SOUTH YORKSHIRE PENSIONS AUTHORITY

# Responsible Investment Update Quarter 3 2023/24

March 2024

# Contents

# Highlights and Recommendations

Highlights over the quarter to the end of December include:

- The casting of over 640 votes at close to 90 company meetings.
- Despite the passing of peak voting season, the overall level of engagement activity, with invested companies, increased compared to the same quarter in 2022 as Border to Coast, LAPFF and Robeco all stepped up engagement.
- High ESG ratings have been maintained for those funds where ratings are available.
- Continued focus on engaging with companies to provide clearer plans for the transition to Net Zero and their business strategies to achieve these plans.
- The overall ESG performance of the listed asset portfolios with Border to Coast has continued to be strong and better than the respective benchmarks.
- Overall financed emissions of the Border to Coast invested assets fell modestly over the quarter. However, the Emerging Markets Equity Fund saw a significant increase due to the restating of reported emissions from a constituent company.

The Authority are recommended to note the activity undertaken in the quarter.

# Background

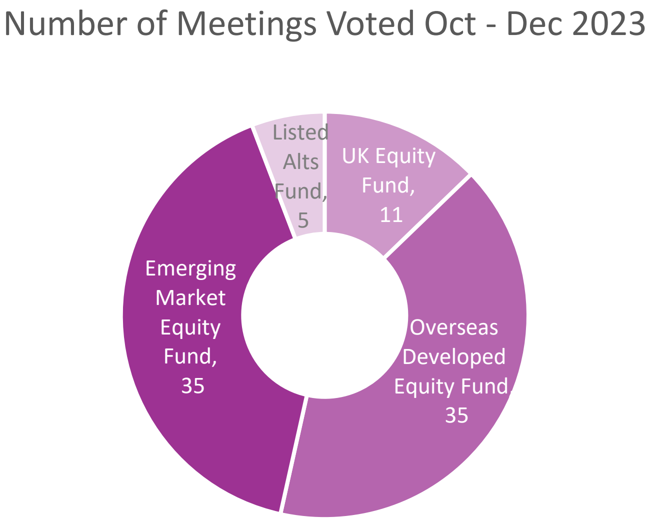
The Authority has developed a statement which sets out what it believes Responsible Investment is and how it will go about implementing it within its overall approach to investment. This statement is set out in the Responsible Investment Policy which is available on the website here.

Our approach is largely delivered in collaboration with the other 10 funds involved in the Border to Coast pool. This report provides an update on activity in the last quarter covering:

- Voting – Information on how the voting rights attached to shareholdings have been used over the period to influence the behaviour of companies to move in line with best practice.
- Engagement – Information on the volume and nature of work undertaken on the Authority's behalf to engage in dialogue with companies in order to influence their behaviour and also to understand their position on key issues.
- Portfolio ESG Performance – Monitoring the overall ESG performance of the various products in which the Authority is invested, and on the commercial property portfolio.
- Progress to Net Zero – Monitoring the carbon emissions of the various portfolios where data is available in order to identify further actions required to support progress to Net Zero.
- Stakeholder Interaction – There is considerable interaction between the Authority and stakeholders around responsible investment issues which is summarised for wider accountability purposes.
- Collaboration – Working with others to influence the behaviour of companies and improve stewardship more generally.
- Policy Development – An update on broader policy developments in the Responsible Investment space some of which directly involve the Authority and others which are of more general interest.

# Voting Activity

This quarter saw a fall in both the number of meetings and votes cast as we moved past peak voting season. Detailed reports setting out each vote are available on the Border to Coast website here. The charts below show a breakdown of the meetings and votes cast by Border to Coast on behalf of SYPA investments.



Robeco highlighted the below in their Q4 2023 Active Ownership report how investors have continued to use their shareholder rights, through proxy voting, to ensure that good corporate governance is in focus for state-owned enterprises. Robeco's analysis is detailed in the box below:

**Corporate Governance in State-Owned Enterprises (SOEs)**

SOEs are amongst the largest corporations in many countries and account for a growing share of the corporate landscape. The OECD reports that the ratio of SOEs in the list of top 500 global companies has tripled over the last two decades. The public sector held almost 11% of the listed companies' global market capitalization at the end of 2022. On top of that, in many countries, SOEs are the sole or main providers of essential services such as water or electricity.

Good governance in SOEs is, however, far from being a simple matter. If an SOE is run well, state control can provide stability. If not, political involvement may also have downsides. State ownership adds to the known corporate governance challenges faced by listed firms for a number of reasons. For one, as noted by the OECD, "the accountability for an SOE's performance is often dispersed across the public administration and among different state bodies with inherently different policy interests". Secondly, SOEs have the hard task of walking a fine line when balancing different, and sometimes conflicting, objectives. Listed SOEs have the advantage of being subject to the much stricter requirements applicable to publicly listed firms, as well as monitoring from external investors. However, minority shareholders often have limited rights and therefore little power to hold management to account.

The growing awareness of the importance of SOEs to our economies and the governance challenges that they face have prompted many countries around the world to roll out reforms. These initiatives point out the fact that there is no one-size fits-all recipe for reform. Nonetheless, the OECD Guidelines on Corporate Governance of State-Owned Enterprises, which are currently undergoing a review expected to be completed in 2024, are widely regarded as the golden standard for SOE reform.

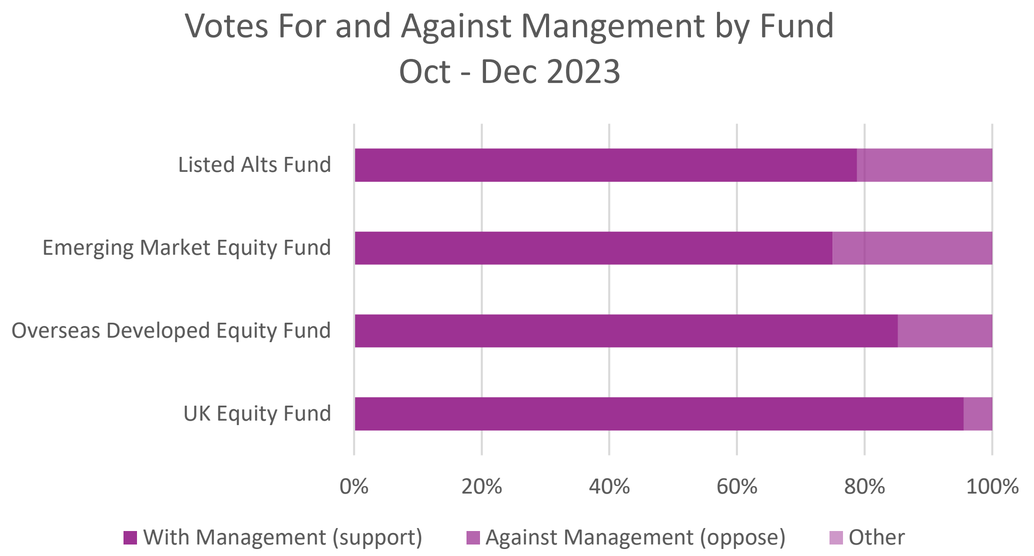
The guidelines provide a multitude of tailored recommendations for SOEs, from encouraging governments to evaluate and disclose the policy rationale that motivates state ownership, to clearly identifying which part of the public administration is responsible for exercising the state ownership function.

Investors can use their voting rights to push for these companies to adopt good governance and sustainable corporate practices. At Robeco, votes are guided by a robust policy which sets out our approach to a wide variety of issues ranging from director elections and remuneration to capital management and shareholder rights.

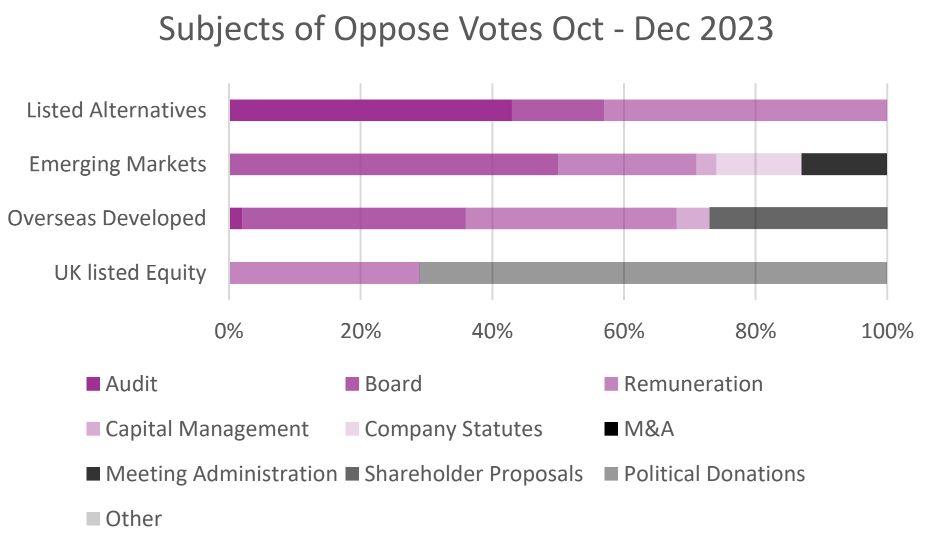
Robeco expect SOEs to have proper safeguards in place, such as the establishment of committees comprising independent members to oversee conflicts of interest, super-majorities or 'majority of minority' voting provisions, and a transparent process for board nominations. If Robeco see that insufficient safeguards are in place, they will hold companies accountable. For example, Robeco would oppose article amendments that would lead to a negative impact on minority shareholder rights or to a deterioration in the process for director nominations. Similarly, Robeco would oppose related party transactions that are not subject to an adequate oversight process that ensures minority shareholder rights are protected. Where Robeco conclude that a company has not ensured adequate minority shareholder protections, they will consider escalation via a vote against the most accountable board member or via engagement. Because poor corporate governance does make a difference – even in our day-to-day lives.

*Robeco Active Ownership Report January 2024*

The breakdown of support and oppose votes, which align with votes for or against management, is shown in the chart below.




The above graph shows the breakdown of votes cast for (in support of management) and against (in opposition to management) resolutions during the quarter. Compared to last quarter, the proportion of votes against the line taken by company management increased from 10% to 15% of total votes cast, albeit on a lower total. As has been previously reported, this reflects the "ratcheting up" of the voting guidelines in a number of areas, as can be seen from the analysis below of the subjects of oppose votes.




The above graph indicates that votes against remain more concentrated across topics than has been the case previously. The three largest areas where we continue to oppose management relate to Board composition, remuneration, and in the case of the Listed Alternatives fund, Audit. Compared to previous quarters, votes against political donations increased from close to 50% to just over 70% of the votes made against management of UK listed companies, albeit the total number of votes was lower. Notably, in the case of the Overseas Developed fund, the proportion of shareholder proposals voted against increased to over 25% of total votes against made of the Fund this quarter. It is worth reviewing the reasons why it is the case that votes are made against management.

- In the case of Board composition there are a number of things which under the voting guidelines automatically trigger an oppose vote. These include insufficient independence, insufficient diversity within the Board, and insufficient progress in terms of adapting the business to the risks posed by climate change.
- In the case of remuneration votes against are triggered by executive pay packages which are either excessive in absolute terms and/or where incentive packages are not aligned with shareholder interests and/or the performance targets are poorly defined or too easily achieved.
- In the case of votes against political donations in the UK, this reflects the fact that in the UK donations must be put to a shareholder vote and the voting guidelines oppose any donations of this kind.
- Auditor appointments are automatically opposed if reappointment would result in an unduly long term which is viewed as compromising the independence of the Auditor.

Shareholder resolutions, as can be seen within the information on notable votes in these reports linked below, can cover a whole range of issues. It can be seen that, in the last year the focus, aside from climate issues, has tended to be on diversity and human rights issues, particularly for US companies. The voting policy does not automatically support such resolutions, rather analysis is undertaken on a case-by-case basis covering both the company's and proponent's positions before votes are decided by Border to Coast on the advice of Robeco.

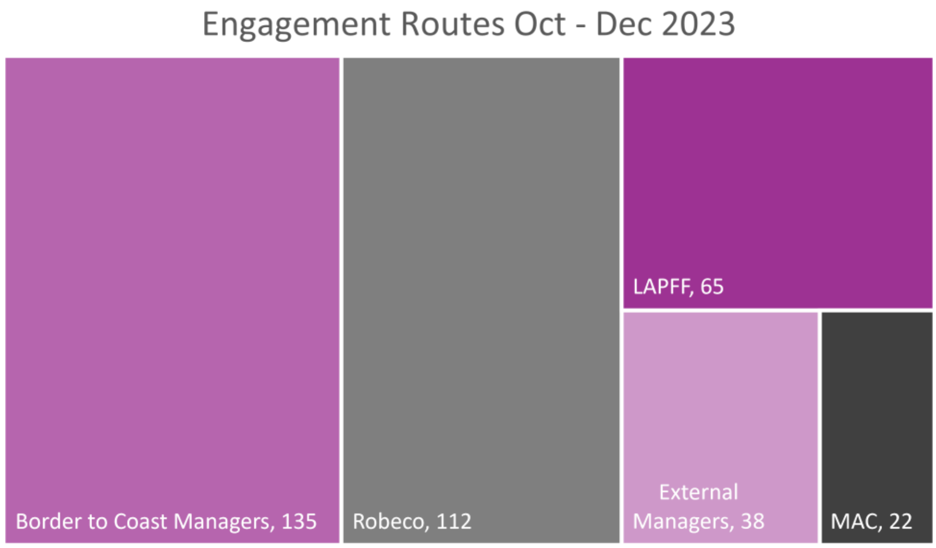
Notable votes in the quarter are summarised below and further details on the voting undertaken can be found here.

**Microsoft's** 2023 AGM agenda featured a number of routine resolutions as well as several shareholder proposals. Similar to previous years, Robeco did not support the Say-on-Pay proposal due to concerns regarding the significant height of the remuneration awarded to the CEO. Robeco identified areas of concern around the short term performance measurements on one year under the Long-Term Incentive plan. Two of the shareholder proposals related to the reporting on data operations in human rights hotspots and on the risks of facilitating AI misinformation and disinformation. Robeco supported both proposals, as they considered both to be of relevance to Microsoft and would allow shareholders additional insights into material risks.

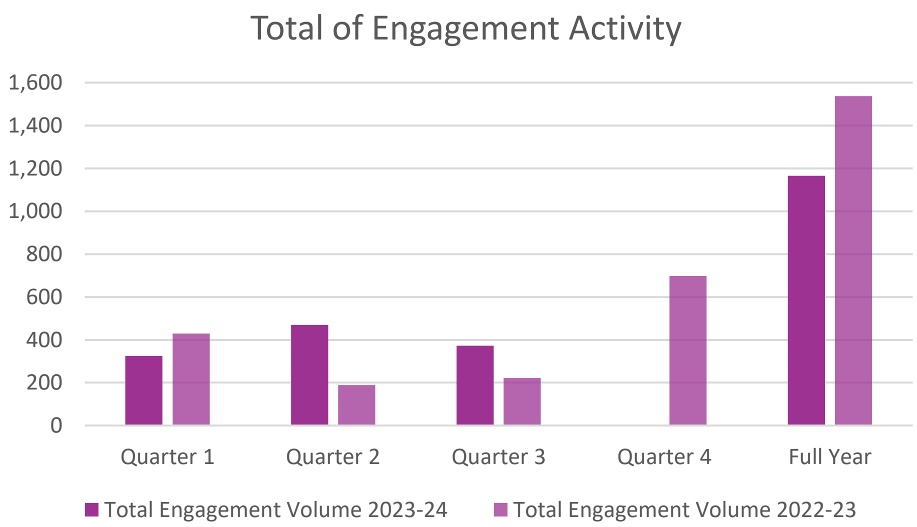
**National Australia Bank Limited, a business focussed bank,** held its 2023 AGM during the quarter which included two shareholder proposals as well as the standard items. The proposal put forward by shareholders on climate change asked the company to disclose whether all fossil fuel producers would require a climate transition plan in order to receive new lending from the bank. The proponents noted that while the company had put in place a requirement for transition plans to come into effect for oil and gas companies in 2025, this policy did not appear to apply to sub sectors such as thermal coal mining and a comprehensive approach to assessting transition plans had not been made public. Robeco decided to vote For the proposal as it aligns with our own climate change policy.

# Engagement Activity

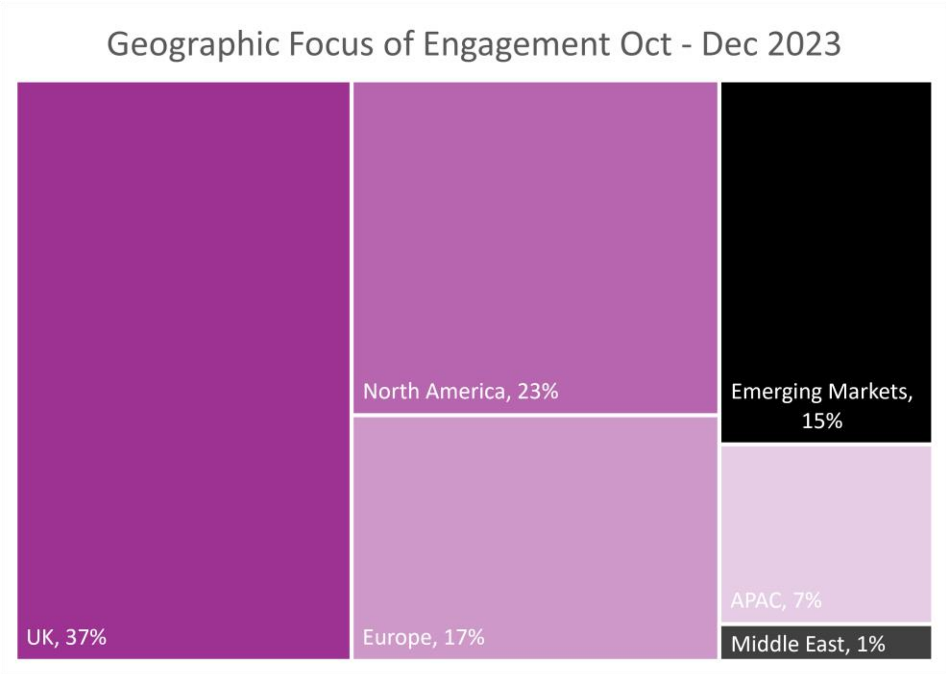
Engagement is the process by which the Authority, working together with other like-minded investors, seeks to influence the behaviour of companies on key issues. Engagement (in distinction to voting) is an ongoing process and is undertaken by those directly managing money for the Authority. This includes the investment team at Border to Coast and the external managers in the Investment Grade Credit fund together with Robeco who act on behalf of Border to Coast and the Local Authority Pension Fund Forum ("LAPFF") which acts on behalf of all its member funds. The graphs below illustrate the scale (in terms of the total number of pieces of engagement activity), the route for and the focus of engagement activity undertaken in the quarter, as well as the method of engagement undertaken.



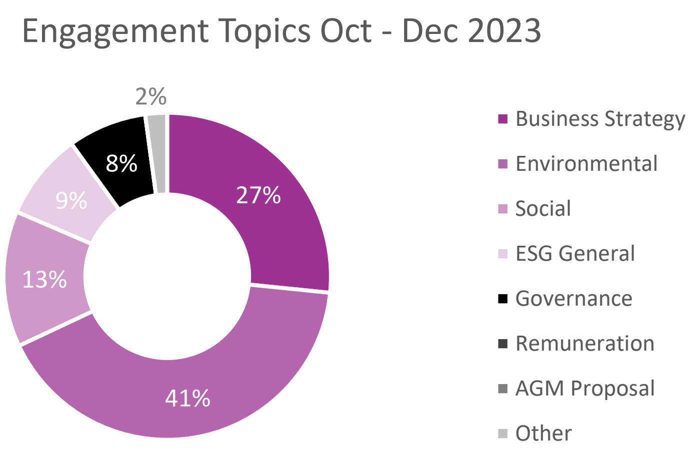

The graph below shows the level of engagement activity in the quarter has increased compared to the same quarter last year, but was down on the previous quarter (Q2 2023-24). Total activity fell quarter-on-quarter due to a decrease in engagement with companies by LAPFF and the passing of peak voting season for the year.



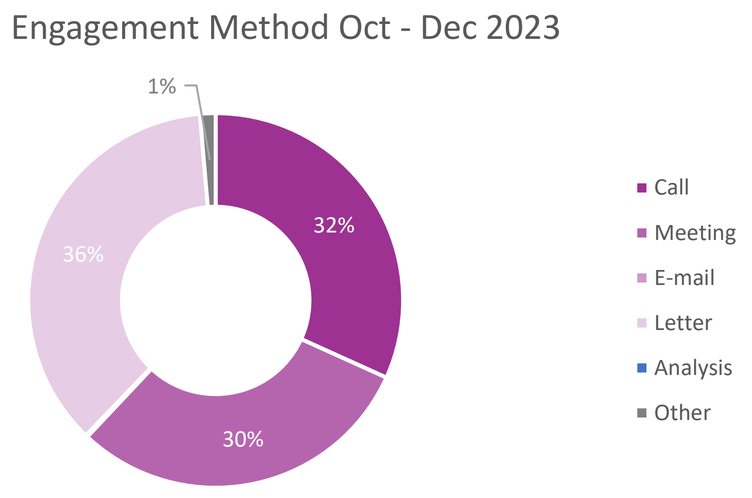
The chart below shows a breakdown of the geographic market focus in engagement over the last quarter. The focus of engagement shifted to a greater proportion being in the UK which is likely reflective of an element of home market bias.




The range of topics covered through engagement is set out in the chart below with a continuing strong focus on environmental and climate issues although the proportion of business strategy engagement increased on last quarter and also received a high degree of focus.




The method by which companies are engaged is important. Letters and emails are much more easily ignored or likely to generate a stock response from companies, whereas calls or meetings allow for more effective and genuine interaction with the company. During the quarter, there was an increase on the proportion of engagement taking place via calls or meetings from c35% to c60%.




More details of the engagement activities undertaken by Border to Coast and Robeco in the quarter are available here. Robeco provided updates over the quarter on their engagement covering the following areas: modern slavery in supply chains; Nature action 100; and Net-zero carbon emissions. The highlights from Robeco's engagement report are summarised below.

**Modern slavery in supply chains**

It is crucial for companies to identify and address modern slavery conditions – which can be hidden deep within their supply chains – to meet their obligation to respect human rights, avoid reputational risks and prevent disruptions. Failing to comply with an increasing number of regulations over modern slavery and human rights issues also poses direct consequences to companies' operations.

An estimated 50 million people are trapped in modern slavery, of which over 28 million are in forced labour, where a person's freedom to accept or refuse a job, or to leave one employer for another, is non-existent. Over 85% of cases are found in the private sector, and they are often linked to industries such as manufacturing, construction and agriculture.

For any company, developing appropriate management oversight and policies is an essential first step to tackling modern slavery as well as addressing wider human rights risks in their operations and supply chains. One of the most important actions is to conduct human rights due diligence.

Robeco expect companies to identify risks according to aspects like sourcing from conflict regions, workplace characteristics and the types of raw materials sourced, and to take appropriate actions. With this in mind, Robeco selected a list of companies to engage with based on their multi-layered supply chains, the nature of operations for raw materials production, and the geographical areas in which they and their suppliers operate. Robeco analyzed publicly available documents and research pieces from international organizations, NGOs and news sources to gain a good understanding of sectors and commodities that face a higher risk.

Robeco's engagement objectives also emphasize whether remediations to affected workers are carried out effectively, and if corrective measures are taken to prevent future recurrence, in collaboration with suppliers, workers and other stakeholders. Collaboration with various players is crucial in understanding the different contexts of each case, and is necessary for creating solutions for the workers at risk, while providing them with alternative means for decent work.

One of the challenges Robeco expect to face is lack of quality information regarding lower-tier suppliers. These are needed to assess whether the companies under engagement are well positioned to identify and remediate modern slavery risks and impacts. Although companies often have a supplier code of conduct, certification and social audits in place, these may be limited in scope, and are often mere box-ticking exercises applying only to direct suppliers.

Dedicated resources are required in order to identify high-risk regions and populations, track raw material sourcing, and compensate wages for affected workers, as well as to develop responsible recruitment policy and procurement practices. Companies also require close collaborations with suppliers' workers and management teams, civil society, and multiple departments within the company, which can be time consuming and costly to set up. However, these short-term costs will be outweighed by the long-term benefits of strong supply chain management and risk oversight, supplier resilience and efficiency, as well as reputational goodwill.

**Nature action 100**

More than half of the world's gross domestic product (USD 44 trillion) is moderately or highly dependent on nature and its services – such as the provision of food, fibre and fuel – and the unprecedented loss of biodiversity places this value at risk. By threatening these key ecosystem services, biodiversity loss and any company practices associated with it can expose both them and their shareholders to significant financially material risks. These include the physical and transition risks, the threat of litigation and regulatory action, as well as the wider systemic risks that come from harming nature.

Nature Action 100 was launched against the backdrop of aligning investor action to contribute to the GBF. It mobilizes institutional investors to establish a common high-level agenda for engagements, and a clear set of expectations to drive greater corporate ambition and action to stem biodiversity loss.

The initiative was launched in September 2023 with more than 200 investors and targets 100 companies in eight key sectors that are deemed to be systemically important in reversing biodiversity loss by 2030, such as chemicals, food, and metals and mining. These sectors are major drivers of damage to nature due to their large impacts on habitat loss and the overexploitation of resources, as well as their contribution to water and land pollution.

Companies are encouraged to set a public commitment to minimize biodiversity impacts and to conserve and restore ecosystems by 2030. They should set time-bound, science-based targets that are based on assessments of their nature related dependencies, impacts, risks and opportunities. These should be followed by an inclusive implementation plan taking into account any local communities that are affected.

Robeco reviewed their investment exposure to biodiversity risks across sectors and markets, as well as took into account our clients investment exposure, before selecting sectors and companies that they wanted to engage with under Nature Action 100. Our results suggested that biodiversity risks are concentrated in three sectors in our portfolios, which are exacerbated in our investment strategies with allocations to emerging markets. As a result, Robeco prioritized their engagement coverage with eleven companies across these three sectors: Materials (chemicals), Consumer Staples (retail, food and beverage, household and personal products) and Consumer Discretionary (retail). More than half of these companies are based in emerging markets.

Robeco's engagement approach aims to be holistic and targeted to each company's footprint and sets of impacts and dependencies. Tailored to each company, the engagements will push for a better understanding and strategy to address corporates' biodiversity footprints, including the establishment of meaningful targets and reporting frameworks, such as adopting the Taskforce for Nature-Related Financial Disclosures.

**Net-zero carbon emissions**

Investor engagement is a critical tool to ensure that companies are on a transition pathway that limits global warming to 1.5°C. In order to more effectively achieve this, in 2020 Robeco grouped all their ongoing climate change engagement efforts under their consolidated 'Net-Zero Carbon Emissions' engagement program.

Robeco's engagement activities set the expectation for companies to set long term net-zero targets, and to substantiate them with credible short- and medium-term emissions reduction strategies, implementing transition plans that ensure a reduction in real-world emissions over the next decade.

A credible climate strategy is difficult to define as each company will have its own challenges and approaches to decarbonization. Nevertheless, Robeco leverage external means of measurement such as the Climate Action 100+ Net Zero Benchmark when defining objectives.

The relevance of Robeco's engagement program hinges on the systemic risks that climate change poses to the global economy and financial system. Companies face significant transition risks encompassing legal and regulatory issues and technology and market changes, which weaken the viability of existing technologies and practices.

Companies also face physical risks from more frequent extreme weather events such as hurricanes, droughts and floods, and the longer-term issue of rising sea levels. This may cause damage to assets or bring cost increases and supply chain disruptions.

Besides these risks, there are also opportunities for companies. Indeed, they can spur growth by pursuing efforts to mitigate or adapt to climate change, using the consequences of the transition to their advantage.

Overall, Robeco registered positive progress for almost all the companies under engagement. The industries which registered the highest level of progress were the steel and cement sectors. Considered to be the hard-to-abate industries, these companies showed meaningful improvements, especially in disclosing detailed capital alignment and decarbonization strategies.

Although the oil and gas industry has taken several initiatives to address the net-zero transition, Robeco feel that there is room for improvement, especially in outlining reduction targets for Scope 3 emissions, and reallocating capex away from potentially stranded fossil fuel assets. Indeed, as Robeco witnessed in the last three years, setting targets for Scope 3 emissions has been one of the main challenges on the net zero pathway for oil and gas companies.

Having originally witnessed early progress coming from this sector, some companies unfortunately have reached a standstill at best in their decarbonization pathways after the global energy crisis. Therefore, Robeco plan to intensify and escalate their engagement efforts with them in the next year to seek more improvements.

**Border to Coast Engagement**

Border to Coast produced their quarterly Stewardship report which outlined a number of their key engagement highlights during the quarter and can be viewed here. Overall, the last quarter was quieter for voting as the main season in most markets passed for 2023. However, Border to Coast continued to engage with investee companies, most notably with water utilities Yorkshire Water and Northumbrian Water as well as airline, EasyJet.

In 2023, Border to Coast joined a collaborative engagement initiative with the UK water utility sector coordinated by Royal London Asset Management. Focus areas include sewage pollution, water leakage, climate change mitigation and adaption, biodiversity, antimicrobial resistance, and industry collaboration.

Border to Coast is leading the engagement with Yorkshire Water and Northumbrian Water on behalf of the collaboration. In October, Border to Coast met with Yorkshire Water to discuss their assessment of the Company against sector expectations. Discussion focused on areas Border to Coast had identified as priorities: pollution and maintenance of good asset health; sustainable water abstraction; and biodiversity targets and net gain.

The Company's response has been positive, and Yorkshire Water recently announced that it is bringing forward sewage infrastructure investment in Scarborough and surrounding area, an area our engagement has highlighted as in need. Northumbrian Water has responded to engagement with further disclosure on our priorities, which is currently being assessed. Engagement with Yorkshire Water and Northumbrian Water will continue.

Additionally, Border to Coast has joined the IIGCC Net Zero Engagement Initiative (NZEI) and is co-leading engagement with easyJet alongside shareholders Ninety-One, Phoenix Group, and Strathclyde Pension Fund.

The IIGCC engagement programme is seeking comprehensive Net Zero Transition Plans from 107 target companies, including a net zero commitment, aligned GHG reduction targets, emissions performance disclosure, and credible decarbonisation strategy.

Following assessment of easyJet's transition plans and response to the IIGCC NZEI questionnaire, a meeting was held in November to discuss its emission reduction targets and decarbonisation strategy.

The Company response was satisfactory, with a well-below 2 degrees aligned Science Based Targets initiative (SBTi) target and comprehensive transition plan. Further disclosure has been requested on the feedstock and sustainability of Sustainable Aviation Fuels, and on the contributions of transition measures to meeting its targets. Engagement with easyJet is continuing.

Local Authority Pension Fund Forum ("LAPFF") are another relevant organisation that SYPA are members of where LAPFF carry out activity and engagement with invested companies. A detailed report of the work undertaken by LAPFF in the quarter is available here. The key issues worked on during the quarter include:

- LAPFF has continued to engage on climate change through both policy and engagement channels. LAPFF coordinated an investor letter to 35 FTSE companies in high emitting sectors requesting a shareholder vote on the company's transition plans. LAPFF received a substantive response with some companies outlining their consideration of such a vote at next year's AGMs. Some companies outlined previous votes and their intention to continue to hold similar votes in the future. Others stated either that they did not plan to hold such a vote and engaged shareholders in the past or held a past vote and did not intent to do so again.

- After restarting its 2020 engagement with insurance companies, LAPFF met with AIA, AXA, Legal & General, Lloyds Banking Group, and Ping An to discuss each company's progress on assessing its impact on climate change and integrating climate considerations into corporate strategy and operations. In LAPFF's view, although there has been some progress in understanding climate related risks within their investment businesses, there is still greater consideration that could be applied to the role of insurance companies in mitigating climate change. As such, LAPFF will continue engagement.

- Miners Glencore and Grupo Mexico were companies of focus this last quarter. LAPFF generally has at least an annual meeting with the Glencore Chair. This meeting was its second with Chair Kalidas Madhavpeddi. Although LAPFF had requested a meeting with CEO Gary Nagle to discuss both climate and human rights performance at Glencore, Mr. Madhavpeddi was accommodating and helpful. LAPFF asked about the company's engagement with affected communities, but Mr. Madhavpeddi did not share much on this front. LAPFF subsequently held a seminar for investors with communities from Colombia and Peru who are affected by Glencore's Cerrejon and Antapaccay projects, respectively. It has also been in touch with IndustriALL representatives who worked with investors last year to bring a climate-related resolution to Glencore's AGM. LAPFF's view from speaking to these stakeholders is that in the coming year, Glencore is likely to be the target of a concerted union and community campaign because of its human rights and environmental practices. Therefore, LAPFF has reached out to the company for a follow up meeting to discuss these stakeholder concerns and to push the company to build and disclose stronger stakeholder engagement mechanisms and climate practices.

- LAPFF continued its engagement with Vale and Anglo American through the PRI Advance human rights initiative, including through bringing investors in other PRI Advance groups into stakeholder engagement meetings on Glencore, BHP, and Rio Tinto. These initiatives are moving quite slowly, in part in LAPFF's view, because investors are generally less aware of and less attuned to human rights considerations than they are corporate governance and environmental issues. Therefore, they are still considering how best to engage companies on human rights, which tend to deal with 'soft' issues such as illegal discrimination and freedom of association rather than 'hard' issues like clear financial costs.

LAPFF has also continued to respond to wider developments and consultations, for example the UN Working Group on Business and Human Rights and will continue to respond to consultation opportunities where it believes it can contribute helpfully with the aim helping investors to understand the link between human rights and financial materiality.

# Portfolio ESG Performance

## Equity Portfolios

Each of the equity portfolios is monitored by Border to Coast in terms of its overall ESG performance with data reported quarterly. This section of the report provides a summary of performance and of changes over time. The full reports are available for Authority members in the on-line reading room, but this summary provides a high-level indication of the position of each of the listed funds.

### Overseas Developed

- Weighted ESG Score 7.3
- 54.2% of portfolio ESG leaders v 52.0% in the benchmark.
- 1.5% of portfolio ESG laggards v 2.4% in the benchmark.
- 4.4% of portfolio not covered all of which are investment trusts etc higher than benchmark
- Lowest rated 5 companies 1.4% of portfolio
- Emissions below or inline with benchmark on all metrics.
- Weight of fossil fuel holdings greater than benchmark
- All 5 top emitters rated on the Transition Pathway with 4 TPI scoring of 4
- 4 of 5 top emitters engaged through Climate Action 100+

### United Kingdom

- Weighted ESG Score 7.8
- 73.8% of portfolio ESG leaders v 70.8% in the benchmark
- 0% of portfolio ESG laggards
- 7.0% of portfolio not covered, mainly investment trusts marginally more than benchmark
- Lowest rated 5 companies 11.1% of portfolio, all MSCI rated BBB or above
- Financed emissions and carbon intensity metrics are below or inline with the benchmark
- Lower weight of fossil fuel holdings than in benchmark.
- 4 of 5 top emitters rated 4 or 4* (highest ratings) on the Transition Pathway, all engaged through Climate Action 100+

### Emerging Markets

- Weighted ESG score 6.0
- 26.1% of portfolio ESG leaders v 23.5% in the benchmark
- 9.7% of portfolio ESG laggards v 13.4% in the benchmark
- 4.1% of portfolio not covered largely investment trusts etc
- Lowest rated 5 companies 5.3% of portfolio.
- Emissions materially below benchmark on all metrics
- Lower weight of oil and gas holdings than in benchmark.
- 2 of the top 5 emitters engaged with the Transition Pathway with average scores of 3
- 2 of top 5 emitters engaged through Climate Action 100+

### Listed Alternatives

- Weighted ESG score 7.3
- 38.2% of portfolio ESG leaders v 44.4% in the benchmark
- 0.4% of portfolio ESG laggards v 2.8% in the benchmark
- 39.8% of portfolio not covered largely investment trusts etc
- Lowest rated 5 companies 10.2% of portfolio.
- Emissions below benchmark on 2 of 3 measures
- Materially lower weight of fossil fuel holdings than in benchmark.
- 4 of the top 5 emitters engaged with the Transition Pathway with two scoring TPI level 4 and further scores of 3 and 2
- 2 of 5 top emitters engaged through Climate Action 100+

Overall, this shows a broadly positive picture, with all funds continuing to score better than, or inline with, the benchmark overall. However, the overall trajectory of improvements within these funds has slowed with progress largely flat, or reflective of changes in proportion to the benchmark, during the quarter.

Each quarter Border to Coast's reporting on carbon emissions features particular stocks and their plans for decarbonisation. To increase the level of transparency on the engagement undertaken with companies and the assessment of their future decarbonisation plans, case studies for each listed fund are included below.

## Overseas Developed Fund

Financed emissions decreased in the quarter. This was largely driven by strong performance in some of the higher emitting companies such as RWE, Holcim and ArcelorMittal.

**Featured Stock: RWE**

In November 2023, RWE outlined a €55bn investment plan to 2030 to expand its green portfolio to more than 65 gigawatts (GW) by 2030, adding net capacity of >30GW between 2024-30. RWE's goal is to be carbon neutral by 2040 and to achieve this it is increasing the pace of its transformation and aiming to reduce its emissions in line with the 1.5ºC reduction path across all corporate activities and all greenhouse gases. This includes the construction of renewable energy plants based on offshore and onshore wind power, solar energy, and battery storage as well as investments in hydrogen-ready gas-fired power plants. RWE has a goal to phase out the use of coal as an energy source by 2030 and is decommissioning coal power plants as soon as their utilisation is no longer required. To achieve the goal of net zero by 2040, the decarbonisation of fossil-fuelled power plants is another key element. The Company is converting its Dutch power plants to run on biomass and is currently developing carbon capture and storage projects in the UK and the Netherlands.

The investment thesis for owning RWE remains; it has one of the strongest balance sheets in the sector and will be looking at the renewable space to grow its earnings. It is at a valuation discount to its peers, which is mainly due to coal-fired power generation exposure. As the exposure to coal/lignite reduces, RWE should rerate to be in line with its peers.

## UK Listed Equity Fund

The weighted ESG score remained consistent over the quarter and remains in-line with the benchmark. This Fund holds a higher weighting of companies considered to be 'Leaders'. Furthermore, the Fund does not hold any companies considered to be 'Laggards' (CCC or B rated companies).

**Featured Stock: BP**

BP is a multinational integrated oil and gas company, operating through three key segments: Gas and Low Carbon Energy, Oil Production and Operations, and Customers and Products. Higher energy prices have seen BP deliver strong cashflows and have provided a strong basis for it to meet its target of allocating 50% of its capital expenditure to the strategic 'energy transition growth engines' by 2030. Recently, BP has made some substantial changes to its short-term emissions targets and the mix of its investments. The company has reduced its ambition with its short-term emissions target for 2025 being reset to a 10-15% reduction (from 20%), and the 2030 target to a 20-30% reduction (from 35- 40%). A 40% reduction in oil and gas production by 2030 is now set at a 25% reduction.

Furthermore, its investment mix has adapted in line with the market as investment in hydrogen has been delayed. Despite these changes, BP continues to target net zero scope 1,2 and 3 emissions by 2050. BP indicates these changes reflect stronger shorter term energy prices and the desire to remain flexible and pragmatic given heightened geopolitical uncertainty.

The unexpected departure of the CEO in September saw short-term management passed to the FD (Murray Auchincloss) whilst a replacement was found. Recent engagement with the Chairman indicated the board are the custodians of the low carbon strategy and that the new appointee will not be able to reverse the current plans. The Company has since announced that Murray Auchincloss has been appointed as the new CEO. Border to Coast continue to actively engage with BP seeking more disclosure around targets and capex plans. Recent engagement with the Chairman indicated the board are the custodians of the low carbon strategy and that the new appointee will not be able to reverse their current commitments.

## Emerging Markets Equity Fund

During the quarter carbon emissions increased in absolute terms but remains significantly below that of the benchmark. This increase was due to Grasim restating their reported emissions for the financial year 2022. In previous years annual reports, Grasim had not included the emissions of UltraTech Cement which is a subsidiary of Grasim Industries. This accounts for the Funds' increased emissions and Grasim now accounts for 45% of emissions. Grasim is this quarter's Feature Stock below.

**Featured Stock: Grasim**

Grasim is an Indian conglomerate operating in three core sectors: cement, viscose staple fibre (VSF), and financial services. Grasim's cement subsidiary, UltraTech, is India's largest cement manufacturer by volume and benefits from rising spend on house building. Its VSF subsidiary is the largest supplier of fibres for viscose yarn in India and is primarily driven by domestic apparel spending. India's cement consumption is growing slightly faster than GDP growth, while use of VSF is also rising. Both businesses lead the competition in scale and profitability. Grasim provides the portfolio with exposure to the India growth story from the perspective of both basic infrastructure and consumption.

Cement production is the greatest source of carbon emissions for Grasim (>90%) as the production of clinker for cement is very energy intensive. Grasim aims to achieve Net Zero overall by 2050. Within cement specifically, Grasim has committed to reduce Scope 1 and Scope 2 emissions (the most material emissions for the cement industry) by 30% by FY30 (versus FY17). This will be achieved by increasing the share of renewable power to 25% by FY25 and investing in waste heat recovery systems. In the VSF business, Grasim has committed to reduce GHG emission intensity by 50% by FY30 and achieve Net Zero Emissions by FY40. The decarbonisation strategy targets new technologies, operational efficiency gains, and new low carbon product offerings. While Grasim is a large carbon producer, cement production is nevertheless vital in pursuing basic development goals, and thus a fundamental ingredient in delivering affordable and safe housing, communications infrastructure, clean water and sanitation. It is therefore an important industry to support in its transition towards net zero.

## Sterling Investment Grade Credit Fund

Similar information is now available for the Investment Grade Credit portfolio as is available for the equity portfolios. It is important to note that while the availability and quality of ESG data has been improving in recent years, there can still be material gaps across the fixed income market. This is particularly prevalent where a debt-issuing entity does not also issue publicly listed equity, which, in most cases, the fixed income issuer maps to. The highlights from this report are set out below:

Weighted ESG score 7.2 which is lower than benchmark of 7.5

40.9% of portfolio ESG leaders compared to 56.8% in the benchmark

0.6% of portfolio ESG laggards compared to 1.0% In the benchmark

23.8% of portfolio not covered compared to 8.7% in the benchmark

The 5 lowest rated issuers represent 1.4% of the portfolio

Emissions above benchmark on two out of three carbon emission and intensity metrics.

Materially below benchmark weight of companies with fossil fuel reserves.

4 of top 5 emitters being engaged by Climate Action 100+ and all four rated 4 on the Transition Pathway

The ESG score and MSCI ESG rating remained stable over the quarter remaining below the benchmark on ESG scoring driven primarily by an overweight position in UK Government Bonds (rated A) of approximately 5%.

## Commercial Property Portfolio

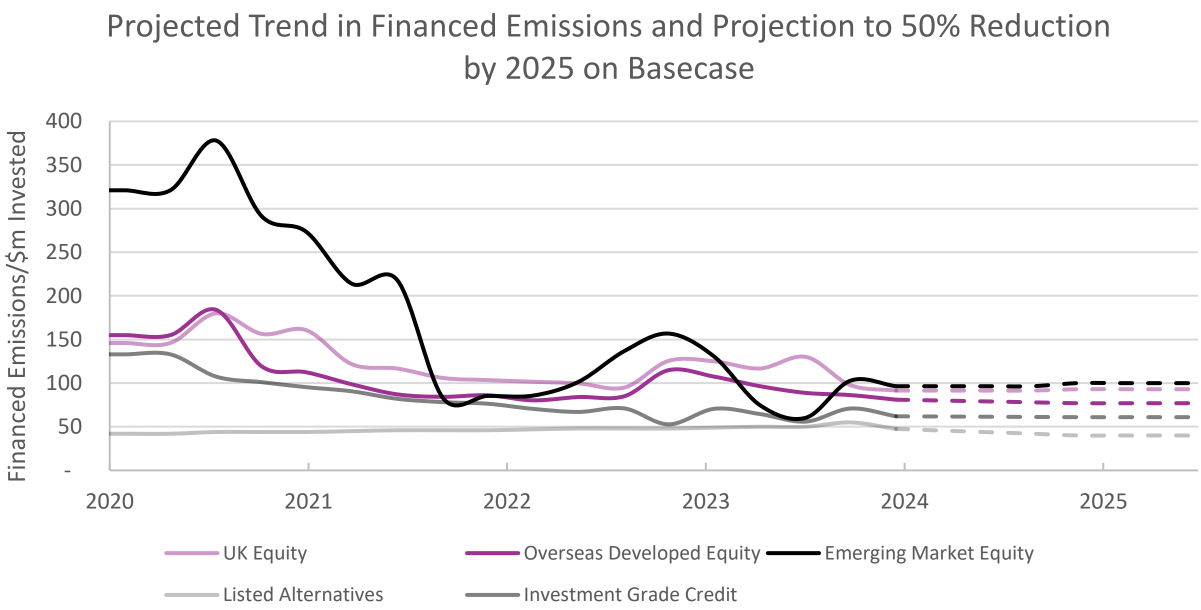
As reported in the last quarterly update the overall ESG performance of the commercial property portfolio as measured by the GRESB (Global Real Estate Sustainability Benchmark) has improved over the last year. The portfolio achieved a 3 star score with an increase in the percentage score from 74% to 78%, compared to a peer average score of 73%. In comparative terms the portfolio's ranking, over the year, moved up to 22 out of 100 from 22 of 80, reflecting the increased focus on these issues by abrdn. Like-for-like total emissions (scope 1, 2 & 3) also showed positive have fallen year-on-year by 11%.

In terms of the more routinely measured metrics, the proportion of the portfolio with EPC ratings A-C remains at 78%.

Abrdn remain concentrated on retaining the best performing assets, and divesting from the worst performing, in both financial and sustainability terms. As a result, the proportion of the portfolio AUM with sustainability green building certification has been on an upward trajectory year-on-year from 10% to 37%. As noted in previous reports, given the costs of in use certification, this measure is expected to increase as all new properties have been rated either BREEAM very good or excellent.

# Progress to Net Zero

This section of the report considers progress towards Net Zero using the emissions data provided on a quarterly basis by Border to Coast. The graph below shows the trend for what is now termed financed emissions (i.e. absolute carbon emissions) which is the main indicator for which targets have to be set. This now includes emissions data for the Listed Alternatives fund therefore covers five publicly traded funds held with Border to Coast for which carbon emissions data is available.




The above graph shows in the solid lines the actual financed emissions of the listed funds held over time. The dashed lines indicate the linear path required to meet the 2025 interim target of reducing financed emissions by 50% on a March 2019 base case. The UK Equity and Emerging Markets funds are both currently in line with their emission reduction targets. The Overseas Equity Fund and Investment Grade Corporate Credit Fund both have small reductions required, on a % change basis, to meet their interim targets with the Listed Alternatives Fund having the largest % reduction required. It should be noted that some volatility in financed emissions quarter on quarter is to be expected however the financed emissions trend has been directionally reducing, albeit at a slowing rate over recent quarters.

## Overseas Developed Markets Equity

Financed emissions decreased during the quarter and remain below the benchmark. This was largely driven by strong performance in some of the higher emitting companies such as RWE, Holcim and ArcelorMittal.

## UK Equity

The Fund remains slightly above the benchmark for Weighted Average Carbon Intensity (“WACI"). However, both WACI and financed emissions decreased quarter on quarter. This was largely due to the exit of CRH following a switch of the main listing to the US and reduced weightings in Shell and BP.

## Emerging Markets Equity

The Fund remains significantly below the benchmark for all three measures of carbon emissions and carbon intensity. However, as mentioned previously, the Fund saw a significant in carbon emissions and WACI due to the restating of reported emissions from one of the companies held. This highlights one of the reasons for potential volatility in reported emissions.

## Listed Alternatives

The Listed Alternatives portfolio has seen a continued increase in the availability of Carbon Emissions Data as the proportion of assets held through Investment Trusts declined. During the quarter, the overall weighted average carbon intensity (WACI) and financed emissions of the fund decreased following a reduction in portfolio weight of Cheniere Energy and NextEra Energy.

## Investment Grade Credit

As mentioned previously, the Investment Grade Credit portfolio has seen a significant improvement in data availability. The overall position being broadly in line with the benchmark on all emissions metrics and with no one holding dominating portfolio emissions. Financed emissions and WACI decreased in the quarter largely driven by an increase in market cap of the Funds' largest emitters as an increase in market cap results in lower emissions per £M invested. This supports the revised position proposed in the Authority's annual policy review of using debt denial as a means of encouraging companies to actively decarbonise their operations through the use of science-based targets.

## Coverage

The proportion of companies covered is an important metric when assessing the progress made to Net Zero. Without a high level of coverage, the emissions reduction picture will not be complete or accurate. The table below outlines the level of coverage in the funds held with Border to Coast. Over time the % of the funds covered has increased, however the progress has largely plateaued towards the end of 2023. It should also be noted that there are further improvements to be made, particularly on the Sterling Investment Grade Credit Fund.

| Fund | ESG (%) | Carbon (%) |
|---|---|---|
| Overseas Developed Markets Equity | 95.6% | 95.6% |
| UK Listed Equity | 93.0% | 93.0% |
| Emerging Markets Equity | 95.9% | 98.6% |
| Listed Alternatives | 60.2% | 89.3% |
| Sterling Investment Grade Credit | 76.2% | 73.0% |

As has been made clear previously, the forecast reduction in emissions shown is dependent upon Border to Coast delivering the targets set out in their own Net Zero Strategy. This further depends on changes within the investment process as well as on the actions of individual companies. Officers continue to engage with Border to Coast to further understand both the nature of the changes being made to the investment process and their likely impact.

Beyond this the recently revised investment strategy, that is undergoing implementation, will result in changes to the mix of assets that reduce the level of emissions from the portfolio. However, this process is too early stage to determine the scale of any reduction. As has previously been reported there remains a very strong probability that the Net Zero Goal will be missed although there is a possibility, should all portfolios achieve the reductions targeted by fund managers, that a date earlier than 2050 could be achieved.

It should also be borne in mind that while there is, rightly, a significant focus on emissions there is no credit in the calculations for the emissions avoided by the significant investment by the Authority in renewable energy and other climate solutions and this is something that we will look to begin reporting on in future.

## Stakeholder Interaction

There was limited stakeholder interaction over the course of the quarter confined to the Director dealing with Responsible Investment related questions largely related to climate change submitted at the Annual Fund meeting.

# Collaborative Activity

This section focuses on the activity undertaken in the quarter through the various collaborations in which the Authority is either directly involved or indirectly involved through Border to Coast.

LAPFF's most recent business meeting considered a draft workplan for the coming year which includes a focus on the following areas, each of which covers a range of specific engagement themes:

- Climate and Strategic Resilience, Environmental Protection and a Fair and Just Transition;
- Natural Resources and Water Stewardship;
- Human Rights and Employment Practices;
- Promoting Good Governance; and
- Reliable Accounts, Capital Market Regulatory Reform.

During the quarter, Climate Action 100+, the world's largest investor engagement initiative on climate change, published its list of produced its list of 10 companies to be assessed against the Net Zero Standard for Oil & Gas (NZS O&G).

The NZS O&G, published by IIGCC in April 2023, provides a comprehensive sector-specific assessment framework for investors to assess oil and gas companies' disclosures and the alignment of their transition plans with a 1.5oC climate scenario. The NZS O&G was developed to help inform investors' corporate engagement priorities and escalation strategies, whilst helping them better understand the transition risk in their portfolios.

10 companies that will be assessed publicly against the NZS O&G in early 2024 include: Exxon Mobil, Shell plc, Chevron, TotalEnergies SE, ConocoPhillips, BP, Occidental Petroleum, Eni S.p.A, Repsol S.A. and Suncor Energy.

# Policy Development

This section of the report highlights the key pieces of policy related activity which have taken place that will impact SYPA in the future.

**UN Climate Change Conference (COP28)**

COP28 took place in Dubai, United Arab Emirates, in December, with the aim of making progress in several areas:

- hammering out the details of the loss and damage finance facility to help vulnerable communities deal with immediate climate impacts;
- driving towards a global goal on finance that would help fund developing countries' efforts in addressing climate change;
- accelerating both an energy and a just transition;
- closing the massive emissions gap, just to name a few.

There were five key developments that came of COP28:

1. A final agreement made on global "transition away from fossil fuels." This is the first time the shift away from fossil fuels has been explicitly included in a final agreement at a COP. Whilst the final agreement does not commit to the phase-out of fossil fuels, it does show progress, albeit slowly.
2. An Oil and Gas Decarbonisation Charter was launched to accelerate climate action. Fifty oil and gas companies committed to decarbonising their direct emissions and taking significant steps towards reducing methane emissions. This is the first time many National Oil Companies (NOCs) have adopted Net Zero 2050 targets. Signatory companies represent over 40 percent of global oil production, with NOCs representing over 60 percent of signatories – the largest-ever number of NOCs to commit to a decarbonisation initiative.
3. Over 123 countries committed to tripling renewable energy generation capacity to at least 11,000 GW by 2030 and double the global average annual rate of energy efficiency improvements from around 2% to over 4% every year until 2030.
4. The Loss and Damage fund was operationalised and mobilised more than US$85 billion in new financial commitments to support the developing countries most vulnerable to negative climate change impacts.
5. Over 100 countries signed a declaration to focus on the impact of food and land-use changes on carbon emissions.