



Pension Fund Committee 2 November 2023

Title	Responsible Investment Update
Date of meeting	2 November 2023
Report of	Executive Director of Strategy & Resources (S151 Officer)
Wards	All
Status	Public
Urgent	No
Appendices	Appendix A – Model Portfolio 2030 Story Board
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Summary

This report provides an update on the Framework we have developed to progress our NetZero strategy.

The Framework seeks to create a 'Model NetZero' portfolio optimised on the priority of meeting a NetZero position by 2030 but in turn also generating a suitable risk /return profile. Our aim is for the actual strategy to converge towards this model portfolio once the risk / return metrics are appropriate.

This Model Portfolio approach will allow us to identify gaps and opportunities. It will also provide a means of engaging with key stakeholders as well as making robust data-driven decisions.

Recommendations

The Committee is asked to note the contents of this report and the progress made towards developing our NetZero Model Portfolio and the actions this generates for 2024.

1. Why This Report is Needed

Context

- 1.1 To help Barnet Council achieve its ambitious climate change goals, the Barnet Pension Fund has devised a strategic plan known as the 'BarNetZero 2030 Model Portfolio'. This plan outlines how the pension fund could, align its investments with climate-friendly objectives and work towards achieving a nearly zero carbon footprint by the year 2030. Initial explanation of this was provided in the Responsible Investment Paper considered at the 4 July 2023 Pension Fund Committee meeting.
- 1.2 The primary purpose of this Model Portfolio is to guide our investment decisions and understand areas where we can converge towards a 2030 strategy and areas where more work or innovation may be needed. We will use our Model Portfolio to engage with key stakeholders, such as our members, industry experts and the broader community.

A "Difficult reality"

- 1.3 It is a difficult reality that striving for a 'NetZero' pension fund strategy by 2030 presents some significant challenges:
 - **Balancing Returns and Emissions Reduction:** Pension funds, like ours, must ensure that the investments they make yield competitive returns while managing associated risks. The process of rapidly reducing carbon emissions, as necessary to achieve a NetZero status, can complicate the task of optimizing returns.
 - **Limited Investment Options:** The pool of companies expected to reach complete carbon neutrality by 2030 is relatively small (only around 20% of large companies are expected to be in the position based on analysis undertaken by a large Investment Manager). This limitation restricts our investment choices, which can potentially increase investment risks due to a lack of diversification.

Addressing these challenges

- 1.4 To gain a better understanding of these challenges and explore potential solutions, the Barnet Pension Fund commissioned its advisors to create a theoretical Model NetZero 2030 Investment Portfolio. This Model Portfolio serves as a blueprint, illustrating how we might attain NetZero by 2030, while also providing insights into the associated risks and potential returns of such a portfolio. Our objective was to identify areas where we can make changes without compromising financial stability and to pinpoint areas where we must work together with stakeholders to find viable solutions.

Key findings

- 1.5 Here are some key findings from our Model Portfolio analysis:
 - **Significant Portfolio Transformation Needed:** To achieve NetZero by 2030, we must make substantial changes to our current investment portfolio. Based on our advisors' analysis, our current investments alone would not come close to reaching NetZero by 2050, let alone 2030.
 - **Exploring Offsetting Assets:** Our advisors have suggested one potential solution for reaching NetZero by 2030 is by investing in 'offsetting' assets. These are investments that inherently contribute to carbon reduction. Examples include investments in Timberland (which is an asset class where you grow trees and sustainably farm those trees for building materials) or technologies that reduce reliance on fossil fuels.

- 1.6 Our Model Portfolio combines an approach which would first reduce the carbon footprint in our core investments (i.e. our equities, bonds and property), aligning them with the goals set by the 2015 Paris Agreement*. We believe this can be achieved without taking on excessive risks. It then subsequently sets an approach where we would allocate a portion of our investments to 'offsetting' assets to neutralize any remaining carbon emissions generated by our portfolio.

What Does This Mean in Practice?

- 1.7 To translate these ideas into practical terms, we need to assess our current carbon emissions and determine what changes are required in both our core investments and offsetting assets to achieve a NetZero position.
- 1.8 Our advisors estimate that our current investments are responsible for approximately 325,000 tons of CO2 emissions. At the current rate, these emissions would not reach zero by 2050. However, if we allocate 80% of our core assets to 'Paris Aligned' funds*, which are expected to emit a reduced amount of 100, 000 to 150,000 tons of CO2 by 2030, we could then invest the remaining 20% in assets that actively reduce emissions to offset this (note data is approximate to give a sense of magnitude)0.
- 1.9 This approach would, in theory, allow us to achieve a net carbon position of zero – there's more work to be done on this, for example, the Fund does not currently invest in 'offsetting assets' and so the Pension Fund Committee would need to get very comfortable about its risk and return characteristic towards making an investment towards such assets.
- 1.10 Given the above, we will be exploring opportunities to move to Paris Aligned Funds and Offsetting Asset Funds through 2024.
- 1.11 Officers can share underlying reports provided by Hymans to Pension Fund Committee members for information on request.
- 1.12 The Appendix provides a "Story Board" setting out our broad strategy for considering Climate Change within the Pension Fund, which we will use to engage stakeholders.

Summary

- 1.13 In summary, we are actively working on how we can reshape our investment portfolio to combat climate change. We have identified ways to do so without unduly jeopardizing our financial stability and will continue to engage with stakeholders to refine our approach.
- 1.14 Our current portfolio and Model Portfolio are set out on the next page. We will share these with people within the Industry so they can challenge us and offer solutions which may make the Model Portfolio work better. We will look to review the Model Portfolio annually and will provide an annual update on progress toward converging towards the portfolio, and if we can't converge, the reasons why.
- 1.15 This paper will be developed into a broader article / thought piece to share with interested stakeholders.

Model Portfolio

1.16 A summary of our Current and NetZero Model Portfolio is provided in the table below.

	Current	Model
Core - Growth	30%	0%
Core - Growth Paris Aligned	0%	24%
Core - Income	70%	0%
Core - Income Paris Aligned	0%	56%
Offsetting	0%	20%
Expected Return (20 years relative to cash)	3.7% p.a.	3.7% p.a.
Variance (1 year)	12.10%	12.80%
Emissions (2030)**	225 KtCO2	0 (NetZero)
Emissions (2050)**	100 KtCO2	-33 KtCO2

**The Paris Agreement is an international treaty adopted in 2015 at the 21st Conference of the Parties (COP21) to the United Nations Framework Convention on Climate Change (UNFCCC). Its primary goal is to combat climate change by limiting global warming to well below 2 degrees Celsius (3.6 degrees Fahrenheit) above pre-industrial levels, with an ambition to limit it to 1.5 degrees Celsius.*

Each participating country submits a Nationally Determined Contribution (NDC) outlining their emissions reduction targets and strategies. Transparency and reporting mechanisms are in place to track progress and hold nations accountable.

The agreement emphasizes adaptation to climate change impacts, particularly for vulnerable regions, and encourages developed nations to provide financial support to developing countries for mitigation and adaptation efforts.

***Note that data is indicative and approximate to give sense of scale and likely trajectory*

2. Alternative Options Considered and Not Recommended

2.1 Taking no action means that the Pension Fund's NetZero position would not be aligned to the Council's wider ambitions around NetZero and would mean that the Pension Fund would not be on track to be in a NetZero position by 2050.

3. Post Decision Implementation

3.1 Broad Next Steps are summarised below:

Current	Next Step	Target convergence date
Equity	Explore RAFI and LCIV alternatives	2024
Fixed Income	Review current portfolio	2024
Securitised Assets	Consider redeployment as current assets mature	Rolling to 2030 as asset classes mature
Property	Defer consideration to 2025	TBD (likely 2025 plus)
Infrastructure	Explore Timberland as asset class (decision on allocation 2024) Explore Expanding RI Explore Green Tech	Partial Transition 2024

4. Corporate Priorities, Performance and Other Considerations

Corporate Plan

- 4.1 The Pension Fund Committee supports the delivery of the Council's strategic objectives and priorities as expressed through the Corporate Plan, by careful monitoring of the Pension Fund activities with a view to ensuring the overall sustainability of the Pension Fund.
- 4.2 Sustainability of the Pension Fund is a crucial pillar in allowing the council to fulfil its wider objectives.
- 4.3 The Pension Fund is also developing its NetZero and Stewardship policies which feed into the wider objectives around Planet, Places and People.

Corporate Performance / Outcome Measures

- 4.4 Not applicable in the context of this report.

Sustainability

- 4.5 Model Portfolio supports the Council's wider objectives around reaching a NetZero position by 2030.

Corporate Parenting

- 4.6 Not applicable in the context of this report.

Risk Management

4.7 Risk management is central to the LGPS. LGPS pension funds are in themselves risk management tools, managing the risk that future employer income streams will be able to meet future pensions liabilities by creating a reserve from which future liabilities will be met. Good governance is essential to managing the risks of the pension fund.

Insight

4.8 This work has been supported by advice from Hymans who have supported forecasts on Carbon Emissions and means of reducing and offsetting this in a sustainable way.

Social Value

4.9 Not applicable in the context of this report.

5. Resource Implications (Finance and Value for Money, Procurement, Staffing, IT and Property)

5.1 Risks that are not mitigated or managed can have a financial penalty to the Fund.

6. Legal Implications and Constitution References

6.1 The Council's Constitution – Part 2B section 15 includes within the responsibilities of the Pension Fund Committee.

6.2 The terms of reference for the committee includes:

- "To have responsibility for all aspects of the governance, investment and administration of the LB Barnet Pension fund, including, but not limited to the following:
- To ensure compliance with all Local Government Pension Scheme statutes, regulations and best practice."

7. Consultation

7.1 Not applicable in the context of this report.

8. Equalities and Diversity

8.1 Pursuant to the Equalities Act 2010, the Council is under an obligation to have due regard to eliminating unlawful discrimination, harassment, victimisation and any other conduct that is prohibited by or under the Act; advancing equality of opportunity between persons who share a relevant 'protected characteristic' and those who do not share it; and fostering good relations between persons who share a relevant 'protected characteristic' and persons who do not share it. The 'protected characteristics' are: age, disability, gender reassignment, pregnancy, and maternity, race, religion or belief, sex and sexual orientation, marriage and civil partnership.

8.2 The rules governing admission to and participation in the Pension Fund are in keeping with the public sector equality duty. The [Public Sector Equality Duty](#) requires public authorities in carrying out their functions, to have due regard to the need to achieve the objectives set out under s149 of the Equality Act 2010. Good governance arrangements will benefit everyone who contributes to the fund.

9. Background Papers

9.1 Further discussion on the Fund's Responsible Investment approach can be accessed from the following links:

Pension Fund Committee – 31 January 2023 – Developing the Fund's Responsible Investment Strategy - update

[Developing the Funds Responsible Investment strategy - update.pdf \(moderngov.co.uk\)](#)

Pension Fund Committee – 4 July 2023 – Responsible Investment Update

[230704 Responsible Investment Update - Cleared.pdf \(moderngov.co.uk\)](#)