NILGOSC
NORTHERN IRELAND LOCAL GOVERNMENT OFFICERS' SUPERANNUATION COMMITTEE

Climate Risk Statement

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1. Introduction

1.1. Climate change is a global challenge for governments, corporations and investors alike. Through this statement, NILGOSC acknowledges that the changing climate will have a significant impact on the global economy, corporations and society, whether through direct physical impacts, tighter regulations or reputational damage suffered by those who fail to adequately address the risks posed.

1.2. As the Local Government Pension Scheme for Northern Ireland, with approximately 160,000 members, NILGOSC expects to be paying pensions to its beneficiaries into the next century and aims to deliver a sustainable Fund, both financially and as a responsible investor. NILGOSC therefore considers it to be in the long-term interests of its members to promote climate risk mitigation and adaptation in the implementation of its investment strategy. By working together with like-minded investors, NILGOSC seeks to create an investment environment which contributes to a low-carbon economy.

1.3. This statement sets out the climate risk framework within which NILGOSC operates.

2. Investment Beliefs

2.1. NILGOSC has a fiduciary duty to act in the best long-term interests of its members, and recognises that environmental, social and governance (ESG) issues can materially impact on the financial performance of its investments. It has incorporated such considerations into its risk management and investment decision making framework.

2.2. NILGOSC believes that climate change presents a material financial risk to the Fund and will therefore take climate risk considerations into account as part of its investment policy. NILGOSC considers that this approach is consistent with its legal duty to act in the best long-term interests of its members and to deliver the long-term returns necessary to ensure an affordable and sustainable pension fund.

2.3. NILGOSC supports the aims of the Paris Agreement and will work with others to encourage the action necessary to limit global temperature rise to below 2°C above pre-industrial levels. NILGOSC demonstrates its support through the various engagement activities it undertakes, as well as investment decisions.

2.4. NILGOSC has classified climate risks into three broad categories, which are applicable across the range of asset classes in which it invests: policy risk; technology risk; and physical risk. The first two risks fall under the bracket of ‘transition risk’, which is the risk to underlying assets in a portfolio resulting from changing policies, practices and technologies as countries move towards reducing their carbon reliance. The other key climate-related risk is ‘physical risk’, which can be either acute or chronic in nature. Different asset classes will be susceptible to different risks, over different time frames, with some assets demonstrating more sensitivity than others, even within a particular asset type or sector. As a general rule, assets such as equities and bonds are likely to see a much quicker impact of policy change, than real assets such as property or infrastructure.

(i) Policy risk: the impact of policy decisions and regulatory change on global economies, companies and individual investments is considered to be both a short and medium-term risk as the exact timescales of necessary changes remains unclear. Current global policy is not aligned with the aims of the Paris Agreement, which is to keep a global temperature rise this century well below 2°C above pre-industrial levels and to pursue efforts to limit the temperature increase even further to 1.5°C. It is not clear how quickly, if at all, governments will act to meet their commitments.

(ii) The implementation of long-term global climate stabilisation targets and securing sufficient investment in future low carbon patent revenues is considered an opportunity for investors. However, Technology risk covers the risk that key low or no carbon technologies do not deliver as planned, as well as the risk incurred if the costs of transitioning to lower emissions technology are more extensive than expected. Technology risk is considered a short to medium term risk and is linked to the pace of policy change.

(iii) Physical risk: the impact of extreme weather, flooding, droughts and rising sea levels on industry, physical assets, companies and infrastructure is considered a medium to longer term risk. Physical risks will have financial implications for schemes, such as direct damage to assets and indirect destabilising impacts from supply chain disruption. Other potential impacts of physical changes in the climate are wider economic and social disruption, including mass displacement, environmental-driven migration and social strife.

2.5. NILGOSC believes that robust management of these risks, together with sound governance practices and responsible behaviour can contribute significantly to the long-term performance of investments.

2.6. NILGOSC believes that active engagement is the most effective way to bring about change, both at a policy level and in respect of individual investments. NILGOSC considers divestment can be a blunt instrument which removes the ability to engage effectively with a company or government. Therefore, NILGOSC does not exclude investments or divest solely on ESG grounds within its actively managed mandates.

3. Our Approach

3.1. NILGOSC's Corporate Plan includes the strategic objectives of: investing scheme funds in accordance with the Statement of Investment Principles; ensuring effective stewardship in line with the Statement of Responsible Investment; and managing the investment risks posed by climate change. The Plan includes a number of climate-related operational actions to assist in meeting those objectives.

3.2. NILGOSC has established a robust risk management framework as a means of identifying, recording and managing those risks which could prevent it from achieving its Corporate Plan strategic objectives. NILGOSC has a single corporate risk register which is subject to formal quarterly reviews to ensure it remains relevant and accurately reflects the risks facing the organisation.

NILGOSC's Risk Management Policy sets out the organisation's risk control framework and appetite to risk. There are two risks on the Risk register that relate specifically to responsible investment.

3.3. The Statement of Investment Principles and Statement of Responsible Investment set out NILGOSC's approach to incorporating responsible investment considerations, including systemic risks such as climate risk, into its investment strategy and decision-making process across the range of asset classes in which NILGOSC invests. To supplement these statements, this Climate Risk Statement sets out the steps NILGOSC will take to address climate risk at both a policy and portfolio level.

Policy and Procedure Level

3.4. NILGOSC has developed a suite of procedures and policy documents which set out how climate risk is incorporated into its investment processes and practice. This will vary across asset types however the high-level principles remain consistent.

3.5. NILGOSC delegates the selection of individual investments held to its externally appointed managers and does not impose restrictions on environmental, social or governance (ESG) grounds alone. NILGOSC has however instructed its active managers to take account of climate risk considerations in their decision-making processes, provided the primary financial obligation is not compromised. Where climate change produces a financial risk for a particular investment, NILGOSC expects this to be a fundamental part of the investment decision-making process and will monitor such decisions accordingly. Managers are asked to account for how climate risk is integrated into decision making.

3.6. The Committee reviews performance on a quarterly basis by way of a balanced scorecard, which assesses investment managers against a range of qualitative criteria, one of which relates to the inclusion of ESG factors in the decision-making process.

3.7. All active investment managers are instructed to engage, on NILGOSC's behalf, with those companies where ESG policies fall short of acceptable standards and where this is likely to have a detrimental effect on the long-term value of the company. NILGOSC requires its investment managers to provide regular reporting on such engagement activity and assesses compliance through the quarterly balanced scorecard monitoring process.

3.8. NILGOSC seeks to ensure that the managers and advisors it appoints have the necessary expertise in assessing climate risk. NILGOSC assesses these capabilities at the selection and appointment stage via the tender process by applying mandatory ESG criteria. NILGOSC will only appoint managers and advisors who have demonstrated that they meet an acceptable threshold and NILGOSC encourage its managers to address climate risks and opportunities in their investment research, analysis, decision-making and engagement activities.

3.9. NILGOSC has instructed its investment advisors to consider the impact and opportunities of climate change in the provision of advice, including the proactive consideration of opportunities to invest in low carbon assets.

3.10. NILGOSC has developed a bespoke Voting Policy which sets out its expectations for good governance, including how companies manage their impact on society and the environment. This policy is reviewed annually and sets out how NILGOSC addresses sustainability-related resolutions, including specific reference to climate risk and climate related financial disclosures. NILGOSC actively supports the Financial Stability Board’s Task Force on Climate-related Financial Disclosures (TCFD) and uses its voting rights to encourage investee companies to comply.

3.11. As a means of demonstrating its commitment to responsible investment practices, NILGOSC has adopted the United Nations supported Principles of Responsible Investment (PRI). NILGOSC seeks to collaborate with like-minded investors, and shares knowledge and resources on managing climate risk through its membership of industry initiatives, including: the PRI; the Institutional Investors Group on Climate Change (IIGCC); the CDP (formerly the Carbon Disclosure Project); the UK Pension Scheme Responsible Investment Roundtable; the Occupational Pensions Stewardship Council (OPSC); and Climate Action 100+.

3.12. NILGOSC will continue to work together with like-minded investors on initiatives which seek to reduce the threat and impact of climate change. A full list of climate change related initiatives are listed on the Engagement and Initiative section of the NILGOSC website: https://nilgosc.org.uk/pension-fund/being-a-responsible-investor/engagement-initiatives/

Portfolio Level

3.13. The assessment of climate related risks and opportunities will vary across asset classes, sectors and individual portfolio holdings. NILGOSC seeks to ensure that climate risk is taken into account across its investment portfolio on a consistent and proportionate basis.

3.14. NILGOSC is an active investor and seeks to use its influence to engage with policy makers, governments, asset managers and individual investee companies in respect of its actively managed holdings. NILGOSC recognises that many companies have begun the transition to a lower carbon world, including many companies whose traditional business models had been carbon intensive. NILGOSC is supportive of companies seeking to diversify their business into renewables and low-carbon technologies and will support calls for greater disclosure of climate change risks and robust company strategies aligned with the Paris Agreement. NILGOSC considers such action to be consistent with its fiduciary duty and is essential to achieve the goals of the Paris Agreement.

3.15. NILGOSC utilises its ownership rights globally to ensure that corporations provide accurate and timely disclosure of the material risks and opportunities associated with climate change. Through the exercise of its voting rights and through targeted engagement, NILGOSC aims to encourage companies to be transparent and accountable in respect of their impact on the environment, for example via setting targets and timeframes for the reduction of greenhouse gas emissions. NILGOSC also expects remuneration committees to consider ESG factors when setting the remuneration of company directors.

3.16. A portion of NILGOSC's assets are held passively. Passively managed funds are designed to follow an index, which means no active decision-making is undertaken when selecting stocks and therefore ESG risks cannot be taken into account. However, a decision can be made as to which index to track. Therefore, as a means of mitigating climate risk in the Fund's passive equity portfolio, NILGOSC's passive equities track the climate-tilted 'Solactive L&G Low Carbon Transition Developed Market' index. The strategy behind the index is to self-decarbonise by reducing exposure to carbon emissions over time. The index aims to reduce carbon intensity by 70% relative to the starting universe, and to reach the goal of achieving Net Zero carbon emissions by 2050, along a decarbonisation pathway of 50% at the outset and a further 7% each subsequent year.

3.17. NILGOSC encourages its real asset managers (e.g. infrastructure and property managers) to consider investment opportunities in low carbon infrastructure and real estate where appropriate. NILGOSC recognises that real assets have a greater negative sensitivity to physical damage and resource availability, and through its infrastructure investments seeks to increase its exposure to renewable assets.

3.18. NILGOSC also encourages its real asset managers to adopt sustainable asset management practices with respect to its infrastructure and property holdings and monitors their progress, at appropriate intervals.

Disclosure

3.19. NILGOSC considers the disclosure of climate risks and opportunities to be essential if shareholders are to determine whether the companies in which they invest are adequately addressing the changing climate. Improving the quality, consistency and transparency of climate-related financial disclosures will allow economies to have the necessary information to better assess the impact and effects of an organisation on climate change. NILGOSC supports calls for greater disclosure of carbon emissions and the impact of climate change on a company's business activities through the targeted exercise of its voting rights.

3.20. NILGOSC actively supports the recommendations of the TCFD, demonstrating that, alongside other supporters, it is taking action to help build a more transparent and resilient financial system through climate-related disclosure. Reporting is not mandatory for NILGOSC, but as an official supporter, NILGOSC prepares annual TCFD-aligned reports. Disclosures are organised around the TCFD's four thematic areas, representing the core elements of how organisations operate: governance; strategy; risk management; and metrics and targets; providing a framework around which to describe and communicate the steps the Fund is taking to manage climate-related risks and incorporate climate risk management into its investment process.

3.21. As a supporter of and signatory to the PRI, NILGOSC reports on its implementation of the principles via the PRI reporting framework on an annual basis.

3.22. NILGOSC also monitors stewardship data, publicly disclosing: quarterly voting records; an annual Voting Review; and a comprehensive annual Stewardship Report, prepared in compliance with the UK Stewardship Code. Principle 7 of the Code necessitates that signatories demonstrate the systematic integration of stewardship and investment (including climate change) to fulfil their responsibilities. Stewardship reports are submitted to the Financial Reporting Council (FRC), which assesses each report and if a report meets the FRC's reporting expectations, the organisation will be listed as a signatory to the Code. Once listed, organisations must continue to report annually in order to remain signatories. NILGOSC's reports are published on its website.

4. Review

4.1. This document is reviewed every three years. It will be updated sooner if required.