Nottinghamshire County Council

Report to Pension Fund Committee

8 December 2022

Agenda Item: 7

REPORT OF SERVICE DIRECTOR – FINANCE, INFRASTRUCTURE & IMPROVEMENT

CLIMATE RISK ANALYSIS AND TASKFORCE ON CLIMATE-RELATED FINANCIAL DISCLOSURES REPORT

Purpose of the Report

1. To present the Climate Risk Analysis from LGPS Central Ltd to Members, and present this year's Task Force on Climate-related Financial Disclosures (TCFD) report.

Information

2. In 2020, in order to enable the Pension Fund to identify its exposure and understand its financial risk arising from climate change, the Fund commissioned LGPS Central to produce some climate risk analysis and scenario modelling, and a TCFD report which contains the key elements of the Climate Risk report. The scenario modelling is only performed every few years, but has been refreshed for 2022 and includes a 1.5° scenario. The climate risk analysis has been repeated based on data at 31 March 2022.

3. This Climate Risk Report has been issued to the Nottinghamshire Pension Fund, and has been presented to the members of the Nottinghamshire Pension Fund Committee by LGPS Central at a training session to communicate the findings and recommendations of the Climate Risk Report, and enable Members to appreciate the challenge in obtaining reliable data for these calculations and the complexity of modelling these issues.

4. Some modifications have been made to the climate risk report this year. Financed emissions have been included as a metric and a comparison between 2019 and 2021 emissions numbers is provided. Financed emissions measure the absolute tons of CO_2 for which an investor is responsible. This is an important metric when measuring the net zero alignment of an investment portfolio and or the decarbonisation trajectory of the portfolio. Unlike Carbon Intensity metrics, financed emissions are not influenced by market capitalisation or revenue. Financed emissions are recommended by the IIGCC Net Zero Framework as one of a number of metrics that investors should monitor.

5. A Net Zero coverage metric is also included. This is calculated as the weight of the portfolio invested in companies that have set a "net zero" emissions target, as defined by the company. Whilst we recognise that not all Net Zero commitments are equal and therefore this metric has limitations, we think that is useful to know which companies have not yet set a target. This can potentially help with engagement and voting prioritisation.

6. In order to give a better indication of a portfolio company's actual exposure to fossil fuels and clean technology, the percentage of revenue derived from these activities is provided. This is also provided at portfolio and fund level.

7. The fund has also completed its second climate scenario analysis this year. The Investment Consultant Mercer's have been retained for this work; three climate scenarios are analysed, Rapid Transition, Orderly Transition and Failed Transition which explore a range of plausible futures over 5 to 40 years. Each scenario analysis has a different combination of transition and physical risks associated with it, playing out over different time frames, with transition risks impacting earlier and physical risks impacting later.

8. Appendix A presents the TCFD report which shares the key results of the analysis.

9. There are restrictions on what can be publicly reported from the climate risk analysis due to commercial confidentiality of supplier intellectual property, so the Climate Risk report is attached as exempt Appendix B.

10. The purpose of the climate risk analysis is to help the Pension Fund better understand the risks and implications of climate change. It does this based on the available data. As this is dependent on what companies currently publish, it should be noted that this data is incomplete. The model requires a number of assumptions and the output of the model should be interpreted in this context. Data is improving, partly due to pressure from engaged shareholders such as ourselves, but the sensitivity to assumptions and estimations and incompleteness of the data needs to be appreciated in interpreting the results of this work.

11. Despite this caveat, the analysis is supportive of the Fund's current investment strategy.

- It shows that the year end equity holdings continue to be 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.
- It demonstrates that a scenario consistent with an orderly transition is of greatest benefit to the Pension Fund financially which means the Fund's financial interests are aligned with global environmental interests.

12. Members should be reassured of these signs that they are discharging their responsibilities appropriately.

Report recommendations and considerations

13. The report provides a number of new recommendations for incorporation into Climate Stewardship Plan for the Committee's consideration. These are as follows:-

Category	Action	Timing	Notes
Climate Stewardship Plan	Add NextEra Energy, Reliance Industries, Cemex and Southern Company to the Climate Stewardship Plan for 2023-24. (Anglo-American was added for 2022-23)	2023-24	With the support of LGPS Central

14. There are no new items for the Climate Action Plan but some wording changes and deletions to reflect completed actions. Progress on existing actions in the Climate Action Plan was

reported to the November Committee meeting. The wording changes will be reflected at the next review.

Ongoing work

15. While this work is ongoing the Pension Fund will continue to implement its long term Strategic Asset allocation. This includes an increasing allocation to infrastructure investments, a significant proportion of which are in clean energy, and a gradual reduction in equity investments. Within our equity investments we have made investments to sustainable funds since year end. Over time our exposure to fossil fuels will reduce as a result of these asset allocation and diversification decisions.

16. The Pension Fund will continue to monitor and manage all financially material risks to which it is exposed.

Other Options Considered

17. The Pension Fund is not required to undertake climate risk analysis or to publish a TCFD report. However undertaking climate risk analysis and publishing a TCFD report are regarded as best practice and are consistent with the Pension Fund's commitment to transparency.

Reason/s for Recommendation/s

18. Members and officers need to better understand and control the climate related financial risks in the Pension Fund investments.

Statutory and Policy Implications

19. This report has been compiled after consideration of implications in respect of crime and disorder, data protection and information governance finance, human resources, human rights, the NHS Constitution (public health services), the public sector equality duty, safeguarding of children and adults at risk, service users, smarter working, sustainability and the environment and where such implications are material they are described below. Appropriate consultation has been undertaken and advice sought on these issues as required.

Financial Implications

20. There are no direct financial implications arising as a result of publishing this report.

RECOMMENDATION/S

1) That members include the new actions in the Climate Action report and consider whether there are any other actions they require in relation to the issues contained within the report.

Nigel Stevenson
Service Director for Finance, Infrastructure & Improvement and Section 151 Officer

For any enquiries about this report please contact: Tamsin Rabbitts

Constitutional Comments (KK 28/11/2022)

21. The proposal in this report is within the remit of the Nottinghamshire Pension Fund Committee.

Financial Comments (TMR 28/11/2022)

22. The financial implications are set out in paragraph 20.

Background Papers and Published Documents

Except for previously published documents, which will be available elsewhere, the documents listed here will be available for inspection in accordance with Section 100D of the Local Government Act 1972.

- None

Electoral Division(s) and Member(s) Affected

- All