PUBLIC

MINUTES of a meeting of the **PENSIONS AND INVESTMENT COMMITTEE** held on 8 December 2021 at County Hall, Matlock.

PRESENT

Councillor D Wilson (in the Chair)

Derbyshire County Council

Councillors B Bingham, M Foster, D Muller (substitute Member), G Musson and P Smith

Derby City Council

Councillors L Care and M Carr

Also in attendance – M Fairman, D Kinley, A Nelson and N Smith (representing Derbyshire County Council)

K Gurney and N Read (representing the Pension Board)

Apologies for absence were received on behalf of Councillors R Ashton, N Atkin and M Yates (Derbyshire County Council) and Mr M Wilson (Derbyshire County Unison)

Declarations of Interest

There were no declarations of interest.

46/21 **MINUTES RESOLVED** that the minutes of the meeting held on 20 October 2021 be confirmed as a correct record and signed by the Chairman, subject to the following addition requested by Councillor Lucy Care with regard to Minute No.41/21:

"does the risk register correctly reflect the risk of not insuring that ESG has been adequately considered by the managers now that we are in a pool?"

47/21 **CLIMATE RISK REPORT** The Committee were presented with Derbyshire Pension Fund's Climate Risk Report dated November 2021, which had been prepared by LGPS Central Limited.

The Climate Risk Report had been structured around the Taskforce for Climate-related Financial Disclosures' (TCFD) four thematic areas of: governance; strategy; risk management; and metrics and targets. It included

the assessment of financially material climate-related risks within the Pension Fund's investment portfolio, highlighted climate-related opportunities and provided a base to set an annual Climate Stewardship Plan for the Pension Fund. This was the second Climate Risk Report that had been prepared by LGPSC, with the first report being presented to the Pensions and Investments Committee in March 2020.

Recognising that there was considerable uncertainty in the crystallisation pathway for climate risk, LGPSC believed that a suite of carbon risk metrics and climate scenario analysis currently provided the most appropriate method of analysing climate risk to support the development of a detailed strategy for integrating climate risk into investment decisions. LGPSC's contractual arrangements with the third-party provider of the carbon risk metrics data had prevented the publication of the full Climate Risk Report because the report contained some propriatary information in respect of individual investment manager and stock holding carbon metrics, which was subject to a non-disclosure clause. The full report would be presented in the restricted part of the meeting. However, a public version of the report, which provided largely the same degree of overall portfolio and asset class information but had omitted the propriatary information noted above, was attached as Appendix 2 to the report.

The Climate Risk Report noted that the Fund had made considerable progress in terms of its responsible investment and climate change practice in the last 16 months. In LGPSC's first Climate Risk Report, LGPSC had issued 12 governance recommendations, all with medium term horizons. The November 2021 LGPSC Climate Risk Report had noted that eleven of these recommendations had been completed.

The LGPSC Climate Risk Report included the climate scenario analysis included in LGPSC's first report, using data at 31 July 2019. The climate scenario analysis covered: (i) the actual asset allocation at 31 July 2019 (the reporting date used Fund's first Disclosures Report); (ii) the strategic asset allocation benchmark at 31 July 2019; and (iii) an alternative strategic asset allocation benchmark (the alternative allocation) which was a close proxy for the Fund's new final strategic asset allocation benchmark which would become effective on 1 January 2022. The key findings of the climate scenario analysis in relation to the alternative allocation were:

- A 2°C scenario would have a positive impact on the Fund's returns considering both a timeline to 2030 and to 2050. This positive impact was boosted by the 29% allocation to Global Sustainable Equities in the alternative allocation.
- A 3°C scenario (which was in line with the current greenhouse gas trajectory) had a mildly positive impact on the Fund's annual returns.
- A 4°C scenario would reduce the Fund's annual returns, with most asset classes expected to experience negative returns.

The scenario analysis produced more positive relative returns for the alternative allocation under a 2°C and a 3°C scenario than the actual allocation, and the benchmark allocation, at 31 July 2019. Under a 4°C scenario, returns across all three scenarios were negatively impacted. The scenario analysis supported the Fund's ongoing transition to the new final strategic asset allocation benchmark from 1 January 2022.

Climate stress testing analysis suggested that should a 2°C scenario suddenly be priced in by the market, the Fund could benefit in terms of financial returns, whereas the opposite was true should a 4°C scenario be priced in by the market.

The LGPSC Climate Risk Reports highlighted that the poor availability of data in respect of asset classes other than listed equities and investment grade bonds had prevented the preparation of carbon metrics in respect of these asset classes (e.g. private equity; infrastructure; fixed income; private debt & diversified multi-asset credit; property, etc). The IIMT had planned to carry-out a review of these asset classes in the next six to twelve months to better understand the climate related risks and opportunities of these investments.

The LGPSC Climate Risk Report set out a review of the progress made in respect of the Fund's inaugural Climate Stewardship Plan. Stewardship activities remained an important aspect of the Fund's approach to managing climate risk. The Fund expected all investee companies to manage material risks, including climate change, and the Fund believed that climate risk management could be meaningfully improved through focussed stewardship activities by investors. Existing fund managers were monitored on a regular basis to review the integration of climate risks into the portfolio management, and to understand their engagement activities. The IIMT noted that eight of the nine companies included in the Fund's current Climate Stewardship Plan were covered by the Transition Pathway Initiative (TPI). The TPI framework evaluated companies based on their climate risk management quality and carbon performance in terms of alignment with the Paris Agreement.

Since the preparation of the Fund's Climate Stewardship Plan, the Fund had sold several investments which were included in the inaugural Climate Stewardship Plan. Furthermore, the transition to the Fund's new final strategic asset allocation benchmark by 1 January 2022 would see further sales from investments included in the existing Climate Stewardship Plan. As a result, the Fund, in collaboration with LGPSC, had developed a forward Climate Stewardship Plan which would include targeted engagement with investee companies of particular significance to the Fund's portfolio following the transition to the Fund's new final strategic asset allocation benchmark. The forward Climate Stewardship Plan included: BP; CRH; Gazprom PA; Rio Tinto; Shell; and Taiwan Semiconductor Manufacturing.

Carbon risk metrics analysis on the Fund's listed equities and investment grade bond portfolios considered: portfolio carbon footprint (weighted average carbon intensity); fossil fuel exposure; thermal coal exposure; and clean technology (portfolio weight in companies whose products and services include clean technology). The key findings of the carbon risk metrics analysis were highlighted.

The Fund had developed a standalone Climate Strategy which was approved by Committee in November 2020. The Climate Strategy set out the Fund's approach to addressing the risks and opportunities related to climate change, including a statement that the Fund supported the ambitions of the Paris Agreement, and aimed to achieve a portfolio of assets with net zero carbon emissions by 2050. The Climate Strategy included two targets: (i) reduce the carbon footprint (Scope 1 & 2) of the Fund's listed equity portfolio by at least 30% relative to the weighted benchmark in 2020 by the end of 2025; and (ii) invest at least 30% of the Fund portfolio in low carbon and sustainable investments by the end of 2025. The progress to date in respect of the two targets was provided in detail.

The Fund had already achieved the first target and expected to make further progress on this measure and significant progress in respect of the second target in 2021-22 as part of the ongoing move to the new final strategic asset allocation benchmark. The targets would be reviewed in 2023, and at least every three years thereafter, and were expected to increase in line with the stated ambition of achieving a portfolio of assets with net zero carbon emissions by 2050. The impact of the significant ongoing transitions on performance and risk within the investment portfolio would be closely monitored and assessed.

In collaboration with LGPSC, the Fund had prepared a second Climate-related Disclosures Report for publication, which included the high level results of the climate scenario analysis, carbon risk metrics analysis and progress against the Fund's Climate Strategy targets. The Disclosures Report also included information on the Fund's governance of climate risk and on the Fund's climate-related stewardship activities. Publication of a Climate-related Disclosures Report represented best practice.

RESOLVED that the Committee notes the LGPSC Climate Risk Report attached as Appendix 2.

48/21 **CLIMATE-RELATED DISCLOSURES** The Disclosures Report, attached as Appendix 2 to the report, had been aligned with the recommendations of the TCFD. It described the way in which climate-related risks were currently managed by the Fund and included information on the Fund's governance of climate risk and on the climate-related stewardship

activities of the Pension Fund which were an important part of the Fund's approach to managing climate risk. It also included the results of recent climate scenario analysis and carbon risk metrics analysis undertaken on the Fund's assets as part of LGPSC's preparation of an annual Climate Risk Report.

Councillor Foster wished to thank the officers for the work they had undertaken in line with the Fund's Climate Strategy and acknowledged the significant progress that had been made, particularly in relation to the benchmarks.

RESOLVED to note the Climate-Related Disclosures Report attached at Appendix 2.

49/21 **INVESTMENT REPORT** Mr Anthony Fletcher, the external adviser from MJHudson Allenbridge Investment Advisers Limited, attended the meeting and presented his report to the Committee. The report incorporated Mr Fletcher's view on the global economic position, factual information for global market returns, the performance of the Derbyshire Pension Fund, and his latest recommendations on investment strategy and asset allocation. Mr Fletcher also provided an update and a general overview of the current market situation.

The Fund's latest asset allocation as at 31 October 2021 and the recommendations of the Director of Finance & ICT and Mr Fletcher, in relation to the Fund's new final strategic asset allocation benchmark, which will come into effect on 1 January 2022, were set out in the report. The value of the Fund's investment assets had increased by £159m between 31 July 2021 and 31 October 2021 to £6.194bn

The recommendations of the Director of Finance & ICT adjusted to reflect the impact of future investment commitments, were highlighted. These commitments (existing plus any new commitments recommended in this report) related to Private Equity, Multi-Asset Credit, Property and Infrastructure and currently totalled around £365m. Whilst the timing of drawdowns would be lumpy and difficult to predict, the In-house Investment Management Team (IIMT) believed that these were likely to occur over the next 18 to 36 months.

The Fund's latest LGPSC Climate Risk Report had indicated that the Fund's Total Quoted Equities portfolio at 31 March 2021 was around 27% less carbon intensive than the benchmark, and 37% lower than the 2020 Benchmark. The IIMT expected that the transition to the new final benchmark would lead to a 'step-up' in the carbon footprint reduction of the Fund's Total Quoted Equities portfolio relative to the current benchmark and the 2020 Benchmark, and would update the Committee following the completion of the transition, including an internal IIMT assessment of the carbon reduction relative to the current benchmark and the 2020 Benchmark.

The Chairman thanked Mr Fletcher for his attendance and informative presentation.

RESOLVED that the Committee (1) note the report of the independent external advisor, Mr Fletcher;

(2) note the asset allocations, total assets and long-term performance analysis set out in the report of the Director of Finance & ICT;

(3) approves the IIMT recommendations outlined in the report of the Director of Finance & ICT; and

(4) approves the benchmarking of any allocation to the LGPSC Climate Factor Fund to the product specific benchmark.

50/21 **STEWARDSHIP REPORT** The Committee was provided with an overview of the stewardship activity carried out by Derbyshire Pension Fund's (the Fund) external investment managers in the quarter ended 30 September 2021.

This report attached the following two reports to ensure that the Committee was aware of the engagement activity being carried out by Legal & General Investment Management (LGIM) and by LGPS Central Limited (the Fund's pooling company) (LGPSC):

- Q3 2021 LGIM ESG Impact Report (Appendix 2 to the report)
- Q2 2021/22 LGPSC Quarterly Stewardship Update (Appendix 3 to the report).

These two reports provided an overview of the investment managers' current key stewardship themes and voting and engagement activity over the last quarter. They demonstrated the importance of engaging regularly on ESG matters.

RESOLVED that the Committee notes the stewardship activity of LGIM and LGPSC.

51/21 **EXCLUSION OF THE PUBLIC** **RESOLVED** to move that under Section 100(a)(4) of the Local Government Act 1972 the public be excluded from the meeting for the following item of business on the grounds that in view of the nature of the business, that if members of the public were present exempt information as defined in Paragraph 3 of Part 1 of Schedule 12A of the Local Government Act 1972 would be disclosed to them and the public interest in maintaining the exemption outweighs the public interest in disclosing the information.

SUMMARY OF PROCEEDINGS CONDUCTED AFTER THE PUBLIC HAD BEEN EXCLUDED FROM THE MEETING

1. To receive declarations of interest (if any)

2. To confirm the exempt minutes of the meeting held on 20 October 2021 (contains exempt information)

3. To consider the exempt report of the Director of Finance & ICT on Climate Risk (contains information relating to the financial or business affairs of any particular person (including the Authority holding that information)).

The meeting ended at 12.55pm