PENSIONS COMMITTEE 23RD JUNE 2023

PUBLIC QUESTION TIME

1. Question from Dr. Jamie Russell

The LGPS Quarterly Stewardship Update offers several examples of the fund's current strategy of engagement with fossil fuel companies. However, there seems to be a huge gulf between targets and outcomes.

For example, Glencore recently rejected a resolution from major institutional investors who were calling for transparency on how the company's thermal coal production aligns with the 1.5C target agreed at Paris. The investors represented $2.2 trillion of assets and included giants like Legal & General and HSBC Asset Management. Glencore ignored their attempts at engagement.

Meanwhile, Shell has abandoned plans to cut oil production and is now ramping up its expansion of fossil fuels while prioritising shareholder profits. Again, engagement by climate-concerned investors has been ignored.

The LGPS Update mentions Metro Inc. It claims that a shareholder proposal on Paris-alignment failed to pass after receiving only 28.7% support from investors. The update claims this sent a "strong message" to the firm's management that climate was important. If committee members received 28.7% of a vote with 100% turnout, would they see this as a victory?

The first half of 2023 has given us record air temperatures, unusually hot oceans, record levels of atmospheric CO2, and record low levels of Antarctic sea ice. Internationally recognised climate scientists have described what is happening as “totally bonkers” and believe it is a signal that our climate may be breaking down faster than predicted (https://edition.cnn.com/2023/06/17/world/four-climate-charts-extreme-weather-heat-oceans/index.html)

Does the committee really believe that its engagement strategy is working?

Response:

LGPS Central’s engagement approach is defined by their belief in responsible ownership, whereby they leverage their rights as company owners to encourage better ESG practice. If enough investors can collaborate on the same issues, there is real potential to drive meaningful change.

Evidence of the success of shareholder engagement is abundant. The differences in climate transparency and decarbonisation ambition between companies engaged by Climate Action 100+ (an investor-led collective engagement initiative) and those not, as well as differences between publicly- and privately-owned companies is clear.

At Glencore’s 2023 AGM, a resolution to approve the company’s 2022 Climate Report received 30% shareholder dissent, and a shareholder proposal regarding the company’s Climate Action Transition Plan received 29% support. 28.7% dissent on a shareholder proposal relating to alignment with the Paris Agreement at Metro Inc’s 2022 AGM was also well above the 20% threshold required to stimulate an obligatory corporate response.

The importance of such votes should not be underestimated. Not only can significant dissent profoundly influence corporate policy in the short term, but it also opens up new channels of engagement from other shareholders in the future. Furthermore, high levels of dissent can be noticed by proxy advisory firms, who may change their voting recommendations for future AGMs. In this way, levels of dissent can quickly grow if corporate policy remains unchanged.

It is also important to recognise that engagement is rarely a linear process. As evidenced by recent announcements from Shell and BP, companies' short-term strategy can continue to develop contrary to the long-term expectations of large groups of shareholders. In such situations, we must turn to our escalation approach and work with like-minded investors to demonstrate the level of our concern on these issues. On this basis, LGPS Central has filed shareholder resolutions and submitted evidence to court to further its commitment to encouraging ambitious decarbonisation from its portfolio companies.

Engagement by responsible investors is having a positive influence on corporate behaviour. Based on data provided by EOS, LGPSC's stewardship provider, approximately 60% of engagements across LGPSC's managed funds progressed towards the achievement of at least one pre-determined objective over the 2022 calendar year. Through thoughtful escalation and targeted engagements, we remain confident that our "responsible ownership" approach is the most effective way of continuing to drive meaningful change with our portfolio companies, policymakers and regulators.

The Funds investments in Glencore have reduced from £4 million at 31 March 2022 to £1.3 million at 31 March 2023.

2. <u>Question from Mr Michael Cripps</u>

In an investor update Shell recently announced that it will continue investing in fossil fuels, while still pledging to be committed to net zero. Experts say this is nonsense (as per this article in the New Scientist see below).

Do committee members agree that the fund's continued investment in Shell and other fossil fuel companies is helping to make the climate crisis better or worse?
And how does this fit with Shropshire Council's (one of the main partners in the pension fund) declaration of a climate emergency several years ago?

https://www.newscientist.com/article/2378414-shell-cant-say-it-backs-net-zero-while-still-betting-on-fossil-fuels/

Response:

As an active member of CA100+ and long-term investor in Shell, LGPSC LGIM and CTI has continuously engaged with the company over its climate transition strategy. This engagement is driven by our belief that companies like Shell, with established access to energy infrastructure and significant economic resource, will play an integral role in any successful transition.

With this in mind, over recent years we have voted against management at AGMs, written to and met with the company, and provided evidence in a court case against the company's Board in order to encourage a more ambitious approach towards decarbonisation and net zero.

One of Shell's more ambitious targets had been to reduce oil production by 1-2% per year until 2030, based on a 2019 baseline. As the company has already achieved a 21% reduction following significant divestments, they have now announced that current oil production levels will remain consistent until 2030. While we were disappointed to see that Shell is not planning to continue such a commendable reduction, we recognise that the company is at least not scaling back on its oil reduction targets.

That said, we still believe that Shell will struggle to align with the Paris Agreement without a substantial further reduction in hydrocarbon production by 2030. We are cognisant of the potential risk of stranded assets as the world accelerates towards net zero, and the impact this could have on investment returns. We have high expectations that our managers will be cognisant of these risks and ESG considerations, including climate change, will be integrated into their investment processes and reflected in their investment decisions.

Future engagements with the company by LGPSC, our engagement partners and external managers will therefore seek assurances around the company's commitment to the transition. It is also critical that Shell reaffirms its commitment to substantially increasing investments in low carbon areas such as renewable energy generation, hydrogen, bioenergy, and electric vehicle charging. This will enable Shell to make a positive contribution to the transition and remain economically viable in a low carbon economy.

We welcome Shell's sustainability-related initiatives. These include its positive acceleration programme aimed at supporting energy startups to develop their capabilities and power business growth within the smart energy landscape, and Shell's continued work on responsibly decommissioning its oil and gas fields.

We remain convinced that by engaging with these companies we are best able to leverage our influence and help drive real-world decarbonisation. Although we recognise the challenges of Shell's transition, we will continue to encourage the company to show leadership and deliver on its short-, medium-, and long-term Paris-aligned decarbonisation targets.

3. <u>Question from Mr Paul Cooper</u>

Many of us are aware that Philip Dunne, one of our local Conservative MPs, is doing sterling work as Chair of the Environmental Audit Committee.

On January 5th this year, that Committee issued a House of Commons report entitled Accelerating the transition from fossil fuels and securing energy supplies.

The Report includes the following prophetic challenge:
'A national "war effort" on energy saving and efficiency is required.'

As your contribution to this 'war effort' will you seize the moment and take up the challenge by divesting the Shropshire County Pension Fund from fossil fuels?

Response:

The scale of effort required to transition to a net zero economy in an equitable manner and at the required pace is vast. Significant contributions are required from all corners of society, including energy providers, governments, regulators, consumers, and investors.

SCPF believe that the most effective way of accelerating this change is through meaningful ESG integration. Key to this approach is ensuring that our managers are focussed on identifying all ESG risks and opportunities, including climate considerations, and incorporating those into their investment decisions. Shifting capital into areas of the economy that are supportive of the transition will be critical to its success.

For companies which may be more exposed to climate risk, we expect our managers to engage in a meaningful way and encourage a timely and just transition. The Funds investments in Shell have reduced from £14 million at 31 March 2022 to £3 million at 31 March 2023 reflecting this dynamic approach. We believe that this collaborative approach is very much in line with that of the government, whereby all sectors have a role to play in facilitating the transition. Focus needs to be placed on both the demand for fossil fuels as well as the supply if the transition is to succeed and global warming is to be limited to well below 2 degrees.

We do not consider that a policy of divestment will accelerate the transition to a lower carbon economy nor do we think that this is the optimal way for investors to manage the risks associated with climate change. Oil, Gas and Coal do not contribute equally to global warming and do not have the same transition risk profile. Equally different companies with different assets are exposed to risks in different ways. We consider the best way to manage investment risks arising out of the transition is for our investment managers to analyse companies on their own merits.

Unfortunately demand for fossil fuels remains robust and it remains an important part of the global energy mix. The performance of the sector has been strong in recent years, and this is exacerbated by the events in Ukraine with have brought energy security into sharp focus.