Investment Beliefs

Introduction

This paper is addressed to the Pension Fund Committee ("the Committee") of the City and County of Swansea Pension Fund ("the Fund"). It sets out an updated version of the Fund's Responsible Investment beliefs, originally set out in November 2017, following training and discussions with the Committee and Board at the Net Zero workshop on 26 October 2021. Our intention is that the Officers and Committee will review the draft beliefs so that these will subsequently form the basis for an updated Responsible Investment Policy that will be formally adopted by the Fund.

Background

Environmental Social and Governance ("ESG") policy

The Committee has taken steps to understand the impact of ESG issues on the Fund. In September 2019, the Committee formally set out a Statement of Responsible Investment and ESG policy. In March 2021, the Committee carried out a full review of the Fund's carbon exposure as part of its commitment to reduce the Fund's listed equity portfolio's carbon exposure to 50% of the exposure of the global stock market by 2022. This was successfully achieved a year ahead of schedule, with the Fund's listed equity portfolio having a 'carbon footprint' broadly equivalent to 42% of the MSCI AC World Index as at March 2021.

The success of the Committee in reaching its goals set the stage for further discussion on ESG and Responsible investment and the Committee and Board attending a Net Zero workshop on 26 October 2021 to discuss next steps for the Fund. Following this workshop, this paper sets out a revised set of investment beliefs which have been distilled from the discussions and decisions at the 26 October workshop.

Responsible Investment beliefs

Having a well-defined set of investment beliefs offers a number of advantages, including:

1. **Clarity on why each mandate is held and the role it performs in the Fund's arrangements** – this clarity is of benefit to the committee and the underlying members. It also offers a basis for framing communication on investment strategy which is particularly relevant where decisions are subject to public scrutiny.

2. **Prioritisation** - having identified which investment decisions are most important, advice can be sought and meetings scheduled around these key priorities.

3. **Long-term thinking** - having a set of stated beliefs, means that the committee is better able to avoid being unduly influenced by short-term market noise and in-vogue investment ideas.

4. **Consistency, both of advice and decision-making** – i.e. all decisions are reached using the same consistent framework.

5. **Continuity of understanding in decision-making** – having a decision-making framework based on a set of beliefs allows decisions to be contextualised, which is particularly valuable if there is turnover of committee members, i.e. the current committee may not "own" the decision on a certain element of the investment strategy, but as they own the framework, they can better understand why the decision was taken.

The Fund's beliefs should be revisited on a regular basis to ensure they remain appropriate. It is also important that these beliefs are reflected in the underlying portfolio of assets and in the fund's ways of working.

Fund specific beliefs

At the October 2021 Net Zero training day, a set of potential beliefs were proposed following a questionnaire exercise completed by the Committee and Officers. Reflecting the Committee's comments and discussions from that meeting, as well as the completed questionnaires, we have prepared a draft set of updated responsible investment beliefs. These are set out below:

Draft RI beliefs for consideration

Overarching ESG beliefs

Belief 1: Environmental, social and corporate governance ('ESG') issues are likely to be one of the biggest drivers of long-term performance. Part of the Committee's fiduciary duty is to ensure that the Fund is positioned to protect against related risks and seek to capture related opportunities.

Belief 2: Responsible investing is a relevant consideration and, where practical, should be assessed, monitored, and reported on, for all of the asset classes the Fund invests in.

Climate and carbon related beliefs

Belief 2: A carbon budget should be set and monitored with the aim of aligning the Fund's emissions with an Average Warming Potential and/or Implied Temperature Rise of 1.5°, and the Fund should commit to reaching Net Zero greenhouse gas emissions by 2037. The Fund's listed equity portfolio's carbon exposure should be at most 50% that of the global stock market (based on the MSCI AC World index, measured in terms of carbon emissions per $m invested).

Belief 3: Companies and other investments which actively participate in and support the climate transition are likely to do better than equivalent investments which do not. Therefore, the Fund should invest a further c30% of the portfolio (a total of c55%) in ESG-linked investments. These investments should be invested across a balanced range of climate-related solutions with a bias towards generating a positive, measurable environmental and social impact alongside a financial return. At least 15% of the portfolio should be invested in a way which directly supports the transition to a low carbon economy (e.g. by investing in companies and investments which provide alternatives to the use of fossil fuels, and/or other carbon intensive activities).

Belief 4: For some investments, the aim of reducing carbon emissions and supporting the transition to a low carbon economy may conflict with the Fund's objectives in relation to financial performance. An appropriate balance will be required between meeting the Fund's financial and climate related objectives.

Belief 5: Average portfolio exposure to green/transition supporting revenues should be at least 30% across the portfolio by 2030. This may include investing in companies whose revenues are derived from the following environmental impact themes: alternative energy, energy efficiency, green building, pollution prevention, sustainable water or sustainable agriculture.

Engagement and stewardship beliefs

Belief 6: Engagement with managers, and through them with investee companies, is important and can have a material impact on progress towards the chosen goals as well as on investment performance. The Fund should engage proactively with managers with the aim of ensuring that their approach is appropriate and effective.

Belief 7: The UN Sustainable Development goals provide a useful framework for thinking about engagement topics. The Fund's engagement activities should have a particular focus (at least initially) on: Climate Change (SDG 13), Decent Work and Economic Growth (SDG 8) and Responsible Consumption and Production (SDG 12).

Summary

This paper sets out a draft of enhanced responsible investment beliefs for the Fund. It is intended as a discussion document, to be amended / added to as the Committee sees fit. We will be happy to work with the Officers to update this draft, in light of the Committee's feedback, to prepare a finalised set of beliefs for the Fund.

We look forward to discussing this paper with the Committee at their forthcoming meeting.

Prepared by:-

David Morton, Partner
Nick Jellema, Senior Investment Consultant
Andre Ranchin, Associate Investment Consultant
Tom Prince, Investment Analyst

November 2021
For and on behalf of Hymans Robertson LLP

General Risk Warning

Please note the value of investments, and income from them, may fall as well as rise. This includes equities, government or corporate bonds, and property, whether held directly or in a pooled or collective investment vehicle. Further, investments in developing or emerging markets may be more volatile and less marketable than in mature markets. Exchange rates may also affect the value of an overseas investment. As a result, an investor may not get back the amount originally invested. Past performance is not necessarily a guide to future performance.