**SURREY COUNTY COUNCIL**

**PENSION FUND COMMITTEE**

**DATE:** **8 JUNE 2018**

**LEAD OFFICER:** **SHEILA LITTLE, DIRECTOR OF FINANCE**

**SUBJECT:** **CARBON ASSET EXPOSURE REVIEW**

## SUMMARY OF ISSUE:

To understand the Surrey County Council Pension Fund's current exposure to assets which are carbon intensive in their activities and how a future reallocation of the Fund's equities will impact its current Carbon Asset exposure.

## RECOMMENDATIONS:

It is recommended that the Pension Fund Committee:

1. Note the report.

## REASON FOR RECOMMENDATIONS:

The Pension Fund Committee must approve and review all working documents produced for the Pension Fund.

## DETAILS:

**Background**

1. The Surrey Local Pensions Board conducted a review of Environmental, Social and Governance (ESG) compliance in spring 2017 which was then reported to the Surrey Pension Fund Committee on 10 November 2017.The Pension Fund Committee then approved the recommendation to establish the fund's current carbon asset exposure, with the initial analysis being carried out on the Fund's passive and active equities.

**Methodology**

2. TruCost's carbon footprint analysis measures the greenhouse gas emissions produced within each equity portfolio (per tonnage) in relation to their annual revenue, demonstrating how much of their return is determined by activities which emit carbon dioxide.

   This is done by measuring the carbon footprint of each individual asset holding, encompassing both direct and first tier indirect impacts. Direct impacts are those which result from a company's own vehicles, operations and waste. First tier indirect impacts occur as a result of a company procuring services from within their supply chain.

**Findings**

3. The table below summarises the carbon asset exposure of each Equity manager in comparison to their Benchmarks.

| Equity Manager | Value of Holdings (£m) as at 28 February 2018 | Total CO2 Footprint per £m holding (tCO2e/£m revenue) | Benchmark CO2 Footprint per £m holding (tCO2e/£m revenue) | Variance | Benchmark used |
|---|---|---|---|---|---|
| LGIM Passive - UK Equity | 351.89 | 361.66 | 358.17 | +0.98% | FTSE UK All Share |
| LGIM Passive - World Developed | 485.13 | 390.90 | 394.02 | -0.79% | FTSE Developed |
| LGIM Passive World Emerging Market | 54.09 | 832.70 | 854.41 | -2.54% | FTSE Emerging Markets |
| Marathon Global Equity | 491.86 | 313.03 | 420.54 | -25.57% | MSCI ACWI |
| Newton Global Equity | 320.8 | 173.54 | 420.54 | -58.73% | MSCI ACWI |
| Majedie UK Equity | 321.27 | 286.45 | 358.17 | -20.02% | FTSE UK All Share |
| UBS UK Equity | 306.06 | 276.04 | 358.17 | -22.93% | FTSE UK All Share |

4. The deciding factor which contributes to how a portfolio's carbon exposure exceeds its benchmark is whether it is heavily invested in carbon intensive markets (the more intensive being the Utilities, Energy or Materials market). The other factor would be if a portfolio is invested in the most carbon intensive companies within a market.

**Contributing Factors**

5. Some of the contributing factors relating to the Carbon Efficiency of each portfolio are highlighted below

| Equity Manager | Contributing Factor to Variance |
|---|---|
| LGIM Passive - UK Equity | In aggregate, the two sectors that have the greatest positive effect on carbon efficiency are Telecommunication Services and Information Technology, which together contribute 0.0% of the increased carbon efficiency.<br><br>The two worst performing sectors in the portfolio are Materials and Consumer Discretionary, which contribute to 0.61% of reduced carbon efficiency.<br><br>The largest Contributors to the Portfolio's Total Carbon Apportionment are Royal Dutch Shell PLC, BP and CRH Plc with a combined carbon apportionment of 45.33% of the portfolio. |
| LGIM Passive - World Developed | In aggregate, the two sectors that have the greatest positive effect on carbon efficiency are Industrials and Materials, which together contribute 1.11% of the increased carbon efficiency.<br><br>The two worst performing sectors in the portfolio are Utilities and Energy, which contribute to 1.24% of reduced carbon efficiency.<br><br>The largest Contributors to the Portfolio's Total Carbon Apportionment are LafargeHolcim Ltd, Exxon Mobil Corp and RWE AG with a combined carbon apportionment of 7.89% of the portfolio. |
| LGIM Passive World Emerging Market | In aggregate, the two sectors that have the greatest positive effect on carbon efficiency are Utilities and Financials, which together contribute 2.28% of the increased carbon efficiency.<br><br>The two worst performing sectors in the portfolio are Industrials and Consumer Staples, which contribute to 0.2% of reduced carbon efficiency.<br><br>The largest Contributors to the Portfolio's Total Carbon Apportionment are Gazprom PJSC, NTPC Ltd and Sasol Ltd with a combined carbon apportionment of 14.36% of the portfolio. |
| Marathon Global Equity | In aggregate, the two sectors that have the greatest positive effect on carbon efficiency are Utilities and Energy, which together contribute 33.24% of the increased carbon efficiency.<br><br>The two worst performing sectors in the portfolio are Consumer Staples and Health Care, which contribute to 18.84% of reduced carbon efficiency.<br><br>The largest Contributors to the Portfolio's Total Carbon Apportionment are Archer-Daniels-Midland Co, Bunge Ltd and |

| | |
|---|---|
| | Praxair Inc. with a combined carbon apportionment of 43.06% of the portfolio. |
| Newton Global Equity | In aggregate, the two sectors that have the greatest positive effect on carbon efficiency are Utilities and Materials, which together contribute 39.21% of the increased carbon efficiency.<br><br>The two worst performing sectors in the portfolio are Health Care and Telecommunication Services, which contribute to 4.95% of reduced carbon efficiency.<br><br>The largest Contributors to the Portfolio's Total Carbon Apportionment are Royal Dutch Shell PLC, Conoco Phillips and Albemarie Corp with a combined carbon apportionment of 41.73% of the portfolio. |
| Majedie UK Equity | In aggregate, the two sectors that have the greatest positive effect on carbon efficiency are Consumer Staples and Utilities, which together contribute 21.41% of the increased carbon efficiency.<br><br>The two worst performing sectors in the portfolio are Financials and Industrials, which contribute to 11.35% of reduced carbon efficiency.<br><br>The largest Contributors to the Portfolio's Total Carbon Apportionment are BP, Royal Dutch Shell PLC and Mondi Ltd with a combined carbon apportionment of 46.53% of the portfolio. |
| UBS UK Equity | In aggregate, the two sectors that have the greatest positive effect on carbon efficiency are Materials and Industrials, which together contribute 19.67% of the increased carbon efficiency.<br><br>The two worst performing sectors in the portfolio are Financials and Consumer Discretionary, which contribute to 3.89% of reduced carbon efficiency.<br><br>The largest Contributors to the Portfolio's Total Carbon Apportionment are BP, Royal Dutch Shell PLC and Anglo American PLC with a combined carbon apportionment of 51.53% of the portfolio. |

## CONSULTATION:

6. The Chairman of the Pension Fund has been consulted and offered full support for the proposals.

## RISK MANAGEMENT AND IMPLICATIONS:

7. Reduce risk by rebalancing holdings to favor companies that are more carbon efficient

8. Engage with companies within the Fund's portfolios to disclose better environmental data

9. Use the analysis to understand how equity allocation rebalance will have an impact on the Fund's existing Carbon Asset exposure.

## FINANCIAL AND VALUE FOR MONEY IMPLICATIONS

10. There are no financial and value for money implications.

## DIRECTOR OF FINANCE COMMENTARY

11. The Director of Finance (Section 151) is satisfied that all material, financial and business issues and possibility of risks have been considered and addressed.

## LEGAL IMPLICATIONS – MONITORING OFFICER

12. There are no legal implications or legislative requirements

## EQUALITIES AND DIVERSITY

13. The Carbon Asset Exposure analysis does not require an equality analysis, as the initiative is not a major policy, project or function being created or changed.

## OTHER IMPLICATIONS

14. There are no potential implications for council priorities and policy areas.

## WHAT HAPPENS NEXT

15. The following next steps are planned:

    - Continued review by the Pension Fund Committee;
    - Seek advice from Mercer and the Independent Advisor on how the proposed equity rebalance will have an impact on carbon asset exposure.

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**Contact Officer:**
Neil Mason, Head of Pensions

**Consulted:**
Pension Fund Committee Chairman

**Annexes:** None

**Sources/background papers:** None

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