

BATH AND NORTH EAST SOMERSET

AVON PENSION FUND COMMITTEE INVESTMENT PANEL

Friday, 17th September, 2021

Investment Panel: Shaun Stephenson-McGall (Chair), Paul Crossley, Chris Dando, John Finch, Pauline Gordon and Shirley Marsh-Hughes

Advisors: Steve Turner (Mercer)

Also in attendance: Tony Bartlett (Service Director - Financial Control and Pensions), Liz Woodyard (Group Manager for Funding, Investment & Risk), Nathan Rollinson (Investments Manager), David Cox (Brunel) and Chris Crozier (Brunel)

13 EMERGENCY EVACUATION PROCEDURE

The Chairman drew attention to the emergency evacuation procedure.

14 DECLARATIONS OF INTEREST

There were none.

15 APOLOGIES FOR ABSENCE AND SUBSTITUTIONS

There were none.

16 TO ANNOUNCE ANY URGENT BUSINESS AGREED BY THE CHAIR

There was none.

17 ITEMS FROM THE PUBLIC - TO RECEIVE DEPUTATIONS, STATEMENTS, PETITIONS OR QUESTIONS

There were none.

18 ITEMS FROM COUNCILLORS AND CO-OPTED AND ADDED MEMBERS

There were none.

19 MINUTES: 26TH FEBRUARY 2021 AND 28TH MAY 2021

The Panel confirmed the minutes of the two previous meetings as a true record and they were duly signed by the Chairman.

20 BRUNEL PRESENTATION

David Cox, Head of Listed Markets gave a presentation to the Panel. The full presentation will be added to the minutes as an online appendix.

There was a discussion about the new Paris aligned benchmarks that Brunel developed with FTSE Russell and how these new indices can meet client requirements. Specifically, the FTSE Russell Brunel Climate Transition Benchmark (CTB) and Paris aligned Benchmark (PAB) indices are designed to reflect the performance of a global and diversified basket of securities where weights are varied in order to achieve climate targets, including:

- i. Emissions – they have target reductions in both Carbon Reserves and Operational Emissions
- ii. Exclusions - Such as activity based exclusions – Oil, Gas, Coal and Electricity generators (PAB only) plus others such as Tobacco, Controversial Weapons, Conduct (e.g. UNGC)
- iii. Corporate Target Setting such as TPI Management Quality Score, TPI Carbon Performance

The Group Manager for Funding, Investment & Risk asked if the Passive / Index Fund was a manageable process and controlled.

David Cox replied that it was 100% rules based and followed the EU approach and had been enhanced by FTSE data. He added that they were not looking to take any undue risk.

John Finch asked if they had looked at historical information regarding the index.

David Cox replied that they had researched data dating back to 2011.

The Service Director for Financial Control and Pensions asked what would happen if companies stray from the PAB.

David Cox replied that the index would then need to be rebalanced.

David Cox explained how Brunel assesses ESG integration in the manager selection process. This includes evaluating the following: the internal ESG Culture, Climate Change Policy alignment, Thought leadership

Finally there was a discussion about Investing in China. Brunel's focus is on Human Rights in Supply Chains, Data Privacy, censorship & surveillance, Corporate Governance, Hong Kong and Taiwan, Climate Change, ADR/H-Share/A-Share

Steve Turner asked if it was harder to engage with companies linked to China.

David Cox replied that there was currently less transparency and that there was Chinese Government involvement in many companies to some degree.

The Chairman asked if companies will be given more time to declare / achieve their climate change targets.

David Cox replied that it was likely that different industries will provide a view point on what they can achieve but said that a net negative level needs to be achieved very soon after 2050. He added that passive indices would be a good judgement of their policies.

The Chairman thanked him for the presentation on behalf of the Panel.

21 EQUITY REVIEW

The Panel, having been satisfied that the public interest would be better served by not disclosing relevant information, **RESOLVED**, in accordance with the provisions of the Section 100(A)(4) of the Local Government Act 1972 that the public should be excluded from the meeting for this item of business, because of the likely disclosure of exempt information as defined in paragraph 3 of Part I of Schedule 12A of the Act as amended.

22 INVESTMENT PERFORMANCE

The Investments Manager introduced this report to the Panel. He informed them that the update on Brunel investment activity could be found at Appendix 3. He explained that as the transition of our assets to Brunel is drawing to a close the focus for the Panel was now on the ongoing management and performance of the Brunel portfolios. He added that a summary table is included which is designed to flag any concerns from a performance and/or RI perspective. He said that there no flags in place for this quarter.

He said that the Fund became a signatory to the '2021 Global Investor Statement to Governments on the Climate Crisis'. He added that this Statement, coordinated by the Investor Agenda and signed by over 450 investors representing \$41tn in assets, calls on Governments to strengthen their Nationally Defined Contributions to align with the transition to net-zero emissions by 2050 or sooner, commit to sector specific decarbonisation roadmaps supported by robust domestic policy, incentivise zero-emissions energy and transport infrastructure investment and support mandated climate risk disclosures.

Steve Turner, Mercer addressed the Panel and gave a summary of Appendix 2.

Market background

- The gradual emergence of many developed countries from restrictions as vaccine rollouts continued drove investor optimism, helping to bring about another strong quarter for risk assets.
- Markets largely saw through continued elevated inflation expectations, but it remains a key question as well as the potential impact of the delta variant on the economic recovery. Government bond yields fell thanks to central bank signals that have been less dovish than expected.

Mercer market views

- their medium-term views on the global economy are favourable, as they expect it to strengthen sharply as economies re-open more fully. Governments and central banks are likely to continue to support economic activity.

Funding level and risk

- The funding level is estimated to have improved from 97% to 101% over Q2 as asset growth outweighed the rise in the value of the liabilities. It is estimated to have increased by 9% over the year to 30 June 2021.
- The Value-at-Risk rose over the quarter to £1,134m, or 20.5% of liabilities. Risk as a proportion of liabilities has reduced over the year, largely due to the decision to move towards a dynamic equity option strategy.

Performance

- Underperformance relative to the strategic benchmark over the one and three-year period to 30 June 2021 is mainly due to the impact of the equity protection strategy, but this has behaved in line with expectations given the increase in the underlying equity markets.
- Relative performance was mixed at the mandate level, though the High Alpha Equity, Hedge Fund and Core Infrastructure mandates have continued to stand out in outperforming their benchmarks.

Asset allocation and strategy

- In May, the Fund implemented the new dynamic structure for the equity option strategy.
- In June, the Fund terminated its Multi-Asset Credit holdings with Loomis Sayles, transferring these to a new MAC fund with Brunel.
- At quarter end, all asset classes were within their ranges, except for the Renewable Infrastructure and Private Debt mandates which are still in the process of being drawn down.

Shirley Marsh-Hughes if there was now less demand for value stocks.

Steve Turner replied that this was difficult to answer and would depend on whether central banks raise interest rates, as they are more sensitive to economic activity.

Pauline Gordon asked if any further comment could be made in respect of the IFM – Core Infrastructure.

Steve Turner replied that this is a legacy portfolio and options for managing this allocation in the future will be discussed at the next Panel meeting.

The Panel **RESOLVED** to note the information as set out in the reports.

23 RISK MANAGEMENT

The Investments Manager introduced this report to the Panel. He explained that the Funding and Risk Management Group (FRMG) is responsible for agreeing the operational aspects relating to the Fund's risk management framework thereby ensuring that strategic objectives continue to be met.

He stated that this report informs the Panel of issues considered and decisions made by FRMG as well as any recommendations. He added that since the last Panel meeting there has been one meeting of the FRMG on the 26 August 2021 and that there are no strategic issues or concerns to raise with the Panel.

The Panel, having been satisfied that the public interest would be better served by not disclosing relevant information, **RESOLVED**, in accordance with the provisions of the Section 100(A)(4) of the Local Government Act 1972 that the public should be excluded from the meeting for this item of business, because of the likely disclosure of exempt information as defined in paragraph 3 of Part I of Schedule 12A of the Act as amended.

The Panel **RESOLVED** to:

- (i) Note the updated funding level and LDI hedging position
- (ii) Note the impact and performance of the equity protection strategy
- (iii) Note the performance of the Buy & Maintain Corporate Bond strategy
- (iv) Note FRMG considerations regarding the hedge ratio of the liability benchmark portfolio.

24 FORWARD AGENDA

The Group Manager for Funding, Investment & Risk introduced this report to the Panel. She said that it was likely that a stocktake review would take place during 2022.

The Panel **RESOLVED** to note the forward agenda.

The meeting ended at 3.53 pm

Chair(person)

Date Confirmed and Signed

Prepared by Democratic Services

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Avon Pension Fund

David Cox, Head of Listed Markets

September 2021





Agenda

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1. Allocations to funds
 2. Paris-aligned benchmarks
 3. ESG integration in manager selection
 4. Investing in China
 5. Q&A

Allocations to Brunel funds

Performance highlights:

- Global Emerging Markets
- Global High Alpha
- Global Sustainable Equities

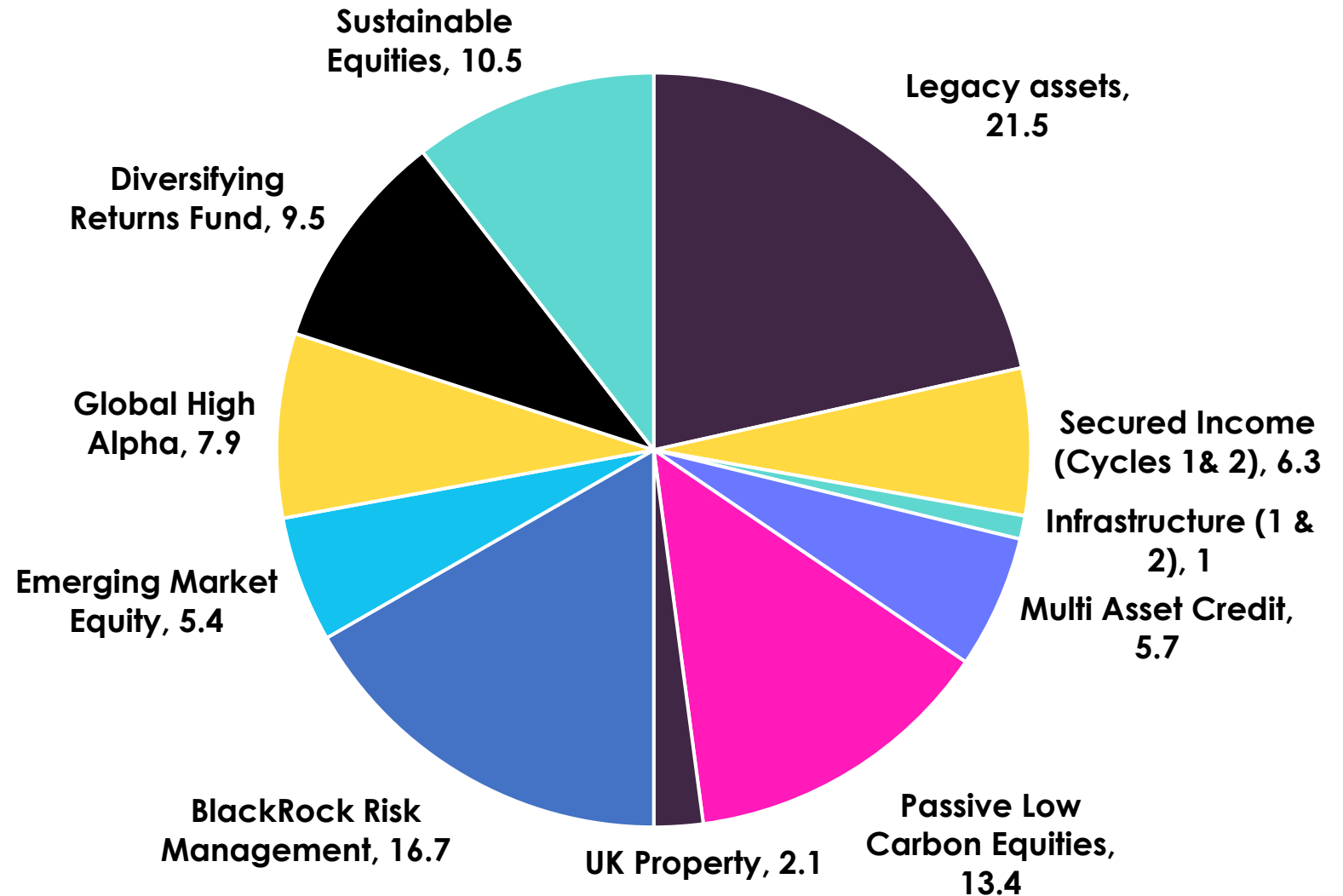
Carbon footprint:

7% y-o-y target improvement
Aggregate Brunel Portfolio at end-2020 was 33.1% lower carbon intensity than 2019 benchmark baseline

Portfolio developments:

- Manager strategy change at Baillie Gifford

Asset Allocation split %



Index leadership: Paris-aligned benchmarks

FTSE Russell-Brunel Climate Transition Benchmark (CTB) and Paris-aligned Benchmark (PAB) indices are designed to reflect the performance of a global and diversified basket of securities where weights are varied in order to achieve climate targets, including:

	FTSE Russell PAB design	FTSE Russell CTB design
Emission Targets*	<ul style="list-style-type: none"> Target reductions in <u>both</u> Carbon Reserves and Operational Emissions: <ul style="list-style-type: none"> Minimum 50% reduction (reserves and emissions) 7% year on year reduction (emissions only) 	<ul style="list-style-type: none"> Target reductions in <u>both</u> Carbon Reserves and Operational Emissions: <ul style="list-style-type: none"> Minimum 30% reduction (reserves and emissions) 7% year on year reduction (emissions only)
High Impact Sector Exposure*	<ul style="list-style-type: none"> Zero aggregate active weight in high impact sectors 	<ul style="list-style-type: none"> Zero aggregate active weight in "high impact" sectors
Green Revenues	<ul style="list-style-type: none"> 100% uplift 	<ul style="list-style-type: none"> 100% uplift
Exclusions*	<ul style="list-style-type: none"> Activity based exclusions – Oil, Gas, Coal and Electricity generators as specified by EC Delegated Act Baseline exclusions: Tobacco, Controversial Weapons, Conduct (e.g. UNGC) 	<ul style="list-style-type: none"> Baseline exclusions: Tobacco, Controversial Weapons, Conduct (e.g. UNGC)
Corporate Target Setting	<ul style="list-style-type: none"> Increase TPI Management Quality Score Increase TPI Carbon Performance 	<ul style="list-style-type: none"> Increase TPI Management Quality Score Increase TPI Carbon Performance
Capacity and Concentration Constraints	<ul style="list-style-type: none"> Capacity Ratio 20x and Effective N >25% of underlying 	<ul style="list-style-type: none"> Capacity Ratio 20x and Effective N >25% of underlying
Additional criteria	<ul style="list-style-type: none"> "Do No Significant Harm" (DNSH) concept: Additional screens applied using "Environmental Watchlist" based on Conduct screening (e.g. UNGC) dataset 	<ul style="list-style-type: none"> "Do No Significant Harm" (DNSH) concept: Additional screens applied using "Environmental Watchlist" based on Conduct screening (e.g. UNGC) dataset

ESG integration in manager selection

Similar ESG Culture

- RI team issue vs whole-company issue
- Face-to-face meetings
- Data requests

Climate Change Policy alignment

- Do they know the Policy well?
- Are their decarbonisation targets aligned?
- Do they just use exclusions?
- Do they know the specifics of climate change alignment in their asset class?
- e.g. carbon data weaknesses in structured credit

Thought leadership

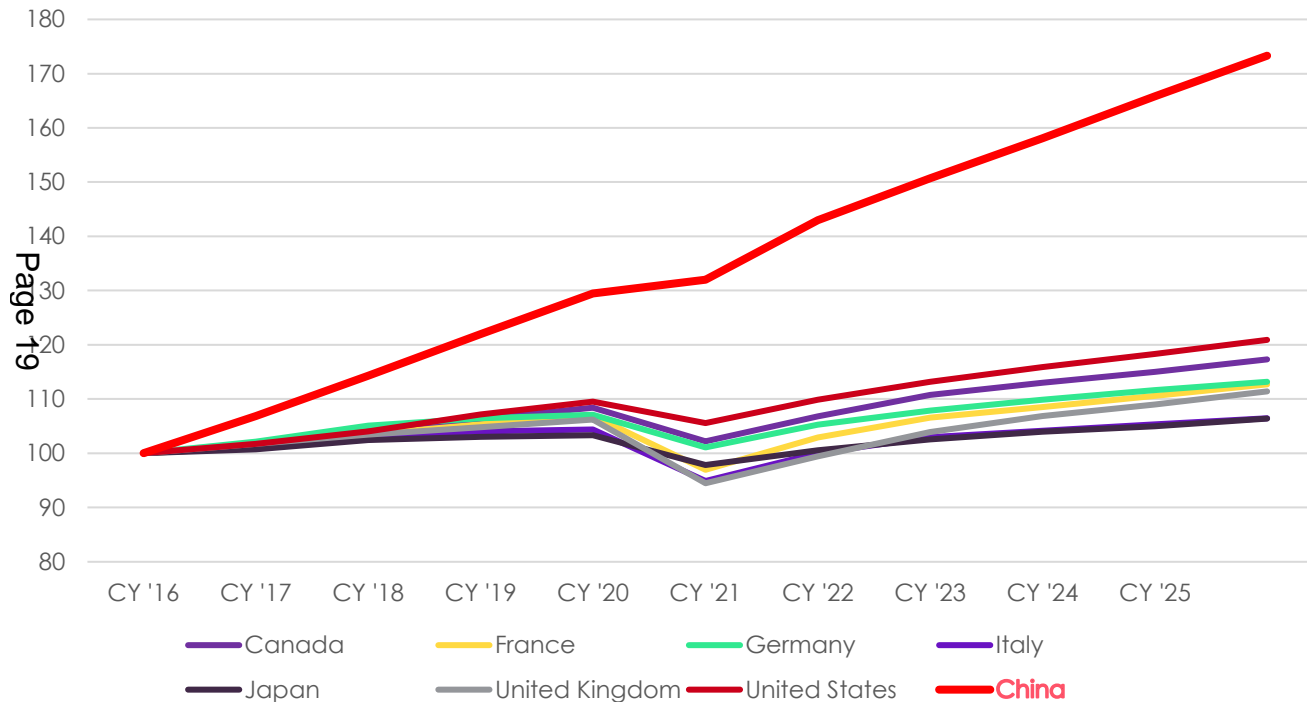
- Do they understand the constraints around getting to Net Zero in their universe?
- Are they knowledgeable on which companies and sectors are aligned on 2C?
- Have they developed an effective engagement approach or framework on 2c alignment?
- Do they know what would improve capabilities? E.g. scenario modelling on physical & transitional risk



Investing in China



Actual & Predicted GDP Growth Compounded YOY - G7 + China



Our research focuses:

- Human Rights in Supply Chains
- Data Privacy, censorship & surveillance
- Corporate Governance
- Hong Kong and Taiwan
- Climate Change
- ADR/H-Share/A-Share

Next Steps

- Continue engagement with companies
- Roll out analytical tools
- Deeper engagement with asset managers is under way
- Continue our research, including engaging with other industry participants (including RI)
- Support Chinese investors

Q&A



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