

# Responsible Investment Policy

April 2020

## 1. Introduction

- 1.1 The Cheshire Pension Fund (“the Fund”) is the name of the Local Government Pension Scheme (LGPS) in Cheshire.
- 1.2 Cheshire West and Chester Council (“the Council”) as the administering authority of the Fund, has a fiduciary duty to act in the best, long-term, interests of the Fund’s scheme members and participating employers.
- 1.3 The Fund’s primary investment objective to meet its fiduciary duty is to maximise returns subject to an acceptable level of risk whilst increasing certainty of cost for employers given the long term nature of the scheme.
- 1.4 The Fund believes that in order to fulfil this duty, it must have a clear policy on how it invests in a responsible manner. Consideration of Environmental, Social and Governance (“ESG”) issues are fundamental to responsible investment, particularly where they are likely to impact on the primary investment objective.
- 1.5 This Responsible Investment (RI) policy sets out the Fund’s approach to embedding consideration of ESG issues in the investment process, utilising the various tools available to manage ESG risks and harness opportunities presented by ESG factors.

## 2. What is our policy on Responsible Investment?

- 2.1 The Fund’s core principles guiding our approach to Responsible Investment are:
  - We will apply **long-term thinking** to deliver **long-term sustainable returns**.
  - We will seek **sustainable returns** from **well-governed assets**.
  - We will use an **evidence-based** long-term investment appraisal to inform **decision-making** in the implementation of Responsible Investment principles and consider the costs of Responsible Investment decisions consistent with our fiduciary duties.
- 2.2 The Fund will invest in sustainable assets to deliver long term financial returns to enable pension promises to be paid now and into the future. This approach places the full consideration of financially material ESG factors at the heart of the Fund’s investment decision making and monitoring process. This approach is distinct from the commonly used definition of ‘ethical’ investing: an approach in which the values or moral beliefs of an organisation or its key decision makers takes primacy over its investment considerations. Such an approach is often typified by an exclusions policy whereby certain sectors or groups of companies are excluded at the initial stage of the investment analysis process.

### 3. What actions will the Fund take to meet these principles?

Core Principle	Associated Actions
<p>We will apply long-term thinking to deliver long-term sustainable returns</p>	<ul style="list-style-type: none"> <li>- Investment objectives are clearly set out in the published Investment Strategy Statement.</li> <li>- Set longer-term performance objectives for investment managers.</li> <li>- Seek to ensure that long term interests are aligned with that of its investment managers on all issues including on ESG considerations.</li> <li>- Policies relating to ESG will be considered as part of the Fund’s long term investment planning process, following a thorough and robust investment appraisal.</li> </ul>
<p>We will seek sustainable returns from well-governed assets</p>	<ul style="list-style-type: none"> <li>- Apply a robust approach to stewardship, linked to the Fund’s approach that engagement can positively and effectively influence behaviours.</li> <li>- Engage with companies when engagement to improve ESG outcomes and add value to the Fund.</li> <li>- Comply with the UK Stewardship Code and work within the spirit of the United Nation backed Principles of Responsible Investment (“PRI”).</li> <li>- Hold investment managers to account to ensure compliance with this policy.</li> <li>- Collective engagement through membership of the Local Authority Pension Fund Forum (LAPFF), the LGPS Central pool and other opportunities that arise from time to time.</li> <li>- Exercise voting rights in all markets where practicable.</li> </ul>
<p>We will use an evidence-based long-term investment appraisal to inform decision-making in the implementation of RI principles and consider the costs of RI decisions consistent with our fiduciary duties.</p>	<ul style="list-style-type: none"> <li>- Consider the potential financial impact of ESG related issues (such as climate change or executive remuneration) on an ongoing basis.</li> <li>- Consider the potential financial impact of investment opportunities that arise from ESG related factors (e.g. investment in renewable energies or housing infrastructure).</li> <li>- Monitor the carbon footprint of its publically listed investment assets and actively manage any potential financial risks that this identifies through a Climate Change Stewardship Plan.</li> <li>- Consider investment opportunities that have positive impacts and recognises that the changing external environment presents new opportunities i.e. renewable energy, green technology and social impact investments.</li> </ul>

#### 4. **How will we monitor performance on Responsible Investment?**

4.1 The Fund will be **transparent and accountable** in terms of its performance on Responsible Investment.

4.2 To achieve this the Fund will:-:

- publish the Investment Strategy Statement on the Fund's website in line with the scheme regulations
- explain decisions relating to the setting of the investment policy
- publish the Responsible Investment Policy on its website, review the policy on an ongoing basis and formally consult on the policy at least every three years
- closely monitor its appointed investment managers whom the Fund rely on to partly implement its Responsible Investment Policy
- publish a Climate Change Report showing the carbon footprint of the Fund's publically listed investment assets and how the Fund will manage any related risks
- undertake an annual review of corporate governance, voting and engagement activity undertaken by the Fund and its underlying managers
- publish an annual summary of voting and engagement activity
- ensure that its decision makers are properly trained and kept abreast of ESG issues
- include ESG as standing item on the Investment Sub Committee (or equivalent) agendas with a view to reporting on manager performance in relation to ESG investing, and noting any hot topics / issues arising
- undertake a fundamental review of any specific ESG issues that are considered by the Investment Sub Committee to be of potentially material financial impact
- consider and respond to feedback from stakeholders in relation to issues of concern

#### 5. **Responsible Investment and LGPS Central pool**

5.1 The Fund has joined with seven other LGPS Funds (Derbyshire, Staffordshire, Shropshire, Leicestershire, Nottinghamshire, West Midlands and Worcestershire) to create the LGPS Central pool. This is one of eight pools across the LGPS.

5.2 The pool was set up to deliver the Government's requirement for all administering authorities in England and Wales to join together and pool the way they managed their investment assets to drive economies of scale and increase opportunities in asset classes which partner funds may not have had the capacity to invest in individually.

- 5.3 In April 2018, the partner funds created a jointly owned company called LGPS Central Ltd, a Financial Conduct Authority accredited investment company, to manage their pooled investment assets, collectively valued at some £40bn.
- 5.4 It will take a number of years to transition assets securely and economically from current management arrangements across to LGPS Central Ltd.
- 5.5 LGPS Central Ltd has now launched a number of investment products and the Fund will continue to work with LGPS Central Ltd and partner funds to help shape further investment products that meet the requirements of the Fund's Investment Strategy Statement.
- 5.6 All partner funds retain ownership and control of their Investment Strategy and asset allocation decisions. Day to day investment decisions such as to engage or dismiss investment managers, and monitoring of investment performance passes to LGPS Central as assets transfer.
- 5.7 To date the Cheshire Pension Fund has transitioned over £800m of assets across to LGPS Central (approx. 15% of the Cheshire Fund's total assets) and this figure will increase as LGPS Central launch new investment products.
- 5.8 It is expected that the Fund's ability invest in a responsible way will be enhanced through LGPS Central due to the inherent benefits of scale, collectivism and innovation that will result from the project.

## **6. Engagement versus Exclusion**

- 6.1 The Fund believes that its influence as a shareholder is most effective by engaging with companies, in order to influence behaviour and enhance shareholder value.
- 6.2 Consequently, the Fund does not implement a divestment approach that excludes certain types of investments, companies or sectors except where barred by UK law.
- 6.3 The Fund actively engages with companies in which it is invested through LGPS Central Ltd, its investment managers and through membership of the Local Authority Pension Fund Forum (LAPFF).
- 6.4 Ultimately the Fund retains the right to divest from certain companies or sectors in the event that all other approaches are unsuccessful and it is determined that the investment is no longer aligned with the interests of the Fund or that the issue poses a material financial risk.
- 6.5 Specifically, in respect of climate change, the Fund does not adopt an approach to divest from companies or sectors on a mechanistic basis. For example, calls to divest from fossil fuel companies by default take insufficient account of the relatively high carbon footprint of many companies outside of the energy sector. In addition, there is strong evidence that some

companies within this sector are transitioning quickly and effectively to a net zero carbon emissions position and/or are engaging positively with the requirements of the Paris Climate Change agreement. The Fund therefore believes that it is not sensible to disinvest from such companies when pursuing a holistic and evidence based approach to managing and monitoring climate change risk.

## **7. Responsible Investment Engagement Themes**

7.1 Working in partnership with LGPS Central the Fund has adopted the following key engagements themes for particular focus during the year:

- Climate Change
- Single Use plastics
- Technology and disruptive industries
- Tax transparency and fair tax payment

7.2 LGPS Central Ltd has appointed a specialist engagement provider, Hermes EOS. Every quarter LGPS Central Ltd reports on their activities and progress in a Quarterly Stewardship report, which is publically available at:

[https://www.lgpscentral.co.uk/wp-content/uploads/2019/11/2019-11\\_QSR\\_v8.pdf](https://www.lgpscentral.co.uk/wp-content/uploads/2019/11/2019-11_QSR_v8.pdf)

7.3 In addition to the focus on the four themes outlined above, LGPS Central Ltd have a wealth of active engagement activity on numerous other themes including executive remuneration, board composition, diversity and workforce rights.

## **8. Exercise of Voting Rights**

8.1 The Fund exercises its ownership rights by actively voting stock it holds.

8.2 The Fund delegates responsibility for voting to LGPS Central Ltd or the Fund's directly appointed investment managers who are required to vote wherever the Fund has a voting interest.

8.3 For Fund assets managed by LGPS Central Ltd, wherever practicable, votes must be cast in accordance with LGPS Central's Voting Principles (available on LGPS Central's website at: <https://www.lgpscentral.co.uk/wp-content/uploads/2019/03/Voting-Principles-March-2019.pdf>)

8.4 For Fund assets managed by appointed external investment managers, votes must be cast in line with industry best practice as set out in the Combined Code of Corporate Governance with a clear focus on enhancing long term shareholder value.

8.5 Investment managers' quarterly performance reports are required to include a specific briefing on corporate governance, detailing all votes cast on the

Fund's behalf. The Investment Sub Committee receives these reports on a quarterly basis and any exceptions or examples of non-compliance are addressed directly with the Fund's managers.

- 8.6 The Fund is committed to becoming accepted as a signatory to the recently relaunched and revised UK Stewardship Code and will submit an annual stewardship report for assessment by the Financial Reporting Council by the required deadline.

## **9. Climate Change**

- 9.1 The Fund recognises that, in addition to the wider impacts of climate change, owning investment assets with a significant exposure to fossil fuels, poses a particular potential investment risk in that markets may re-price fossil fuel assets in response to growing public concerns over climate change and the response of policy makers to this concern.

- 9.2 It is impossible to predict the timing or quantum of any market re-pricing. Given this, the Fund believes it is sensible to adopt a precautionary approach to climate change investment risk and pursue three different strands of activity to pro-actively manage the potential risk. These are:

- a) Commission an independent assessment of its publicly listed investment assets to determine the Fund's overall carbon footprint and assess potential climate change impacts and opportunities.
- b) Produce a climate change stewardship plan to set goals of engagement with companies, fund managers and policy makers and influencers. Wherever feasible engagement objectives will be SMART (Specific, Measurable, Actionable, Relevant and Time-bound) to enable the Fund to adequately assess a company's progress towards their net zero carbon target. The Fund believes that all companies should align their business activities with the Paris Agreement on climate change and will actively engage with companies, ideally in partnership with like-minded investors, to persuade companies to align their business plans with the 1.5C target.
- c) Wherever possible, fully assess the impact of all new investment decisions on the carbon footprint of the investment portfolio. In particular, the Fund will explore investment opportunities that may present themselves as the world transitions to a lower carbon economy, where these opportunities align with our investment requirements and our overall investment strategy. This approach was reflected in the decision the Fund took in 2019 to transition over £500m of its equity portfolio to the LGPS Central Carbon Factor Fund, one of the aims of which was to boost investment in firms producing technological solutions to meet the climate challenge.