be held accountable for our progress towards those targets. We have already begun to report publicly on our progress towards the net zero goal and also on the specific steps we have taken towards that objective.

We will also need to identify a number of specific measures that will form a core part of our reporting under the forthcoming LGPS Regulations addressing the need to report in line with TCFD requirements. The measures we will adopt, subject to any change to reflect the final regulations and being able to agree a common position across the Border to Coast partnership are:

- An emissions metric
- A carbon intensity metric
- A weighted average carbon intensity metric (WACI)
- A data quality metric indicating the proportion of the portfolio covered by the relevant metrics
- An alignment metric providing a forward-looking measure

The aim will be to produce the first four of these at both asset class and whole portfolio level while the alignment metric is only meaningful at whole portfolio level.

We will also be required to provide some scenario analysis, although at this stage the detailed requirements are not clear and we will work with colleagues through the Border to Coast partnership to ensure that this analysis is consistent across the whole partnership regardless of what, if any Net Zero goal, each partner has adopted.

The targets that have been adopted while supportive of the Authority's direction of travel are in themselves not sufficient to achieve the Net Zero Goal and other tools such as adjustments to the balance of the overall asset allocation will be required to bring the Authority closer to its goal.

Ref	Action	Responsibility	By When
TR1	Following Investment Strategy Review identify interim targets leading to net zero	Director / Assistant Director - Investment Strategy	Completed but subject to ongoing revision and refinement
TR2	Work with Border to Coast and other investors in relevant products to ensure mandates and performance objectives specifically reflect the Net Zero Commitment	Assistant Director - Investment Strategy	Ongoing
TR 3	Conduct an annual review of progress towards Net Zero and make adjustments to either targets or implementation approach as necessary while continuing to meet return objectives	Assistant Director - Investment Strategy	Annually from April 2022. This update is the second such review

Asset Class Implementation

The products in which the Authority invests are all made up of very different sorts of asset which have different characteristics, therefore it is highly unlikely that one approach to implementing net zero will be applicable across such a wide range of assets ranging from farmland to private equity investments in tech start-ups, through traditional instruments such as shares and bonds.

This section of the document looks at each major asset class in turn and identifies an initial approach which reflects the need to focus on the real economy and the practical issues associated with operating within the context of pooling, where the Authority is not wholly in charge of its own destiny. All of this also needs to be set within the context of the Authority's broader beliefs about how to do investment.

Specifically the Authority believes in:

- Being an active investor – This means picking the best stocks to invest in using the skill of individual managers. However, our moderate risk appetite means that while we believe in active investment, we invest in active products that maintain broad portfolios within a particular asset class and select the best companies in particular sectors as opposed to highly active products which would select both companies and sectors, and thus generate much more concentrated portfolios.
- Being a global investor – This means that we will be exposed to investment in emerging economies such as China and India where the stage of development means that economic growth is sometimes being driven by companies in industries such as cement which are high emitters.
- Managing money internally wherever possible – While we now invest through Border to Coast for listed assets we look to the company, where possible, to provide products using its own team rather than external managers. This makes changing products more difficult as a wholesale switch away from the current range of products could significantly undermine and destabilise this important aspect of what Border to Coast offers to its partner funds, and if we wish to make changes which would impact the investment universe we need to get agreement with other investors.
- Engagement over divestment or exclusion – The Authority has long operated on the basis that it seeks to influence companies through engagement, this is part of being rooted in the real economy.

As we progress along the road to net zero (and further along the pooling journey more generally) these beliefs about how to do investment are all likely to be challenged in different ways and the Authority will need to keep them under review to ensure that they remain compatible with achieving both our return and net zero objectives. In particular in order to hasten the move of portfolios towards investment in companies with a longer term future the Authority will be seeking to influence partners to continually reduce the revenue threshold for exclusion of pure coal and coal sands companies so that it reaches zero before 2030.

The other contextual factor to be considered before looking at the approach in each asset class is the fact that the Authority (like all other LGPS Administering Authorities) is part of a pool and needs to secure the co-operation of the other partner funds within Border to Coast in order to make progress where changes are required to investment products. The Pool has now agreed its own Net Zero objective (setting a goal of 2050) and while this is not the same as the Authority's the setting of the objective requires the setting of targets and the reporting of metrics. In themselves these will support the Authority's work while the ability to alter the asset mix through the Strategic Asset Allocation and to manage the legacy portfolio (the assets not yet pooled or not to be pooled at all) provide potential levers for accelerating or reducing the pace of movement to Net Zero.

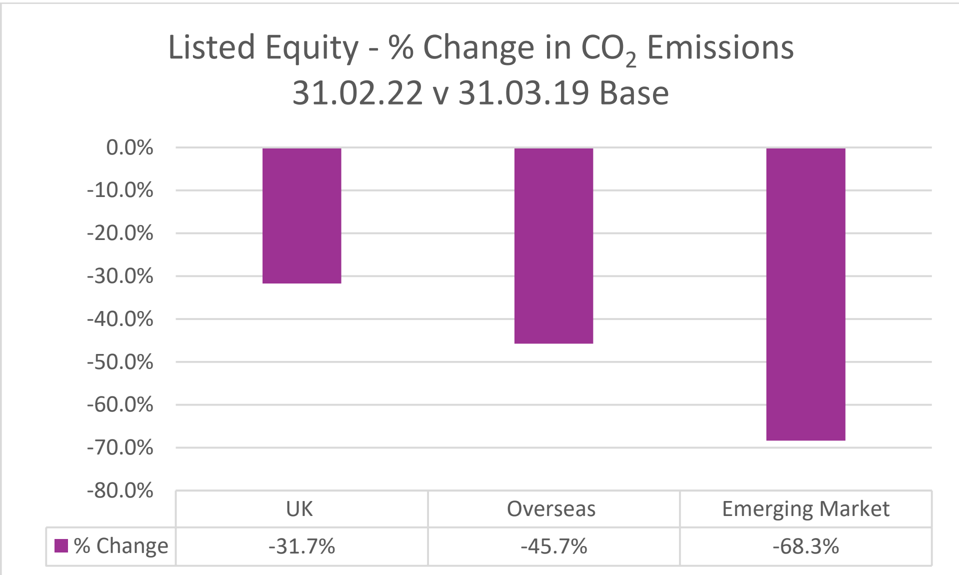
The following sections deal with each asset class in turn.

Listed Equities

The Authority's listed equity investments are managed against benchmark indices with a performance target of 1% over the benchmark and a core risk tolerance of a 3% tracking error. This latter tolerance limits the scale of "active bets" (i.e. the degree of divergence from the index) which the fund manager can take.

Border to Coast have identified a series of changes to the investment process which will make it more sensitive to the scale of climate risk posed by individual companies. These are in the process of being implemented with a target to reduce emissions from these funds by 45% - 50% by 2030 from 2020 levels.

Compared to the base year of 2019 emissions across the equity portfolios have, as shown in the graph below reduced substantially, in particular in the Emerging Markets portfolio, as a result of the restructuring of the China element of the portfolio. Some of the reduction experienced may be pandemic related and there remains a risk of some rebound in emissions as economies recover, although perhaps counteracted to some degree by the countervailing pressure for a reduction in fossil fuel use arising from the war in Ukraine.



Listed equities are the single largest asset class in which the Pension Fund is invested and in order to achieve SYPA's ultimate goal, it will be necessary to reduce the contribution to aggregate emissions from these portfolios in total by at least 50% by 2025. While the targets set by the fund manager do not reflect this maintenance of the current rate of progress would indicate that this is within the range of possible outcomes Beyond this the impact of the changes in the investment process to make it more climate aware and the weight of assets held in the different products which will be reviewed as a matter of course are likely to further influence the level of overall emissions beyond 2025.

Border to Coast as Fund Manager already operate a policy of excluding "Pure coal and coal sands" companies from the investment universe based on a threshold of more than 70% of revenues coming from these sources. The Authority will seek to influence the Partnership to further ratchet down this threshold with the aim of it being zero by 2030.

An important feature of investment in listed equities is the voting rights which are conferred on asset owners. The way in which the Authority, through Border to Coast, chooses to exercise these voting rights has the potential to accelerate progress by companies towards net zero. Border to Coast has updated and strengthened the voting guidelines on climate change for the 2023 proxy voting season. As well as voting against the reappointment of board members where companies are not making progress towards net zero as assessed by the Transition Pathway Initiative (TPI), votes against the Chair will also be cast where a company fails one or more of the first four indicators of the Climate Action 100+ Net Zero Benchmark. The Authority will review proposals for the casting of votes in relation to companies' climate transition plans and where it feels that Border to Coast policy is resulting in support for plans that do not deliver a credible move to Net Zero for a company and reserves the right to vote its portion of the shares held in a different way to the remainder of the Partnership.

The ability to exercise voting rights is supported by engagement with investee companies. Most engagement activity is undertaken by Robeco, acting for Border to Coast (the actual share owner in the pooled products). The issues associated with climate change and the achievement of Net Zero remain the single most significant focus of engagement activity. During 2021 two additional engagement themes around the Net Zero themes were added, "acceleration to the Paris Agreement", and "climate transition of the financial sector". An additional theme covering this area will also be launched during 2022, "net zero emissions", this expands on current engagements focussing on high carbon emitting companies that are lagging in their transition to net zero. Border to Coast are seeking to develop clearer tracking and reporting in this area. Successful engagement on these issues will, likely, hasten progress towards net zero, and engagement will need to remain a key tool in the armoury in order to ensure that companies in which the Authority is invested meet their commitments to reducing emissions. Climate issues continue to represent a very significant proportion of the engagement activity which we support and we report on this each quarter. The Authority will work through the Partnership to seek to define much clearer success criteria for climate engagements and clearer escalation of consequences up to and including divestment in the event of engagement not meeting those criteria.

Both the Authority and Border to Coast are also members / supporters of a number of investor bodies in the climate space such as the Institutional Investors Group on Climate Change (IIGCC) and Climate Action 100+. Involvement in groups such as these can be used to assist in tracking the progress of individual companies towards Paris alignment but can also be used to assist in influencing the development of standards in relation to data and measurement for adoption by investee companies.

Fixed Income

These portfolios are handled by a mixture of internal and external managers within Border to Coast products, using a variety of performance targets against a benchmark index. The favoured investment styles within these products tend towards relatively low turnover approaches which seek the best credits to buy with little reference to the composition of the index.

Emissions data is less available within fixed income than in equity investment, although for corporate credits there is the ability to use the same underlying data for both types of investment. However, many of the credits included in these portfolios are from sovereigns or multi-lateral institutions (such as the European Investment Bank) where the calculation of emissions data is much more difficult. While it is possible to engage with corporate bond issuers in the same way as for equities this is not possible for sovereigns and multi-lateral institutions so the ability to influence behaviour is not present in the same way.

Fund managers in this space do seek to engage with corporates and there is an increasing issuance of “green bonds” both by corporates and governments. Border to Coast will be beginning to examine options for a product in this space and the Authority will be positively supporting this work as it may provide the opportunity provide funding for a more rapid transition to Net Zero, however any investment will depend on successful due diligence being undertaken.

Given Border to Coast’s Net Zero commitment they will need to produce metrics and set targets for fixed income products, although at present sovereign bonds and the Multi Asset Credit Fund are excluded from their emissions targets due to data issues. The combination of products provides an opportunity for the Authority to set its own targets for the asset class as a whole once such data is available.

Data is only currently available for the Investment Grade Credit portfolio and this indicates a decline in emissions of close to 50% from inception. However, as indicated above data quality in relation to this product, in particular coverage of portfolio companies, is not as good as for the equity portfolios and this may mean that this statistic is not a representation of the on the ground position. However, it is a starting point for this portfolio and the Fund Manager has set specific targets for emissions reduction for the portfolio aiming for a c50% reduction in emissions by 2030. Based on the information available this may be overachieved, although overachievement here may compensate for slower progress on more recently launched fixed income funds.

The Authority will take the following actions in relation to fixed income investments in the coming year:

- Seek to understand and monitor the impact of changes to the investment process required by the adoption of the Net Zero target and assess their impact.
- As with equities seek to define much clearer success criteria for climate engagements and clearer escalation of consequences up to and including denial of debt in the event of engagement not meeting those criteria.
- Seek to ensure existing exclusion policies for pure coal and coal sands are applied across fixed income portfolios.
- Continue to support work to develop a “green” bond product as a positive way of financing the transition.

Alternatives

While there are three asset classes within alternatives (Private Equity, Private Debt and Infrastructure) these will, at this stage, be considered together.

The key initial issue here is the lack of data, which is being addressed, to some extent, through work already commissioned by the Authority and through the introduction of new regulatory requirements on asset owners which give leverage with fund managers to secure data. While this is helpful it is likely to be some time before data is comprehensive and it will also take some time to achieve the necessary quality of data, although starting later may allow some of the mistakes made in the early stages within other asset classes to be avoided.

Regardless of the data issue though alternatives are the area where Net Zero provides the greatest opportunity. We already have significant investments in renewables and other investments which support the transition (such as electric trains replacing more polluting diesels), and the low carbon transition is a clear investment theme within these portfolios. This will over time result in a build-up of assets with positive offsetting characteristics.

Any investment portfolio of the scale of SYPA's alternatives portfolio is likely to contain some investments which could be regarded as "carbon negative". The work commissioned on data should allow at least some of these to be identified, and it will then be necessary to consider whether any action is appropriate. By their nature alternatives cannot just be bought and sold like listed equities and secondary sales very often result in a loss of value, so it is likely to be necessary to hold such investments to maturity and acquire additional carbon positive investments to offset them.

In order to achieve diversification, it would not be unreasonable to seek to emphasise low carbon or transition supportive investments within the alternatives portfolio. To support this Border to Coast are have successfully launched a Climate Opportunities sleeve within the alternatives platform. The success of this Fund and growth of the market mean that it is likely that the planned 3 year investment period will be reduced to 2, which will to soe extent mitigate the scaling back of our original intended allocation. We will be looking as this Fund is deployer to ensure that these investments can be measured in terms of their offsetting characteristics and thus how they can be used in our net zero calculations.

The review of the Investment Strategy is likely to result in recommendations to more significantly tilt the alternative portfolio in a climate positive direction and we will be exploring with Border to Coast ways of doing this through the pooling framework recognising that this is likely to be a route that is deliverable given our limited in house resource.

Property

The property portfolio provides a number of opportunities in terms of the movement to Net Zero. Again, there is a lack of comprehensive data, and there are some challenges in undertaking alterations such as the addition of solar panels where the cost needs to be recovered through service charges, particularly in the current economic climate.

Over the last 12 months Abrdn as the Fund Manager have made significant progress in the overall management of ESG risks (including climate) related to the portfolio with a consequent improvement in the GRESB score and plans to improve it further in 2023. A number of projects to improve environmental performance have been identified, with some (including a solar installation on a very large industrial unit) completed. In addition "green clauses" are being added to all new leases. This programme of work will continue and provide a foundation on which Border to Coast will be able to build when it transitions into the proposed pooled product. The initial measurement of emissions has been conducted which shows a decline in emissions of around 10% between 2020 and 2021 although this may have been impacted by the pandemic. Data coverage has significantly improved and the workplan reflects the need to deliver further improvements.

The delivery of Project Chip by the end of March 2023 will set the agricultural portfolio on a road to be a positive asset in terms of the Authority's approach to climate. It will take a number of years to deliver the projects necessary to achieve this and in the next year we expect to see the establishment of both an understanding of the current position and of the opportunities available and associated actions.

The table below sets out the specific actions proposed in relation to each asset class.

Ref	Action	Responsibility	By When
AC1	Agree and implement changes to equity mandates following production of proposals by Border to Coast (subject to agreement by other investors).	Assistant Director - Investment Strategy	Completed
AC2	Consider whether further changes are required to the structure of equity products, including implementing further exclusions in the light of the impact of the changes made under AC1 and whether they are achievable given SYPA's current product mix and other investment beliefs.	Assistant Director - Investment Strategy	By December 2024 to contribute to the 2025 Strategy Review
AC3	Continue to seek tightening of the voting guidelines in relation to climate issues and actively review potential votes in relation to climate issues	Director	Annually as part of Border to Coast Policy Review and as necessary.
AC4	Work within the Border to Coast partnership to achieve clearer success criteria for climate related engagements with clearer escalation of consequences up to and including divestment or denial of debt in the event of engagement not meeting those criteria.	Director	Ongoing process feeding into the annual Border to Coast Policy Review
AC4	Consider the approach to Net Zero for Fixed Income Portfolios in the light of emerging data and undertake the identified actions set out in this Action Plan	Director & Assistant Director - Investment Strategy	During 2023-24
AC5	Support the further development of a "green bonds" product by Border to Coast	Director	Decision as to launch of product by end of 2023-24

AC6	**Identify through the work being carried out on data any particularly carbon negative alternative investments and consider whether any action is possible**	**Director**	**This action will now be taken as part of a deep dive into the legacy alternatives**
AC7	Engage Border to Coast in discussion over the best means to achieve a positive bias to supporting the low carbon transition within the alternatives portfolios	Assistant Director - Investment Strategy	Completed – Climate Opportunities Fund being provided in Series 2 Discussions to begin about further "tilts" as a result of Strategy Review during 2023
AC8	Work with Abdn to identify and initiate a programme of improvements to the environmental performance of the commercial property portfolio	Director	Completed property level action plans in place and being reported.
AC9	Deliver intended outcomes of Project Chip in terms of the climate opportunities within the agricultural portfolio.	Director	Ongoing from March 2023.

Targets and Direction of Travel

Based on the data we have available for the equity portfolios and the initial work carried out by Border to Coast in relation to their interim targets in order to achieve a 2030 goal we will need to achieve a trajectory of emissions reduction which:

- Reduces emissions by between 67% and 75% by 2025 compared to the 2020 baseline
- Accelerates the rate of emissions reduction significantly beyond that set out in Border to Coast's interim targets.

The current direction of travel is positive, and possibly ahead of Border to Coast's targets, and if maintained would on a straight-line basis result in achieving net zero between 2045 and 2048. Thus, it is clear that a significant increase in the rate of reduction is necessary, as well as needing to fill in the data gaps which continue to exist, particularly in the area of alternatives.

By the end of 2022 we expect that at least 2/3rds of the portfolio will be covered by regular emissions data and as part of the work to be carried out during 2022 on the revision of the investment strategy we will be considering the likely trajectory of emissions and the impact of a number of different wider world scenarios on the overall position of the Pension Fund. This will allow us to have a clear idea of the likelihood of the Fund delivering its overall objective of being able to pay pensions when due in each scenario. The review will also examine whether changes in asset allocation will have a positive or negative impact on emissions and thus on the Fund's ability to meet the Net Zero goal.

Risks

Achieving net zero by 2030 is a very ambitious goal, and consequently there may be a greater degree of risk that the goal is not achieved than if a less ambitious goal had been adopted. That does not mean that the goal is wrong, simply that the risk of not achieving it is greater, and therefore it is important that we understand the risks so that we can identify actions which can mitigate against them.

The key risks identified are:

Unintended Consequences

Changing one aspect of the way in which we invest can result in unexpected results elsewhere. Thus, for example, adopting a more climate aware benchmark could reduce oil and gas exposure but increase tobacco exposure which could be seen as undesirable for other policy reasons. Similarly, a focus on scope 1 and 2 emissions could result in an increased exposure to financial institutions, although they represent very significant different forms of investment risk within a portfolio. Similarly when Scope 3 emissions are examined Apple's emissions increase by 475x whereas Shell's only increase by 12x which might appear counter intuitive.

Given this it is important, given that the Authority will wish to continue to invest in internally managed products with a broadly similar risk appetite, that changes affecting the structure of mandates and the investment process are thoroughly researched and debated before implementation which in the context of the Pooling process will also require the agreement of other investors.

Inability to Secure Agreement of Other Investors

This is perhaps the most significant risk to SYPA being able to make changes to the way in which money is invested so that net zero can be achieved. Effectively the pooling process means that other investors can block SYPA from achieving its objectives (although equally viewed through a different lens SYPA could be seen as moving others in a direction which is not in line with their objectives). Fundamentally this is a challenge of the pooling process, perhaps magnified by SYPA's commitment to internal management which makes it more difficult simply to change managers. The only mitigation is for all involved to maintain an open dialogue. However, ultimately it may not be possible to secure agreement to changes which are necessary to allow the achievement of SYPA's climate goal. In this case the Authority will need to determine an appropriate course of action within the context of pooling which allows it to meet its financial objectives. This may require the reconsideration of key aspects of the Authority's current investment beliefs, and the weighing of the relative importance of different factors against the achievement of the climate goal. This action plan highlights the need for these fundamental conversations to take place as part of each strategy review and with partners on an ongoing basis.

Data Gaps

As indicated throughout this document this is an area that is bedevilled by gaps and inconsistencies in data. While the Authority has taken action to address this it will on occasion have to act in the absence of data and almost always with limited data. This is to accept that in the initial stage of the process it is important to build a momentum behind measures moving in the desired direction allowing the development of measures and the achievement of comprehensive data to follow.

Regulation is supporting the Authority's direction of travel in relation to data. However, this is likely to be a long road and there will be resource implications from securing and analysing data.

Transition Cost / Performance Erosion

This risk exists if the Authority decides to make changes in the products in which it is invested solely in order to achieve the net zero goal. It is unlikely that this will be the case. For example, in the case of the Emerging Market Equity allocation a reduction in carbon metrics has occurred as a result of the restructuring of the China allocation which was done in order to improve the overall management of the Fund and make achieving its performance objective more likely.

Whenever changes are made to the way in which funds are managed some form of transition cost is incurred. The nature and scale of the change is what determines the scale of the cost. The key issue for SYPA will be to minimise the number of times changes need to be made. The ability to achieve this is constrained by the Authority's success in achieving agreement to a direction of travel with other investors in relevant products and is therefore linked to the previous risk.

In terms of performance the Authority needs at all times to ensure that the construction of its investment portfolio is designed to achieve the actuarial return target. This is always based on assumptions and estimates and will always be subject to market events. Clearly the Authority would not make changes to its investment mandates which were designed specifically to erode performance and any changes need to be made in the context of the overall objective of being able to meet the Fund's liabilities when they become due, and the likelihood of success is a key element in each strategy review.

Success and Embedding of Process Changes

In order to deliver their own net zero goal Border to Coast have committed to changes in the investment process for the equity funds in which SYPA invests. These changes are intended to reduce emissions so as to achieve a 2050 target. However, it remains to be seen how these changes will interact with the overall approach to these portfolios of taking small "active bets". This risk will remain until there is evidence of the impact of the changes proposed by the Company and the Authority will need to focus on the impact of these changes as part of its overall oversight process.

Lack of Integration

The Authority's investment strategy has one overriding goal which is to ensure that the required returns are delivered to ensure pensions can be paid. Given that Climate Change is the largest systemic risk to the value of the Fund's assets (and hence the long-term achievement of return targets) it is important that delivering the Net Zero Goal is regarded as a key part of the overall investment strategy rather than something separate which is overlaid on the strategy at a later stage, otherwise either one or both of the return objective or the Net Zero Goal will be compromised. This will be addressed in the scope of work commissioned to support the review of the investment strategy following the 2022 valuation.

Conclusion

The actions set out in this Action Plan will not, in themselves, be enough to achieve the 2030 goal. However, we must start to make progress and the specific steps outlined here will begin moving us towards the Goal. Progress has been made since the goal was agreed in engaging with Border to Coast and Robeco, in analysing a specific approach by asset class, engaging with third parties such as Abrdn and planning a climate solutions strategy and in taking the first steps to implement these plans. These building blocks are essential to enable proper governance and oversight as we continue along the road to net zero

In these initial stages a stand-alone action plan like this is appropriate. However, in carrying out our next review of the investment strategy we must ensure that Net Zero becomes part of how we do investment rather than something separate which is overlaid on the strategy once it has been developed, and consequently this may be the last action plan of this sort.