We had 21 questions submitted to the Pension Fund for answer at the AGM. Many of these were on similar themes. Given the volume of questions, for the meeting some of these have been grouped and answered together. All questions submitted will be published on the Pension Fund website with individual responses.

The questions and responses during the meeting were as follows:-

Question from Nottingham City Council, one of the biggest employers in the Fund.

"Nottingham City Council has declared a climate and ecological emergency and is committed to being carbon neutral by 2028.

On behalf of the many employees of the City Council, partner organisations and citizens of Nottingham who are concerned about the impact of their Pension Fund on climate change, and, given the decreasing financial performance of fossil fuel related investments, I would like to ask that the Pension Fund agree to consult with its members on a divestment strategy and timeline before the next AGM, in order to ensure the long term sustainability of the Fund and to play it's part in the prevention of catastrophic climate change."

Councillor Sally Longford,

There were six similar questions.

Response
The Pension Fund shares the concerns of Nottingham City Council about climate change. Climate action failure is the stand-out, long-term risk the world faces in likelihood and impact according to the 2020 Global Risks Report from the World Economic Forum.

How companies manage climate-related transition and physical risks and opportunities is highly likely to affect long-term profits and company returns. Policy makers response equally so. We therefore actively debate how the Fund alongside other like-minded investors can best encourage a broad transition towards a low-carbon economy.

We have discussed divestment at length particularly over the past few years, most recently at a Working Party in 2020 to discuss the Climate Risk Analysis report procured from LGPS Central. From these and previous discussions we have concluded that divestment is a less effective strategy than engagement at delivering beneficial outcomes as well as being less consistent with our fiduciary duty to pension fund members. Engagement remains a more powerful and more effective tool that we use both at corporate, industry and policy levels to influence not just individual company behaviour but the "rules of the game". By the same token that we ask companies to align their businesses with the Paris Agreement, we ask policy makers to take policy action that will facilitate the transition to a low-carbon economy. As an example of the latter our pool company LGPS Central has co-signed, on our behalf, letters to EU and UK leaders asking for a green recovery from the health pandemic.

Importantly, focussing on the exclusion of Oil and Gas companies ignores the impact other companies have on climate change. Almost every business in the world to some extent depends on the use of fossil fuels and will do so for some time to come. Selling shares in oil & gas companies will not make real world changes to greenhouse gas emissions, indeed it could be counterproductive. It requires systemic change across many industries and governments to make the impact required to limit global warming. We believe there needs to be corporate change across a wide range of sectors, which in our view is more likely with an engagement strategy. Many companies seek out investors for their views on decarbonisation plans and strategies.

Our Investment Strategy Statement therefore continues to state that the Pension Fund believes that a strategy of engagement (i.e. working from the inside to influence company behaviours) rather than exclusion is more compatible with fiduciary duty and will lead to a better outcome in terms of climate change. We note that most other LGPS funds and major pension funds take this view. If Nottinghamshire Pension Fund were to sell its fossil fuel holdings to another less engaged investor the pressure on those companies would reduce with potentially a negative impact on carbon emissions and speed of transition. The Fund actively influences companies by engagement through our investment managers and LAPFF, and by exercising our voting rights.

Our pooling company, LGPS Central is an active member of a collaborative engagement called ClimateAction 100+. ClimateAction 100+ engages 161 companies across the globe that are responsible for 80% of industrial carbon emissions globally. The initiative builds on a simple but powerful logic: If you engage and influence the highest emitters, you influence whole sectors, markets and the global economy. ClimateAction 100+ is currently being ramped up through a Benchmarking project. All companies are asked to set an explicit target of net-zero emissions by 2050 – and to provide verifiable evidence that this will be achieved in the short, medium and long term. This introduces an element of “no-where to hide” and investors will be able to assess companies’ progress relative to sector-peers and across the board.

Question from the Nottingham City Council Energy Projects Team which also asks about divestment plans and consulting members. This includes the comment:-

“Energy Services understand that the Nottinghamshire Pension Fund has no investments in sustainable, low carbon or renewable energy equity funds.”

Response

The implication that the Fund has no investment in renewable energy or sustainable investments is not true. Over the past fifteen years, the Fund has made investments in a range of listed investment trusts and private funds whose model is partially or wholly based on sustainable investments. Examples are The Renewable Infrastructure Group, Impax Environmental Markets Trust on the listed side and Green Investment Offshore Wind Bank on the private side. In addition our two main active managers have carbon footprints of 58% and 31% respectively of their benchmarks, showing that they also pay attention to investing sustainably. We expect, subject to due diligence, to make a significant allocation to a sustainable equity mandate when LGPS Central has one available.

We gave our reasons in the previous response why one of our investment beliefs stated in our Investment Strategy Statement is that engagement is a more appropriate response than divestment and more likely to lead to a better outcome in terms of climate change. We emphasise again that in doing this we are aligned with the great majority of pension funds around the world who have a fiduciary duty to members. We discuss this issue at Committee on a regular basis, but at the moment there are no plans to divest from fossil fuels.

We understand the request to consult members or employers. If the Fund were planning to make an investment or divestment for non-financial reasons, it would have to have good reasons for believing that Fund members shared its belief. As the Fund has not invested or divested for non-financial reasons, there is no requirement at this stage to hold a consultation, which carries a significant cost. We note also that the Fund is not bound by the results of a consultation, though it should take them into consideration.

To summarise, we share the questioners' ambitions that the Pension Fund should invest in a way which is consistent with mitigating climate change and we are actively pursuing that strategy. However we do not share their view that divesting from fossil fuels is the most effective way of achieving that.

Question from Mr Patrick Hort.

"Since we are agreed that minimising average temperature rises is the goal, and since 1.5 degrees represents LESS warming than 2 degrees – but was NOT modelled – please can you tell me when a risk analysis of 1.5 degrees will be made available to the committee?"

There were three similar questions and we will respond to these together.

Response
The Pension Fund takes the financial risks of climate change very seriously and commissioned LGPS Central to deliver a Climate Risk Report which was taken to Committee in October. This analysis is supportive of the Fund's current investment strategy in three ways:-

- it demonstrates that minimised global warming is of benefit to the Pension Fund financially which means the Fund's financial interests are aligned with global environmental interests.
- It shows that the March 19 equity holdings were already below the market cap benchmark in terms of carbon footprint and weight of fossil fuel reserves, which indicates that the fund has been considering and managing climate risks.
- And it shows that as the Fund progresses towards the long term strategic asset allocation these positions will further improve.

LGPS Central uses an external service provider to conduct the Climate Scenario Analysis for the Climate Risk Reports. The service provider considers its 2˚C scenario to be aligned with the commitments of the Paris Agreement. The direction of travel is more important than the target in order to achieve a better outcome and we will continue to monitor carefully the development of climate change science, both in its modelling of different scenarios and the impact they might have on the world and ultimately the Fund's financial investments. At the time of the tendering process in 2019, data limitations meant the service provider had not yet developed a 1.5 ˚C scenario. It is likely that a 1.5˚C scenario will be developed by the service provider in due course as climate change integrated assessment models are updated to consider such a scenario. In future Climate Scenario analysis, LGPS Central will consider including a 1.5˚C scenario if data quality and models permit.

Question from Nicholas Pearson.

In October 2020 South Yorkshire Pension Authority voted to make its investment portfolio carbon neutral by 2030, and asked officers to produce a route map for this in 6 months. Given the environmental and financial risks of continuing with fossil fuel and other high carbon investments, and the massive investment opportunities in low carbon and renewable energy industries, can I ask when Nottinghamshire Pension Fund will be setting a similar target?

Response

We agree with the aspiration to reduce carbon emissions, and the Climate Risk Analysis we undertook in 2020 demonstrates that by showing that our active equity managers' carbon footprint is around half that of the benchmark. However, we have to balance this desire with all the other objectives which the Pension Fund is obliged to follow, most notably our fiduciary duty to members. We cannot allow one goal to dominate everything.

A core investment principle is to allocate in a considered way on the basis of robust data. If we use unreliable data, we may end up with a poor outcome. Carbon data scoring is still a young industry in the process of development, and, while the data provides useful insights there are a number of limitations. For example, little attention is paid to Scope 3 emissions (i.e. by the user), and much data provided by companies is neither audited or standardised. As climate-related data quality and availability improves, more reliance can be placed on that data.

We anticipate that as we implement our long term investment strategy we will reduce carbon emissions from the portfolio and will continue to review target setting as part of the overall climate-risk monitoring we will be undertaking on an ongoing basis. This will be done alongside continuing robust ESG integration into investment decisions by our investment managers and active and responsible stewardship (engagement and voting) of the assets we hold.

Question from Sue Mallender.

Fires in the Amazon and Pantanal region of Brazil - driven by illegal logging and cattle ranching - are increasing carbon emissions, damaging carbon sinks and destroying some of the most biodiverse areas in the world. Does the Pension Fund have an investment policy on preventing deforestation? What concrete actions is it taking to prevent deforestation associated with its investments?

Response

Through our pooling company LGPS Central, and our main equity managers Legal & General and Schroders we engage on the long-term investments risks inherent in deforestation both at policy and company levels. We recognise the crucial role that tropical forests play in tackling climate change, and protecting biodiversity, which again has an impact on economic development and the stability and well-functioning of capital markets.

As examples of a concrete action taken recently:-

LGPS Central is on the Advisory Committee of an Investors Policy Dialogue on Deforestation initiative known as IPDD which expects Brazilian authorities to halt and reverse deforestation while allowing investors access to data to monitor progress. This message has been communicated by investors over the last 4-5 months to the highest political levels, including to the Brazilian Vice President, the Governor of the Brazilian Central Bank and members of the Brazilian Congress. IPDD will be a two-year project that also aims to span other regions of the world that face deforestation risk.

For Legal and General tackling deforestation is recognised as a key element of achieving net-zero emissions and as such features significantly in the engagement their Investment Stewardship team undertakes across a wide range of companies. Deforestation features as part of Legal and General's Climate Impact Pledge as it is one of the issues they raise with companies in the relevant sectors and also with governments.

Legal & General have been engaging with some of the largest food companies on tackling deforestation since 2016. In addition, they are publicly assessing 125 food companies on the strength of their deforestation policies. The lack of a deforestation policy may result in a vote against at the companies' upcoming AGM.

Schroders recognise that deforestations, changes in land use, increasing agricultural intensity, over-population, climate change and pollution contribute to biodiversity loss and therefore take these factors into consideration in their ESG analysis of companies and engage with companies where they believe their practices are unsustainable.

Question from Ben Homfray

Did the training course on Climate Risk recently given to the Pension Fund Committee by LGPS Central include an explanation of the different impacts projected by the IPCC between heating of 1.5, 2.0, 3.0 and 4.0 degrees C? And if not, what actions are the Committee prepared to take to familiarise themselves with impacts projected by the United Nations Environment Programme and the IPCC?

Response
The answer to the question is, yes, the training course on Climate Risk recently given to the Pension Fund Committee by LGPS Central did include a section looking at estimates of the different impacts of varying degrees of temperature increase. Climate related scenario analysis is an immature discipline. It is difficult modelling the impacts and implications on a multi asset investment portfolio of an unprecedented global transition, which is in the process of being affected by governments around the world. It is the intention to repeat this analysis as the data and analytical tools evolve, and the Pension Fund Committee will continue to receive training from LGPS Central.

Question from Julia Bristow relating to an article which appeared in the Financial Times last year.

Response
The article in the Financial Times refers to estimates compiled by environmental campaign group Platform London. We have not been provided with the basis on which these estimates have been calculated so are unable to comment in detail on them. At a high level the article estimates performance over a relatively short time frame and it is not clear whether or not the article assesses performance on a total return basis, covering both share price and dividend payments.

Questions about investments in renewable energy and sustainable investments, particularly to replace fossil fuel investment.

Response
As part of portfolio diversification the Pension Fund has committed to an allocation of 8% to Infrastructure, equivalent to over £440m. Some of the investments already made are specifically in renewable energy funds, but the clean energy sector makes up a significant share of the infrastructure investment universe so this constitutes a major proportion of our more general infrastructure funds. It should be noted that many other infrastructure investments (for example in public transport infrastructure) contribute indirectly to reducing the demand for fossil fuels.

However most of these infrastructure investments are made through private equity funds. This places them outside the scope of the Climate Risk Analysis which focusses on equity investments as this is the only area where some reportable data exists. This is one of the limitations of this kind of analysis and is why it is not the only information considered by the Pension Fund in assessing its climate risk and its investment strategy.

The Pension Fund states in its Investment Strategy Statement an investment belief on the relevance of climate change for financial markets. In line with this belief, the Fund actively looks for investments which can be expected to benefit as a result of the long-term impacts of climate change. Opportunities may also arise from the response of policy makers and potential disruption in the market. The Fund will continue to look for investments which can be expected to benefit as a result of the current and long-term impacts of climate change and other global issues.

More specific plans for the next financial year include the evaluation of sustainable equity investments and the Fund is working with LGPS Central to develop a Sustainable fund. Over time the Pension Fund’s exposure to fossil fuels will reduce as a result of these diversification decisions as we implement our long term investment strategy.