YORKSHIRE AND CLYDESDALE BANK PENSION SCHEME

Trustee's Report in respect of the Occupational Pension Schemes (Climate Change Governance and Reporting) Regulations 2021

In respect of the Scheme year ending 30th September 2023

2023 Scheme Climate Change Report

March 2024

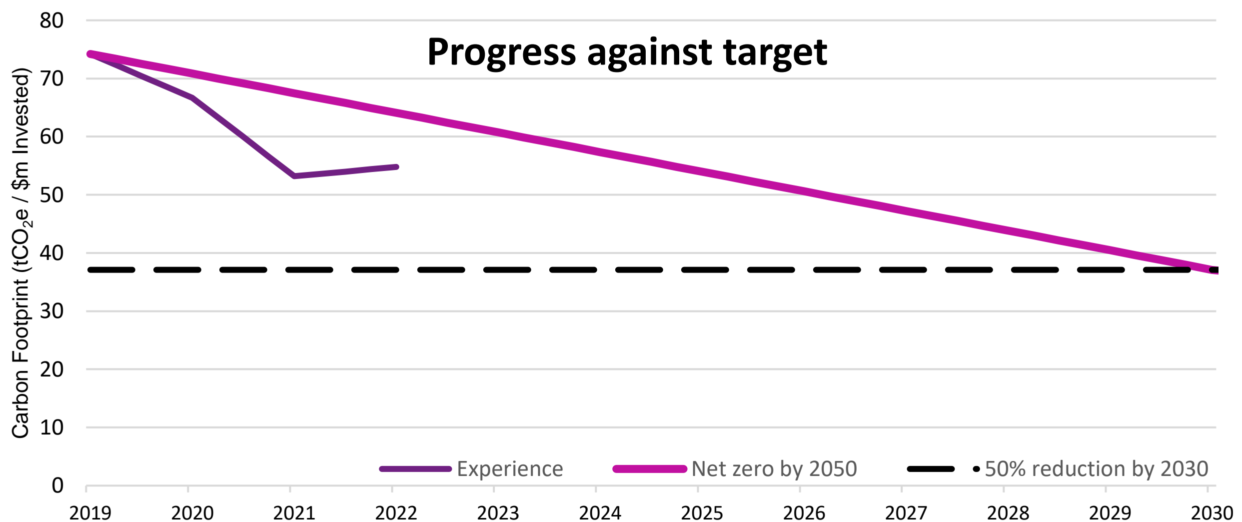
Chairperson's Letter

A word from the Chairperson of the Yorkshire and Clydesdale Bank Pension Scheme trustees

On behalf of the Yorkshire and Clydesdale Pension Scheme, we are pleased to present the first Climate Change report. This report is an accumulation of work undertaken by the Trustee over recent years in the area of climate change and the management of climate-related risks and opportunities.

The Trustee believes that climate-related risks could have a material impact on the Scheme, and as such believes it is its fiduciary responsibility to manage these risks. The Scheme has made very strong progress over the past few years with improvements to the funding position allowing the Trustee to reduce the Scheme's overall risk exposure, including to climate-related risks.

Throughout this report we detail the steps that the Trustee has taken to allow it to monitor and manage climate-related risks appropriately. These include the governance structure that the Trustee has put in place, the work that has been undertaken in order to assess the risks and the actions required to mitigate them. The Trustee has adopted a range of climate metrics to help it measure the Scheme's exposure to climate change and to monitor how the associated risk changes through time. The Trustee has also set a target of reducing the carbon footprint of its portfolio to net zero by 2050, with a 50% reduction by 2030. The Scheme has made strong progress towards meeting this target already, as demonstrated in the chart below.



Reporting on climate change in the investment industry is a relatively recent development. Whilst data availability will continue to improve, there are limitations in the availability, consistency and quality of the information reported by companies and investment managers. The Trustee expects that over time the quality of the data will improve as will its availability and the Trustee continues to encourage both its advisors and investment managers to push for improvements.

Although the Trustee has made significant progress in recent years through the enhancements made to the Scheme's governance and risk management processes to manage against climate risks, the Trustee will continue to seek opportunities to improve the Scheme's position, including assessing the merits of changes to its investment strategy, the specific mandates with its managers or through engagement with the underlying companies invested in (directed by its investment managers). The Trustee remains mindful that climate-related risks, whilst material, are just some of the risks facing the Scheme and it looks to take a balanced approach to managing these risks. The Trustee recognises also that its ability to achieve its targets, and to manage climate-related risks more generally, are reliant on the actions taken by other stakeholders, including governments, regulators, companies and consumers, and the Trustee encourages its advisors and investment managers to work with relevant parties to continue to press for the changes needed.

The Trustee looks forward to sharing progress over the coming years.

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Introduction

The Yorkshire and Clydesdale Bank Pension Scheme ("the Scheme") is managed by the Yorkshire and Clydesdale Bank Pension Scheme Trustee Limited ("the Trustee"). The Scheme is a defined benefit pension scheme with assets of around £2.8bn as at the Scheme's year end, 30 September 2023. In addition to the defined benefit element, the Scheme also holds relatively small investments in relation to Additional Voluntary Contributions ("AVCs") made by members, totaling around £4m at the same date. Given the relative size of these AVCs, the focus of this report is on the defined benefit assets and liabilities.

The Trustee is pleased to issue its first Climate Change Report. The Scheme is subject to the requirement to produce disclosures in line with the recommendations of the Task Force on Climate-Related Financial Disclosures ("TCFD"), as set out in the Occupational Pension Schemes (Climate Change Governance and Reporting) Regulations 2023. The aim is to improve and increase the reporting of, and hence the attention paid to, climate-related financial risks and opportunities.

The Trustee is supportive of the aim of the TCFD and believes that part of its fiduciary responsibility is to manage climate-related risks and opportunities within the Scheme's investment portfolio.

The TCFD framework requires disclosures in four broad categories:

- **Governance:** around climate-related risks and opportunities
- **Strategy:** the actual and potential impact of climate-related risks and opportunities on the strategy and financial plans of the Scheme
- **Risk management:** how the Trustee identifies, assesses, and manages climate-related risks
- **Metrics and targets:** the metrics and targets used to assess and manage climate-related risks and opportunities

This Climate Change Report sets out the Scheme's approach to compliance in each of these four categories for the **year ending 30 September 2023.**

Section 1 - Governance

1.1 Trustee's oversight of climate-related risks and opportunities

This section describes the governance in place to facilitate the identification, assessment and management of climate-related risks and opportunities which are relevant to the Scheme.

The Trustee has ultimate responsibility for the management of the Scheme, but it also has a number of sub-committees with delegated decision-making powers. The Investment Sub-Committee (the "ISC") has delegated responsibilities relating to investment matters, including climate-change related considerations. The Trustee, however, retains responsibility for setting appropriate frameworks and for key strategic decisions such as the Scheme's net zero target and the metrics adopted for the measurement of climate-related risks, as detailed later in this report, and the exclusions policy as communicated to the investment managers.

The ISC typically meets eight times a year, with the Trustee Board meeting at least four times a year. As part of these meetings the Trustee and ISC have, over 2022 and 2023, received training on a range of sustainable investment-related matters, including on the findings of the TCFD, the requirements on trustees to report on pension scheme exposures, the different metrics which can be used for assessing climate change-related exposures and on possible frameworks for managing these risks.

Trustee beliefs and policies with respect to Sustainable Investment

The Trustee's policies in relation to Sustainable Investment ("SI") matters are detailed in the Scheme's Statement of Investment Principles (the "SIP"). In addition to this document, the Trustee prepared, in May 2023, a Sustainable Investment Policy which outlines the Trustee's beliefs with regards to sustainable investment and how it expects to manage risks and opportunities.

The following statements are a summary of the Trustee's approach and beliefs with regards to sustainable investing:

- Sustainable investment, including Environmental, Social and Governance (ESG) issues, can have a material impact on the returns achieved from the Scheme's assets, and is best considered as part of a broader risk management framework and the Scheme's Journey Plan;

- The Scheme's investment managers are best placed to take decisions on the sustainability of the Scheme's underlying investments and to take action on the Scheme's behalf, whilst the Trustee focus is on monitoring their processes and managing any outsized risks at a total Scheme level;

- The SI Policy explicitly recognises that the Trustee's primary focus within sustainable investing is on risks and opportunities relating to climate change; and

- The Scheme has applied an exclusions policy on new purchases within the portfolio's Buy-and-Maintain credit allocation. This exclusions policy excludes issuers that have any tie to controversial weapons, have failed to comply with UN Global Compact or derive more than 20% of revenue from thermal coal, thermal coal power generation or oil sands.

1.2 Management's role in assessing and managing risks and opportunities

As noted above, both the Trustee Board and the ISC (together "Management") have specific roles in the assessment and management of climate-related risks and opportunities. The ISC is responsible for the

detailed monitoring of the Scheme's exposures and working with the investment advisor and the Scheme's investment managers to ensure the Trustee's policies are implemented, while the Trustee Board receives summary information on a regular basis and retains responsibility for setting the strategic policies and framework.

The ISC is also responsible for the appointment and review of the Scheme's investment managers. As part of this process the ISC considers the approach taken by these investment managers in relation to sustainable investment matters. The ISC recognises that climate change may impact on different asset classes in different ways and also needs to balance the approach to managing the risks associated with climate change with the other risks facing the Scheme and the Trustee's wider fiduciary duties.

The ISC is responsible for challenging the climate risk analysis that is provided; this is done by challenging methodology during meetings and discussing the relevance to the Scheme. Over the year members of the ISC also attended an out-of-cycle meeting with abrdn speficially to discuss their climate scenario analysis, as initially the results were not aligned with the ISC's expectations.

Whilst consideration of climate-related risks is a key priority for the Trustee, it recognises that there are also other material financial risks facing the Scheme. The Trustee therefore seeks to find the right balance between managing climate-related risks and spending sufficient time discussing the other material risks. Over the year, the ISC discussed climate-related topics 5 times across 8 meetings.

The ISC receives regular training from its investment advisor across a wide range of climate-related risks, for example the climate scenario analysis undertaken every three years (discussed in more detail later in this paper) which demonstrates both the risks and opportunities caused by climate-related risks.

The role of Investment Managers

The Trustee delegates the day-to-day decision-making to the Scheme's investment managers who act on behalf of the Trustee. The Trustee believes the investment managers are best placed to assess the risks and opportunities available to them, subject to the nature of their mandate. The ISC assesses the managers' approach to managing climate-related risks, and other risks, when appointing the managers. In addition to asking those investment managers to assess whether their policies, including those relating to voting and engagement activities, are in line with the policies set out in both the SI Policy and the SIP, the ISC also reviews reporting from its investment managers on their activities and meets with managers of segregated holdings on an annual basis.

Other Parties

Scheme-wide decision making, consideration of climate-related risks and opportunities and the review of the SIP is undertaken with advice from the advisors listed below:

- **Investment advisor (WTW)** helps the Trustee to formulate investment beliefs and to reflect these in the Trustee's investment policies and strategy. The investment advisor also helps the Trustee with conducting scenario analysis, advises on how climate-related risks and opportunities might affect the Scheme over the short, medium and long term and provides ad hoc specialist advice on a variety of pension matters, including risk management. The investment advisor is also responsible for providing the Trustee with advice on potential investment opportunities, assessments of the Scheme's investment managers and reporting on the climate-related metrics for the Scheme.

- **Actuarial advisor (WTW)** performs valuations of the Scheme's liabilities and advises on how climate-related risks and opportunities might affect the Scheme's liabilities over the short, medium, and long term. The actuarial advisor's understanding of the Scheme's membership profile and the sensitivity of the Scheme's liabilities to changes in economic conditions means it can more easily incorporate the impacts of climate change into its assumptions as compared to any other party involved in advising the Scheme.

- **Other:** The Trustee also receives input and advice from its covenant advisor, legal advisor and the Scheme Sponsor (Clydesdale Bank PLC). These parties assist the Trustee in ensuring that all relevant considerations are taken into account in the Trustee's decision-making.

The Trustee retains responsibility for ensuring that its advisors have the experience and knowledge required to support the Trustee in considering climate-related risks and opportunities. The ISC has reviewed the credentials of its investment advisor and determined that they have the expertise required.

Where appropriate, the Trustee sets out the objectives for its advisors and reviews performance relative to this. For example, the Trustee has set an explicit requirement for its investment advisor to reflect the Trustee's views in relation to ESG matters in any advice provided, and this objective is assessed annually.

Section 2 - Strategy

2.1 Identification and assessment of climate-related risks and opportunities relevant to the Plans

The Trustee believes that part of its fiduciary duty is to manage climate-related risks and opportunities within the Scheme's investment portfolio. Climate change is a financially material consideration that will have significant influence on the future success of companies and their ability to service debt, and on security of cashflows and asset values. As such, climate-related risks impact all investment strategies and mandates, across both long and short-term horizons.

Due to the strength of the Scheme's funding position, the investment strategy has evolved over the past few years to focus on longer-dated, cashflow-generative assets that better match its liability cashflows. Climate-related risk considerations have influenced both this choice of strategy and the implementation of the strategy, with a key factor being the security of the cashflows generated by the assets.

When assessing risk to the funding and investment strategy, the Trustee considers risks holistically in the context of liabilities, assets, covenant and members. The ISC considers two major categories for climate-related risks and opportunities defined by the TCFD to be financially material for the Scheme, namely, risks and opportunities related to the physical impact of climate change and risks and opportunities related to the transition to a lower-carbon economy.

- **Physical risks**: Physical risks relate to the direct effects of climate change on the Scheme and its members. These risks would be expected to impact the Scheme increasingly in the longer term if global average temperatures continue to rise. These could have varying effects on the funding and investment strategy of the Scheme, but the direction and size of the effects is unlikely to be clear for a considerable period of time. Physical risks are expected to have a more significant impact in the longer term.

- **Transition risks**: Transition risks are an indirect impact of climate change, relating to the risks and opportunities arising from efforts made to transition towards a net-zero economy (both domestically and globally) in order to limit climate change. These risks and opportunities are generally expected to occur in the short to medium term.

Short, medium and long-term impact

The Trustee has considered the impact of the climate change on the Scheme's funding position over the short, medium and long term:

Short (1 year): The Scheme is potentially exposed to climate-related shocks in the short-term, with these expected to result primarily from transition-related impacts. Whilst the funding position is believed to be strong enough to allow the Scheme to absorb these shocks and still pay member benefits in full, the size of the modelled shocks themselves is still material. As detailed in the risk management section of this report, the Trustee has taken actions to reduce the risk facing the Scheme, both through reducing its exposure to more volatile asset classes such as equities and through entering a longevity swap, to help mitigate these risks. The Trustee will continue to explore opportunities to manage short-term risk, whilst noting the need to balance climate-related risks with other risks facing the Scheme and the Trustee's wider fiduciary responsibilities.

Medium (to 2031): In the medium term the Trustee's primary strategic objective is to be fully funded on the low-dependency basis by 2031. The projections of the funding level at this point in 2031 show that, whilst the funding position could be detrimentally impacted by climate change (due primarily to transition risk), this objective would still be achieved under all the scenarios modelled (see below) and thus the investment and funding strategy adopted to achieve the objective is believed to be robust to the climate

risks faced. This conclusion is a result of the strength of the current funding position and the low-risk nature of the Scheme's portfolio. The Trustee recognizes, however, that the impact of climate change may be greater than assumed in its analysis and will continue to monitor this.

Long (beyond 2031): Over the longer term the Trustee expects the Scheme to be less exposed to climate change risks, particularly physical risks which are more likely to manifest in the long term. This assessment on the long-term risks is due to the time horizon of the Scheme, with the expectation that the Scheme will be very de-risked, including potential settlement of the liabilities with an insurer, as it moves into the next decade. As noted however, longer-term climate outcomes could still impact the Scheme through early pricing in financial markets.

Covenant Impact

A comprehensive risk management approach requires that the Scheme's covenant risk is assessed alongside the asset and liability risks. The ISC discussed the potential impact of each scenario on the Bank when considering the scenario analysis, addressing the possible outcome for default levels, real asset values, regulations and levels of borrowing. Overall, the ISC saw no reason to be concerned about the strength of the covenant in any of the scenarios, in particular considering the reduced reliance on the covenant owing to the strength of the funding position.

2.2 The impact of climate-related risks and opportunities on the Scheme

Using the scenario analysis and the resulting discussions, the Trustee has identified the key climate-related risks and opportunities that face the Scheme. These are summarised below, alongside some of the mitigating actions that the Scheme has taken to reduce these key risks.

Risks	• Given the time horizon and the credit-focused asset allocation, the main risks on the asset side are the costs of transition. • Climate change may also be a material source of longevity risk, which would impact on the total value of the benefits expected to be paid to members.
Opportunities	• Finance required for transition will open opportunities in credit, for example through green bonds, or investments in companies which are expected to benefit from climate change. • Impact investments may be made and the Scheme has taken advantage of opportunities already, such as through the BlackRock Renewable Power Fund and the Greencoat Solar and Alpha Real Wind funds.
Mitigating Actions	• The Scheme's corporate bond managers are required to take sustainable investment matters into consideration when determining which bonds to purchase. • The Trustee expects its managers to engage with the underlying companies being invested in to manage climate-related risks, and monitors the actions being taken by those managers. • The Scheme has made exclusions (applied to new purchases) within the Buy-and-Maintain credit portfolios, with some of these exclusions applying to climate-unfriendly industries. • The Scheme has already implemented some longevity hedging to reduce the impact of longevity volatility.

	• The Scheme has made investments into a number of renewable energy mandates, including infrastructure construction through the BlackRock mandate.

2.3 Describe the resilience of the organisation's strategy, taking into consideration different climate-related scenarios including a 2°C scenario

The Trustee is required, as far as it is able, to undertake hypothetical scenario analysis which considers the potential impact on the Scheme's assets and liabilities of the effects of a global average increase in temperature and of any steps which might be taken (by governments or otherwise) because of such an increase in temperature. The aim of this is to assess the potential resilience of the Scheme's investment and funding strategy to these scenarios. The Regulations require that, in at least one of those scenarios, the global average temperature increase be within the range of 1.5 degrees Celsius to 2 degrees Celsius above pre-industrial levels.

Through 2023, the Trustee has carried out climate change scenario analysis in partnership with its investment and actuarial advisors. The aim of this analysis was to help the Trustee to assess the potential effects of climate change on the Scheme's assets, liabilities and covenant.

The Trustee considered four separate scenarios which are in part defined through their success, or otherwise, in meeting the Paris Agreement target of a sub-2.0ºC temperature rise. The scenarios differ in the size of the physical risks, based on the resulting temperature impacts, but also in the size of the transition risks. For example, the Climate Emergency scenario, where decisive action is taken, and the Inevitable Policy Response scenario, where transition is more disorderly due to delays in meaningful action, represent bigger transition risks than the Global Coordinated Action scenario, which reflects a more managed response to tackling climate change.

The Trustee recognises that there is a great deal of uncertainty around the assumptions used, and the expected outcome, under each of the scenarios. The scenario analysis is designed to help the Trustee understand the potential magnitude of the climate risk faced by the Scheme but results from the analysis are highly dependent on the assumptions used. The Trustee has therefore drawn conclusions from the analysis undertaken whilst recognising that financial impacts may be greater than indicated, and has requested that the investment advisor continues to develop and refine the scenario analysis as the risks become better understood through time.

The Trustee's focus for this analysis is on the potential impact of climate change over the next 10 to 15 years. This is because the Trustee might explore settling the Scheme's liabilities with an insurance company within this period.

The Trustee understands that the advisors made a series of simplifying assumptions to shield the analysis from being obscured by other factors. The key assumptions were as follows:

- The investment strategy in place over the projection period is the strategic asset allocation as at the date of the analysis. Whilst recognising that any de-risking over the period might be expected to result in better outcomes than shown, this approach allows the Trustee to consider the risks associated with the current investments and to compare with alternative strategies.
- No change is made to the level of prudence assumed in the liability discount rate relative to the yield on government bonds.

- The impact of climate change is time-dependent, with transition risk being front-loaded over the first 10 years, and physical risk following over the remainder of the projection period (up to 20 years).
- Gilts will not be materially impacted by climate risk over the short- to medium-term
- Liability impacts are incurred over a 15 year period.
- The analysis is undertaken at asset class level, and no allowance has been made for the specific holdings in the Scheme's portfolio.

The table below summarises the climate scenarios used in the Scheme's scenario analysis:

	Lowest Common Denominator	**Inevitable Policy Response**	**Global Coordinated Action**	**Climate Emergency**
Description	A 'business as usual' scenario where current policies continue with no further attempt to incentivise further emission reductions.	A delay in meaningful action but a rapid shift in policy in the mid/late 2020s. Policies are implemented but not in a completely co-ordinated manner.	Policy makers agree on and immediately implement policies to reduce emissions in a globally co-ordinated manner.	An immediate, ambitious and co-ordinated response in which an aggressive policy is pursued and more extensive technology shifts are achieved.
Temperature rise vs pre-industrial levels	~3.5°C	~2.0°C	~2.0°C	~1.5°C
Renewable energy by 2050	30-40%	80-85%	65-70%	80-85%
Transition risk level (shorter term)	Low	High	Low – Medium	Medium – High
Physical risk level (longer term)	High	Low – Medium	Low	Low

The impact of the climate scenarios was assessed both as an instantaneous shock to the Scheme's balance sheet and as an annual impact on the funding level through time as climate impacts emerge. This was done in recognition of the fact that the timing of climate change impacts on asset values is uncertain, with markets able to price in future outcomes once they are expected. It is therefore possible that the Scheme's assets might reduce in value in the short term due to climate impacts expected further in the future.

The results of the analysis are summarised in the table below:

	Projected low-dependency funding level in 2031	Funding level post instantaneous shock
Base case	106.7%	99.0%
Lowest Common Denominator	108.2%	99.1%
Inevitable Policy Response	105.4%	93.9%
Global Coordinated Action	105.2%	95.5%
Climate Emergency	104.7%	94.4%

Asset Impacts

The analysis suggests that transition risks are likely to be more costly to the Scheme than physical risks.

This is in part due to the Scheme's debt-based allocation which exposes it to more transition risk than physical risk because transition is potentially a bigger driver of defaults. It is also in part due to the time horizon for this analysis, with the possibility of exploring settlement of the liabilities with an insurance company with the next 10 to 15 years. The analysis found that a climate emergency and the inevitable policy response delivered the worst outcomes from a financial perspective due to their more disruptive transitions.

The asset class with the greatest contribution to the Scheme's climate risk is the corporate bond holdings, which is the area of the portfolio where the Trustee directs most focus in managing climate risks. Due to the strategy adopted, defaults in the corporate bond portfolio are a key risk to the Scheme and climate risk could be a cause of defaults.

Liability Impacts

For each scenario the potential impact on the life expectancy of Scheme members was assessed, with poor physical outcomes due to climate change assumed to reduce the rate of future life expectancy improvements. It is also assumed that there can be benefits to transition, such as cleaner air, that could increase the rate of improvement in future life expectancy. The analysis translates these assumed life expectancy impacts within each scenario into an impact on the value of the Scheme's liabilities. The change in value of the Scheme's liabilities shown are net of the longevity hedging that the Scheme implemented over the course of 2023, which reduces the risk of climate change to the funding position.

The Trustee notes that, while the modelling suggests that there may be a funding level improvement from higher temperature increases due to the negative impact on life expectancies, the assessment of what is in the best interests of the Scheme and its members is a much broader subject than simply looking at the funding level. A key consideration for the Trustee is the quality (and length) of members' lives and the environment into which they will retire.

Scenario impacts

The scenario in which the Scheme's assets would be most impacted is the Inevitable Policy Response. In this scenario policy actions are taken to limit temperature rises to around 2.0ºC, but decisions are delayed and not co-ordinated. As a result the actions required are greater than if decisions had been made earlier,

resulting in higher transition costs, with the Scheme's real estate and corporate bond holdings in particular seeing losses relative to the base case. The Scheme's secure income assets (and renewable energy investments in particular) are projected to increase in value under such a scenario. Any asset value losses are, however, assumed to be offset in part by longevity improvements being lower than in the base case.

The Global Co-ordinated Action scenario anticipates a similar increase in temperatures to the Inevitable Policy Response scenario, but with policy actions taken much earlier. This results in the actions required to achieve this temperature rise having a smaller impact on the global economy and on companies' profits (and their ability to meet debt repayments), with corresponding reductions in the potential impact of climate change on asset returns. Longevity improvements are assumed to be better than in the base case because of the positive implications of managing the increase in temperature rises while doing so in a co-ordinated and measured fashion.

The Lowest Common Denominator scenario is projected to see returns on all asset classes lower than under the base case. The reduction in corporate bond valuations is assumed to be lower than in any of the other scenarios over the projection period. The Scheme's illiquid asset holdings (such as property and other secure income investments) are assumed to see lower returns than in any other scenario. Whilst in this scenario assets might be expected to be most impacted by physical risks, when this outcome is assessed in the context of the Trustee's time horizon and any possible settlement of the liabilities with an insurer, the overall impact is likely to be less pronounced. A key risk here is, therefore, that these physical risks emerge much earlier than assumed. It is also assumed that longevity improvements would be lowest under this scenario, which would be beneficial for the Scheme's funding position (although not for the health of the Scheme's members or wider society).

Finally, under a climate emergency scenario in which strong actions are taken quickly and temperature rises limited, there would be significant levels of transition risk, similar to the Global Co-ordinated Action scenario. Corporate bonds would again be the most impacted with renewable energy assets benefitting (through rises in valuations). Longevity improvements are assumed to be broadly in line with the base case, with the positive impacts of limiting temperature rises offset by the cost of implementing the policy changes necessary and the impact this is assumed to have on global economic growth.

Section 3 - Risk Management

3.1 Processes for identifying and assessing climate risks

The Trustee views climate change as a risk which cuts across the majority of the other risks faced by the Scheme, in that those risks may all be changed, mitigated or worsened by the effects of climate change.

Whilst the Trustee retains ultimate responsibility for the management of climate-related risks, and receives summary reporting on the Scheme's exposures and the actions being taken by managers, the Trustee has delegated responsibility for the appointment and monitoring of managers and for the detailed review of the Scheme's exposures to the ISC, as supported by the Trustee's advisors.

The ISC's priorities for managing climate-related risks have focused on those areas of the portfolio that are most exposed, as highlighted from the scenario analysis undertaken and analysis of the Scheme's metrics. In particular, the Scheme's Buy-and-Maintain credit portfolio is a major source of climate-related risks. The two credit managers are invited to meet with the ISC on an annual basis and sustainablity is always a topic that they are asked to present on.

The Trustee reviews its risk register at each meeting taking into account views on new and existing risks from its members, sub-committees and advisors. The Trustee has an Audit and Risk Sub-Committee which has responsibility for reporting to the Trustee on any issues which might arise.

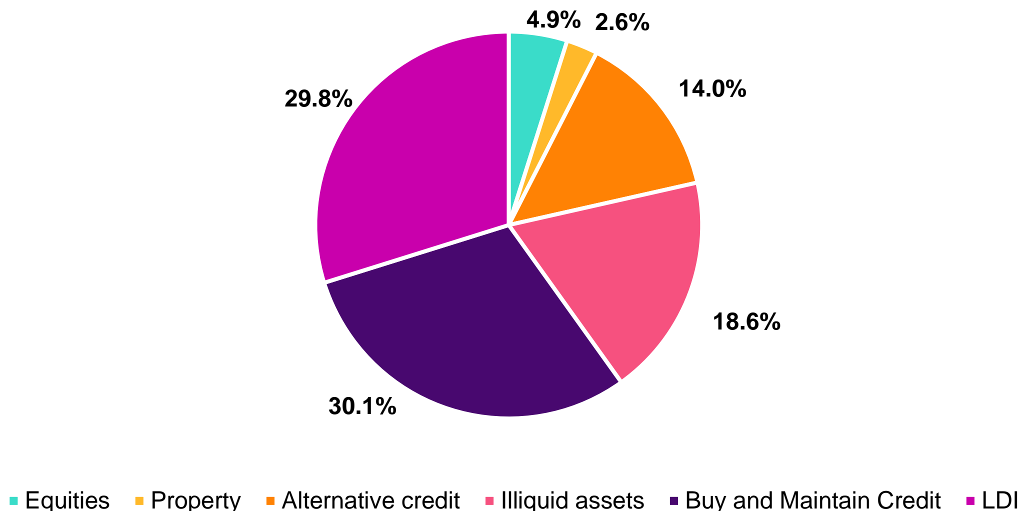
The Trustee also has responsibility for ensuring that the Trustee's advisors have appropriate levels of experience and knowledge to support the Trustee, and for assessing those advisors to ensure that they take account of the Trustee's approach to climate-related risks and opportunities in the advice being given. The Trustee has reviewed the credentials of its investment advisor and undertakes an annual assessment of the performance of its investment advisor, including consideration of the quality and appropriateness of climate-related advice received.

The Trustee and ISC have received training on the management of climate-related risks and opportunities, including on metrics which can be used to understand the Scheme's climate-related risks and exposures better. The Trustee has agreed the metrics to be used and the overarching policies and framework to be used for the management of risk, as documented in the SIP and SI policy.

The Trustee's policy is to delegate to its investment managers responsibility for stewardship activities such as the exercise of rights attaching to investments, including voting rights, and engagement with issuers of debt and equity and other relevant persons about relevant matters including sustainable investment considerations. The Trustee expects that, where appropriate, investment managers cast votes on its behalf in a manner that is consistent with the agreements of the relationship and the Scheme's SIP and SI Policy. These votes and examples of engagement undertaken on the Trustee's behalf are documented on an annual basis as part of the Scheme's Implementation Statement.

The scenario analysis undertaken by the Trustee, mentioned in the previous section, provides the Trustee with a holistic overview of the ways in which climate change may affect the Scheme's funding and investment positions. The Trustee can consider this at overall Scheme level or can look at individual asset classes.

The below chart illustrates the Scheme's asset allocation as at 30 September 2022:



The Trustee has materially de-risked the Scheme's portfolio over recent years, due to the strength of the funding position. As such, the Buy-and-Maintain credit investments now form a significant portion of the assets held. Corporate bonds are therefore an important asset class to the strategy and, as per the scenario analysis, potentially the greatest source of climate-related risk to the Scheme. However; the analysis is based on considering the potential impact of the scenarios on the asset classes (equities, corporate bonds etc) invested in rather than the specific allocations held by the Scheme's investment managers at a point in time. Actions the Scheme's investment managers take to limit exposure to transition-related defaults and downgrades in the bond portfolio will improve outcomes. To this end, the Trustee adopted and implemented an exclusions policy over 2023 that applies to any new bonds to be bought in the Buy-and-Maintain credit mandates. This policy prevents the managers buying new bonds that meet certain criteria around exposure to controversial weapons, thermal coal and oil sands and failure to comply with the UN Global Compact. This policy is intended to reduce climate risk alongside other sustainable investment-related risks.

3.2 Risk management process

In order to manage the Scheme's climate risks, the Trustee has also developed the structure for a "Carbon Journey Plan", which the Trustee believes will act as a tool in helping the Scheme to meet its ultimate net zero goals, and lead to effective decision-making along the way. The Trustee has also established a suitable governance structure for the Carbon Journey Plan, which is ultimately owned by the Trustee but incorporated into the ISC's activities.

The Trustee will use the Carbon Journey Plan to monitor changes in the Carbon footprint (or 'emissions intensity' – see the next section for further details) over time, assessing these against its agreed target of reaching net zero by 2050 and an interim target of a 50% reduction by 2030, starting with a baseline of 30 September 2019.

There are a number of ways in which the Trustee is aiming to achieve these targets, all of which will be considered by the ISC and wider Trustee Board in the years ahead. These include:

1. **Engagement** – The Trustee acknowledges that one way to reduce emissions is through changing the behaviour of the companies invested in, and believes that this can best be achieved through engagement. The ISC will continue to engage with managers of key mandates and expects managers to do the same with underlying companies. Given the proportion of the

Scheme's assets invested in Buy-and-Maintain corporate bonds the ISC looks to meet with its two Buy-and-Maintain managers annually to understand their performance and their approach to investing the Scheme's assets (including how the risks and opportunities relating to climate change are taken into account)

2. **Mandate changes** – the ISC will continue to review mandate guidelines, restrictions and benchmarks, review the Scheme's investment strategy to understand any disproportionally emitting strategies, and where necessary, review the inclusion of assets that are most exposed to climate risk in the longer-term portfolio. This assessment will consider other risks to which the Scheme is exposed and the Trustee's wider fiduciary responsibilities. The exclusions policy is an example of this, and the Trustee has also been reducing its exposure to more exposed asset classes such as listed infrastructure holdings.
3. **Impact** –The Trustee will continue to review the current and future strategy to understand opportunities to add impact investments, providing capital to market participants offering new technology and/or solutions to reduce emissions where this is consistent with the Trustee's other objectives, risk management approach and fiduciary duties. In 2020 the Scheme made an investment into the Global Renewable Power Fund with BlackRock, which is an example of such an impact investment.
4. **Free rider** – recognising common goals across the finance industry, the Scheme is expected to benefit from a reduction in emissions due to the actions taken by other market participants, such as the UK Government, and notes that financial markets may move more quickly as companies look to meet their own targets and high carbon industries fall in value or are taken private. This effect is expected to be a key factor in the reduction of the Scheme's carbon emissions in the coming years.

Sustainable investment, including management of climate risk, has been an increasingly important focus for the Trustee over recent years when considering the construction of the Scheme's investment portfolio. The Trustee's approach to monitoring and integrating sustainable investment issues into the management of the Scheme's assets has evolved over time.

As the Scheme matures the Trustee increasingly holds longer-dated assets that better match the liability cashflows of the Scheme, which include credit and real assets. Due to the long-dated nature of these assets, the Trustee is very focused on the sustainability of these assets and credentials for assessing and managing ESG-related risks were key criteria for selecting the Scheme's investment managers.

In appointing investment managers, the Trustee, with input from WTW as investment advisor, considers in detail their experience and capabilities in managing sustainability in the securities or assets in which they invest. This assessment also forms a part of the regular ongoing monitoring of the investment managers, who are always asked to present on the subject when attending ISC meetings.

The Trustee expects managers to integrate ESG considerations into their management of the Scheme's assets and recognises that as investors in a diversified portfolio of various underlying asset classes with different objectives and characteristics, a 'one-size-fits-all' approach to sustainable investment is not optimal. Therefore, the expectations of managers are not uniform across all of the Scheme's funds but based upon the individual characteristics of the Scheme's different mandates.

3.3 Integration of climate into the overall risk management framework of the Plan

The Trustee recognises the impact which climate change could have on a wide range of areas affecting the Scheme's financial position, including the returns which will be achieved on the Scheme's assets, the health (and therefore life expectancy) of the Scheme's members and the strength of the Sponsor. The Trustee receives advice from its investment, actuarial, covenant and legal advisors on the risks facing the Scheme, including the potential impact of climate change and related regulations.

The Trustee also reviewed and updated its risk register to ensure that these reflect the Trustee's intended approach to managing the potential risks relating to climate change.

The Trustee's beliefs in relation to climate risk, and how this should be managed are also documented in both the SIP and the SI Policy.

Section 4 - Metrics and targets

4.1 Metrics used by the Trustee to assess climate-related risks and opportunities in line with its strategy and risk management process

In order for the Scheme's investment strategy to match the Trustee's ambitions in managing climate risk, the Trustee has set climate-related targets and will monitor performance against them. In particular, the Trustee has set the target of reducing the Scheme's carbon footprint by 50% (compared with 2019 levels) by 2030 and to achieve net-zero by 2050.

In line with regulation, the Trustee has undertaken to calculate and monitor emissions as defined below, on investments held across the Scheme's investment portfolio, where it can collect the necessary data:

- **Scope 1 emissions**: all direct emissions from the activities of an entity or the activities under its control, for example, the fuel combustion used to run delivery vehicles across the country, and leaks of greenhouse gases from retail store air conditioning units.
- **Scope 2 emissions**: indirect emissions from electricity purchased and used by an entity which are created during the production of energy which the entity uses, for example, lighting and heating in retail stores.
- **Scope 3 emissions:** all indirect emissions from the activities of the entity, other than scope 2 emissions, which occur from sources that the entity does not directly control, for example, the transport and distribution of products from stores around the world.
- **Scope 4 emissions:** "Negative" emissions, defined as either carbon avoidance (e.g., investments in renewables) or carbon reducing (e.g., investments in carbon capture technology).

For the purposes of this first climate change report the Trustee has reported Scope 1 and Scope 2 emissions. Scope 3 emissions have not been included in this report due to concerns regarding the accuracy and the level of asset coverage of this information. The Trustee will look to include scope 3 emissions, and emissions relating to a greater proportion of the Plan's assets, when the availability and quality of data improves as expected in the coming years.

Data on the exposure of the Plan's LDI holdings (around 29.8% of assets as at 30 September 2022) are also included although the Trustee recognises that the methodology in respect of the carbon exposure of these assets is continuing to evolve and, based on the methodology used, results in some double-counting of carbon exposure. These figures are therefore quoted separately.

The Trustee recognises the difficulties with producing the emissions data consistently across the whole portfolio and as such has been monitoring the different metrics routinely over several years in order to better understand the data. Whilst this has allowed for improvement in the data quality, the Trustee will continue to improve the data where possible in the future.

The Trustee has also agreed a set of climate change-related metrics to assist the Trustee in assessing the potential impact of climate change on the Scheme. The agreed metrics are:

1. **Total Carbon Emissions** – This is an 'absolute emissions' metric which gives the total greenhouse gas emissions attributable to the Scheme's assets. This is calculated in line with the guidance provided by the Greenhouse Gas Protocol.

2. **Carbon Footprint** – This is an 'emissions intensity' metric which is normalised by the market value of the portfolio, and the primary metric that will be monitored as part of the Scheme's Carbon Journey Plan. This metric gives the total greenhouse gas emissions attributable to the Scheme's assets, per $m invested (based on EVIC methodology, see appendix). This is an important complement to the total carbon emissions metric, as well as aiding comparability over time and to industry peers. This is also the preferred metric as set out in DWP guidance, helping to ensure

regulatory alignment. The methodology for the calculation of this metric takes the total carbon emissions as calculated and divides it by the total value of the assets to which the emissions refer.

3. **% of assets with approved SBTi targets** – This is an 'alignment' metric which is forward-looking and aims to communicate a direction of travel and consider the Scheme's exposure to future climate risks. The percentage of assets with approved SBTi targets has been chosen to allow comparisons of portfolios with peers and track progress over time. The Science-Based Targets initiative (SBTi) is a partnership between CDP (formerly known as Carbon Disclosure Project), the United Nations Global Compact, World Resources Institute (WRI) and the World Wide Fund for Nature (WWF) enabling companies to set science-based emissions reduction targets.

4. **Percentage of climate focused engagements –** This measure reflects a desire to have a metric that is forward-looking and impactful. It aims to represent how often managers are engaging on climate-related topics, which is a key area the Trustee is striving for improvement on over the coming years.

The Trustee does not expect these metrics to remain static over time – instead they will be reviewed and, if appropriate, amended to reflect industry best practice and the availability and quality of data.

4.2 Disclosure of emissions and metrics

The initial exercise in gathering and interrogating data has been carried out by the Scheme's investment advisor, using manager-provided data covering 30 September 2022.

	30 September 2022
Metric 1 - Total Carbon Emissions (tCO_2e)	132,624
Metric 2 - Carbon Footprint (emissions/$m invested)	55
Metric 3 - % of assets with approved SBTi targets	30.3%
Metric 4 – Percentage of climate-focused engagements	31.4%

Notes:

1. All data provided by investment managers as at 30 September 2022 unless otherwise stated.
2. LDI assets have been excluded from the table above. Asset values based on EVIC methodology.
3. Data includes scope 1 and 2 emissions.

Metrics for the LDI assets have been provided separately below:

	30 September 2022
Metric 1 - Total Carbon Emissions (tCO_2e)	75,857
Metric 2 - Carbon Footprint (emissions/$m invested)	70
Metric 3 - % of assets with approved SBTi targets	n/a
Metric 4 – Percentage of climate-focused engagements	n/a

Notes:

1. Data provided by investment manager using the position as at 30 September 2022 and 2022 government bond emissions data.
2. Data includes scope 1 and 2 emissions.
3. Metrics are based on the portfolio including leverage.

In calculating the 30 September 2022 absolute emissions and carbon footprint, the Trustee was able to obtain data on 56% of the non-LDI part of the portfolio. The Scheme's illiquid Secure Income assets is the area in which data has the largest scope to improve, with the majority of these assets relying on proxied data. The Scheme's Buy-and-Maintain portfolio's emissions figure is built up of both actual and proxied data, which, given the importance of these assets to the portfolio, the Trustee will continue to monitor separately and engage with the managers as appropriate to improve data quality.

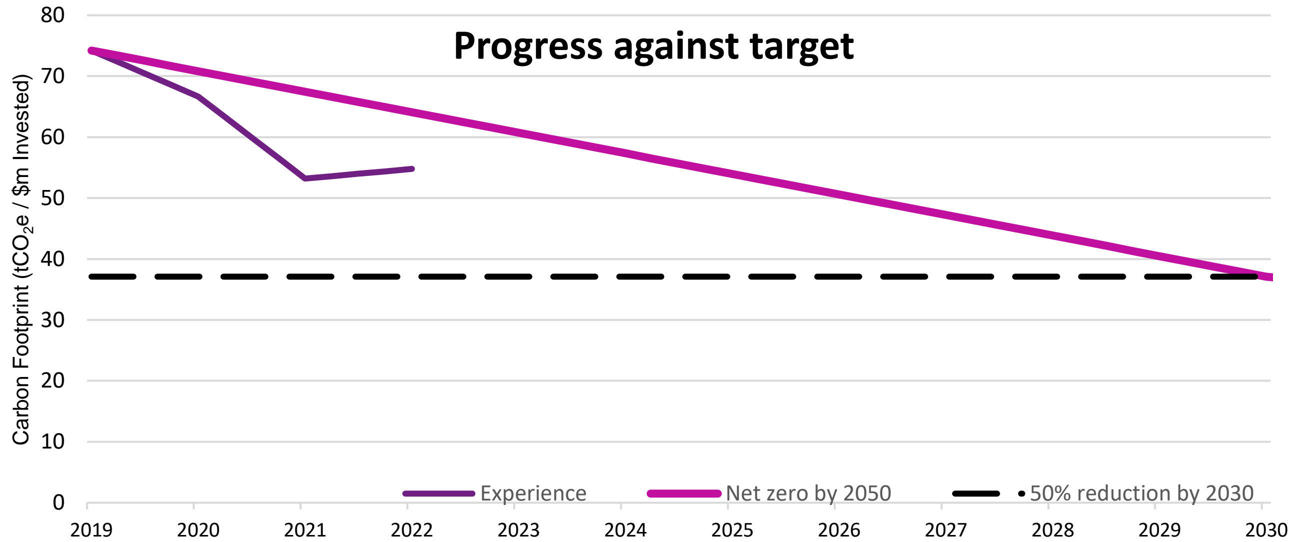
	% of assets 30 September 2022	Data provided by manager or proxied	% coverage
Equities	4.9%	Manager	85%
Property	2.6%	Manager	45%
Alternative credit	14.0%	Manager	29%
Illiquid assets	18.6%	Manager/proxied	45%
Buy-and-Maintain corporate bonds	30.1%	Manager	62%
LDI and cash	29.8%	Manager	100%

Recognising some of the limitations in gathering data the analysis has been carried out on a "best endeavours" basis, noting that the data quality metric itself will help gauge the improvement in the Scheme's output over time. The Trustee expects data quality to continue to improve over time as the industry collectively works together towards that common goal.

4.3 The Scheme's target for managing climate-related risks and opportunities

Carbon Journey plan

The analysis below is based on manager-provided data (where available; where data is unavailable WTW has proxied, on behalf of the Trustee, the exposure based on the characteristics of similar assets for which data is available from the MSCI) as at each 30 September between 2019 (the baseline date) and 2022.



The estimated Carbon Footprint has decreased by around 25% since 2019 and the Scheme is therefore on track to meet its interim 2030 reduction target. As shown by the chart, whilst in general the carbon footprint has been falling over time there has been some volatile experience since the inception of the analysis in 2019, which in part reflects changes in data availability and calculation methodologies over that period. It should therefore be recognised that the progress towards the ultimate target is unlikely to be a smooth one; however, the Trustee expects the analysis to become more robust over time, as data improves, and industry practice evolves. The Trustee will review the Scheme's progress relative to the agreed targets over time and may amend these over time if appropriate, for example due to changes in the data available or a change in the Trustee's preferred approach (for instance, the Trustee recognises that it may be preferable to remain invested in high-emitting companies and engage with them to reduce their emissions rather than to fully disinvest).

The main driver for the reduction in carbon footprint (both since 2019 and over the last year) has been the de-risking activity undertaken by the Scheme. In particular, the sale of the Scheme's listed infrastructure holdings resulted in a net reduction in the Scheme's carbon footprint. Whilst the figures suggest that the Trustee is on target to meet its interim objective, the Trustee is not complacent around the risks facing the Scheme from climate change and continues to be open to opportunities to further reduce this, and encourages its investment managers and advisors to take action to reduce global emissions and manage the potential impact on the Scheme.

Conclusion – Looking forward

Recognising the contribution of the Scheme to climate change is an important first step to understanding the actions the Trustee can take to help shape a better future. The Trustee is committed to achieving the targets set out in this report through enhancing its engagement with managers and encouraging them to increase the transparency of their data.

An awareness of potential climate-related impacts will form part of investment strategy over the coming years. The Scheme has made progress over previous years and the Trustee will continue to identify future opportunities that will contribute towards the Scheme's ultimate goals. However, the Trustee also wishes to reassure members and their beneficiaries that securing members' pensions will always be its priority.

Appendix: Glossary

GHG emissions

The Trustee refers to GHG emissions, which is used as shorthand for the six main greenhouse gases (GHGs), defined by the Kyoto Protocol (Carbon dioxide (CO_2); Methane (CH_4); Nitrous oxide (N_2O); Hydrofluorocarbons (HFCs); Perfluorocarbons (PFCs); and Sulphur hexafluoride (SF_6).

Absolute Emissions Metric: Total GHG emissions (tCO_2e) (scope 1 & 2)

Total amount of greenhouse gas emissions (“CO_2 equivalents”) (as mandated by the Kyoto Protocol) emitted by the underlying portfolio companies, attributed to the investor based on the total investment in each company.

$$\sum_{n}^{i}\left(\frac{Current\ value\ of\ investment_i}{Investee\ company\ enterprise\ value_i}\right) \times Investee\ company's\ scope\ 1\ and\ 2\ emissions_i$$

Emissions Intensity Metric: Carbon Footprint (tCO_2e / EVIC $m) (scope 1 & 2)

An intensity measure of emissions that assesses the level of greenhouse gas emissions (as mandated by the Kyoto Protocol) arising from $1 million investment (based on Enterprise Value Including Cash) in a company.

$$\frac{\sum_{n}^{i}\left(\frac{Current\ value\ of\ investment_i}{Investee\ company\ enterprise\ value_i} \times Investee\ company's\ scope\ 1\ and\ 2\ emissions_i\right)}{Current\ value\ of\ all\ investments\ (\$millions)}$$

Net zero

As noted by the Intergovernmental Panel on Climate Change (IPCC), net zero emissions are achieved when anthropogenic emissions of greenhouse gases to the atmosphere are balanced by anthropogenic removals over a specified period. Anthropogenic in terms of climate change refers to the impact humans have had on climate change, primarily through emissions of greenhouse gases.

Enterprise Value Including Cash (EVIC)

Defined as the sum of market capitalisation of shares and book values of total debts and minority interests at fiscal year end. No deductions of cash or cash equivalents are made to avoid potential negative enterprise values. This is the recommended denominator metric for carbon attribution according to the GHG Protocol, the global standard for carbon accounting endorsed by the European Union and the DWP.