Avon Pension Fund

Local Government Pension Scheme

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Dear Alasdair,

Thank you for your statement to the Avon Pension Fund Committee on 26 March 2021 on behalf of the Unison branches.

The Fund has taken significant action to reduce the financial risk from stranded assets as well as reduce its carbon exposure but we do recognise that there is more potentially that needs to be done. We are proactively collaborating with partners to develop investment solutions that are aligned to the transition to the low carbon economy; as well as reducing financial risk these will provide opportunities to drive invest in a greener world.

Has the fund identified which companies in which it invests are engaging in fossil fuel extraction and fossil fuel energy production?

The Fund has committed to becoming a net zero investor by 2050 or earlier and we have set out a roadmap including interim targets to help us achieve this goal. We have made a declaration to selectively divest from companies that operate in a way that is inconsistent with our net zero ambition. There is a distinction between companies that are not presently aligned with a net zero pathway but show clear intent to get there and those companies that are intentionally failing to take account of climate transition risk and adapt their business models accordingly. These companies clearly represent a material financial risk to the Fund and would necessarily be candidates for divestment.

There are several tools at our disposal to help identify companies that present a risk to our climate change objectives and that threaten our ability to deliver positive outcomes for our members. This 'toolkit' consists of carbon analytics at portfolio and individual stock level, an engagement programme that comprises clearly defined and measurable milestones, and access to industry leading research and initiatives such as the Institutional Investors Group on Climate Change (IIGCC). Critically, our pooling provider, Brunel, use best-in-class analytical tools such as the Transition Pathway Initiative to assess how portfolios and the underlying companies that we invest in are managing climate transition risk; ensuring that any decision to invest (or not) stands up to scrutiny. Further information is provided below.

How is the progress those companies are making towards decarbonisation being measured?

The Fund assesses its carbon footprint on an annual basis, which highlights companies that exhibit the greatest direct and downstream emissions outputs, future emissions exposure, the type of fossil fuel activity investee companies engage in and the level of transparency with which they report climate risks. This information, combined with inputs from our strategic memberships to organisations such as the Institutional Investors Group on Climate Change (IIGCC) and Climate Action 100+ (CA100+), inform a comprehensive engagement programme, which is designed to quantify engagement success. Information relating to this framework can be found in the Fund's Annual Engagement Report here.

We also recognise that there is a need to develop and decarbonise the products and services we use to invest in underlying companies. This is a complex area with very little standardisation and a proliferation of new products. As we look at the viability of shifting our entire equity allocation (37.5% of total assets) into low carbon and sustainable solutions later this year we will evaluate, among other things, the effectiveness of current passive low carbon equity funds (such as the one the Fund currently invests over £650m in). These products are extremely effective in removing emissions from a portfolio at the point of investment and exhibit low 'stranded asset' risk relative to their market-cap equivalents due to the lower allocations to oil & gas companies. However, in order to maintain risk adjusted returns these products might increase allocations to companies that are highly correlated with the oil & gas industry, which is fundamentally inconsistent with a net zero pathway.

Recently we played an integral role in the development of the IIGCC Net Zero framework, which recommends actions to help investors align portfolios to net zero and maximise the contribution to the decarbonisation of the real economy. The work undertaken as part of this initiative, along with the outcomes of our equity allocation review, will inform a wider stocktake undertaken by Brunel in 2022 where underlying asset managers, and, indeed, the holdings themselves will be assessed based on the steps taken to manage climate risks and enable overall net zero alignment.

The criteria to evaluate companies and managers is being developed but could, for instance, take account of current emissions, the level of capital expenditure committed to renewables projects and other forward looking metrics designed to capture transition risk such as future reserves emissions and the extent to which net zero commitments are backed up with credible net zero plans.

For further information I would direct you to the dedicated climate change page on the Brunel website here, which includes information relating to the 2022 stocktake, the governance structures in place to support clients investment objectives as well as some recent examples of high profile engagements with fossil fuel extraction companies.

Finally, we expect to publish our latest annual carbon metrics report before the end of June and in the meantime would invite you to read the results of last year's analysis here

For reference I attach a link to the holdings data published on our website that includes the value of investments in underlying companies and the sectors in which they operate.

Has the fund begun the process of assessing which, if any, of those companies will be considered for selective divestment ahead of the Paris Stocktake in 2023, owing to their insufficient progress towards meeting the 2015 Paris Agreement?

If not, when does the fund plan to begin the process of identifying these laggard companies?

We deliberately set a timeframe to assess companies that ensured there was time for the engagement initiatives to develop and be measured. As engagement is a tool to change attitudes and behaviours, companies need to be able to respond to the challenge set by investors with credible, measurable and implementable policies and strategies and the process is by necessity iterative. In the meantime, we are monitoring progress but the review will be part of the 2022 stocktake as previously stated.

Yours sincerely,

a R Bartlett

p.p. Tony Bartlett, Head of Pensions on behalf of Councillor Bruce Shearn, Chair of Pension Committee, Avon Pension Fund