WINTER 2023/24

ENGAGE

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LOTHIAN PENSION FUND

CONTENTS

HAPPY NEW YEAR AND WELCOME TO ISSUE 7 OF ENGAGE

2023 was an exciting and award-winning year for Lothian Pension Fund (LPF). In November, Emmanuel Bocquet joined us as Chief Investment Officer (CIO), succeeding Bruce Miller who retires later this month. Under Bruce's tenure as CIO, we've evolved into one of the leading LGPS in the UK, generating peer-leading risk-adjusted returns at industry-leading costs for our employers and members.

'Lothian Pension Fund is unique within the Scottish LGPS sector in operating an FCA-regulated investment arm. It's well known in the industry for its commitment to sustainably growing its pension fund through good stewardship of its assets. I'm delighted to be joining to continue the great work of the team and delivering the very best service to our members, employers and partner funds.'

Emmanuel Bocquet, CIO, Lothian Pension Fund

This issue provides an update on our most recent Responsible Investment (RI) activities, including our voting and some of the collaborative engagement initiatives we're involved in. We also celebrate the fact that 2023 was an award-winning year, including LPF winning the LGPS Fund of the Year at the LAPF Investment Awards 2023 in September and Bruce Miller receiving the Lifetime Achievement Award at the LGC Investment Seminar in October.

For more information on our RI initiatives and commitments, you can view our 2023 Stewardship Report that's now available on our website.

David Vallery
Chief Executive Officer
Lothian Pension Fund

RESPONSIBLE INVESTMENT UPDATE

In this issue we provide further insight into our voting activity in the oil and gas industry. At LPF we manage most of our assets internally, which provides us with control over our voting.

Our Statement of Responsible Investment Principles provides more details about how we incorporate Environmental, Social and Governance issues into our investment activities. However, our scale means that our potential for direct influence is relatively modest. That's why we recently participated in the 'Asset Owner – Asset Manager Aligning Expectations roundtable' recognising the need for better alignment of proxy voting by asset managers with asset owners' climate stewardship ambitions.

Our biggest impact can come through working with others: On pages 7-8 we provide an update on the collaborative initiative Climate Action 100+ which seeks to engage to support the world's largest corporate greenhouse gas emitters to take necessary action on climate change. We're an active participant in the initiative as a co-lead engager with one target company, while our voting and engagement provider is a co-lead with 23 companies.

Mining is a sector that we recognise as posing a range of environmental, social and governance issues, while also providing critical minerals for society and the low carbon transition, making the sector systemically important to the economy. We therefore recently became an investor supporter of the Global Investor Commission on Mining 2030, which seeks to develop a consensus amongst investors on the role finance has in realising a vision of a socially and environmentally responsible mining sector by 2030.

Gillian de Candole, Portfolio Manager and Responsible Investment Lead

THOUGHTFUL VOTING

Background

Launched in 2020, the Say-on-Climate initiative encourages companies to consult shareholders about their climate strategies and net zero action plans at their annual general meetings. The number of companies providing these ballots doubled over the first two years, however the number of management-proposed Say-on-Climate proposals has dropped this year.

There were also several climate-related shareholder resolutions, including some filed by Follow This (a Dutch non-governmental organisation of activist shareholders), requesting that companies set comprehensive greenhouse gas emissions targets that are consistent with the goals of the Paris Agreement.

When exercising our equity voting rights, we're guided by proxy vote recommendations provided by our voting and engagement provider, EOS. These recommendations consider both global best practice and regional governance requirements. EOS applies a rigorous case-by-case approach to assessment of transition plans and progress reports, only recommending support of plans that demonstrate robust targets and a clear and credible strategy to achieve the stated targets.

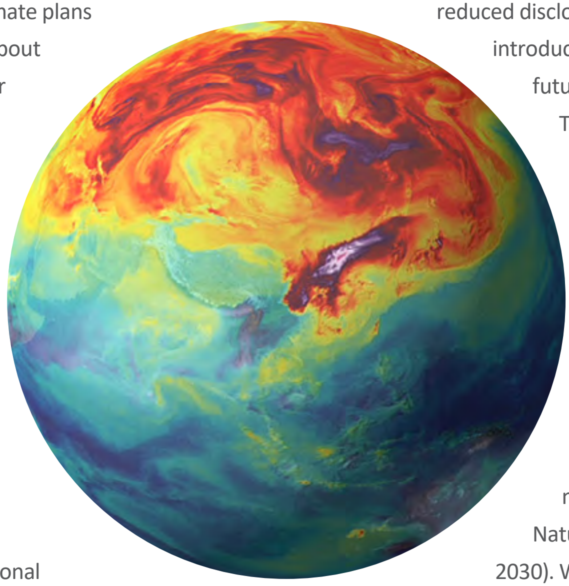
Voting activity and outcome

Examples of how we voted on climate plans or emission reduction targets are presented in the table below with an explanation and assessment.

	Management Proposed Say-on-Climate vote	LPF Vote	Vote Result	Follow-This Shareholder Resolution	LPF Vote	Vote Result
Mining Companies						
Glencore	2022 Climate Report	Against	70% support	n.a.	n.a.	n.a.
Energy Companies						
Shell	Shell Energy Transition Progress Update	Against	80% support	Yes - Aligning emissions targets to Paris Agreement	For	20% support
Total Energies	Sustainable Development and Energy Transition Plan	Against	89% support	Yes - Aligning emissions targets to Paris Agreement	For	30% support
Exxon Mobil	n.a.	n.a.	n.a.	Yes - Adopt a medium term Scope 3 target	For	11% support
Chevron	n.a.	n.a.	n.a.	Yes - Adopt a medium term Scope 3 target	For	10% support
BP	n.a.	n.a.	n.a.	Yes - Aligning emissions targets to Paris Agreement	Against	17% support

Assessment

Management proposed Say-on-Climate votes continued to garner strong support from shareholders this year, while resolutions filed by climate activist groups such as Follow This received support from only a minority of shareholders. This indicates that a majority of shareholders in these companies continue to be willing to support incremental progress on climate plans in the context of ongoing concerns about energy security and affordability. Our voting record shows we continued to exercise our voting rights in alignment with our identification of climate change as a key systemic risk, while being willing to recognise leadership.



We voted against Glencore's climate report due to poor disclosures and action on climate change. Glencore's targets for emissions reduction fall short of expectations relative to the International Energy Agency's net zero coal pathway for the company to be 1.5°C aligned. Additionally, Glencore continues to allocate more capital expenditure to coal – up from 16% in 2021 to 22% in 2022 – and we believe Glencore should be maintaining production at existing mines as they wind down, rather than expanding. We also voted in favour of a shareholder resolution calling for improved disclosure on the alignment of Glencore's thermal coal production and related capital expenditure to the Paris Agreement's 1.5°C goal, which would help evaluate the emissions from coal and related risks of producing coal above a 1.5°C aligned pathway. However, the resolution received 29% support.

Consistent with last year, we voted against Shell's energy transition progress update as we consider Shell's strategy to be materially misaligned to a 1.5°C scenario, in addition to poor disclosure of metrics allowing tracking of overall decarbonisation progress. Shell also reduced disclosure relating to future capital expenditure, introducing further uncertainty about the company's future direction. We voted in favour of the Follow This shareholder resolution to align the 2030 reduction target for Scope 3 emissions to 1.5°C, as we assessed it could prompt a review of metrics used to demonstrate Shell's alignment with a 1.5°C scenario, and we don't believe that the company's current targets are aligned with this.

We voted against Total Energies energy transition plan as the strategy still relies on maintaining and growing fossil fuels (Liquified Natural Gas production forecast to grow 40% by 2030). We consider the companies' targets as lacking ambition as they're designed to be reached largely by an increase in low carbon energies rather than a decline in fossil fuels. This lack of ambition and alignment led us to vote in favour of the Follow This shareholder resolution for Total Energies to align its Scope 3 targets with the Paris-aligned 1.5°C scenario by 2030.

On Exxon, we voted in favour of the Follow This shareholder resolution to adopt a medium-term scope 3 target, consistent with the Paris Agreement, as we believe this would increase the transparency of Exxon's climate change strategy. We also voted in favour of several additional shareholder proposals relating to emissions, plastics, and tax transparency, which would all improve the management and transparency of environmental, social, and governance impacts.

At Chevron, we voted in favour of the Follow This shareholder resolution to adopt a medium-term scope 3 emissions reduction target as we believe this would increase the transparency of Chevron's climate change strategy and improve management of climate-related risks. We also voted in favour of several shareholder resolutions which would enhance transparency and governance practices.

At BP, we voted against the Follow This shareholder resolution, as the additionality of this resolution was unclear given that BP have already had a shareholder resolution successfully passed (in 2019) requiring the company to disclose its strategy consistent with the Paris goals. In 2020, BP responded by launching its strategy to become a net zero company by 2050 including targets for emissions reductions in the short and medium term. This climate strategy was supported by a majority of shareholders (including LPF) in BP's 2022 Say-on-Climate proposal. In February 2023, BP disappointingly reduced the ambition of some of these targets, however we recognise that BP's climate strategy (with 50% of its spending budget committed to low-carbon business by 2030) and disclosure remain ahead of their sector peers. We continue to engage with BP through our voting and engagement provider, EOS, and Climate Action 100+, reiterating the need to see clear progress on reducing both absolute emissions and the carbon intensity of its business.

Edward Braidwood, Graduate Investment Analyst

COLLABORATIVE ENGAGEMENT: CLIMATE ACTION 100+

Working with CA100+

CA100+ is an international collaborative initiative by institutional investors representing over $55 trillion in assets. Signatories to Climate Action 100+ engage with the boards and senior management of companies to take necessary action on climate change

LPF committed internal engagement resource to CA100+ by becoming a participant member of CA100+ in 2020 and co-leading engagements with a focus company. In addition to direct engagement as part of CA100+, we encourage our external managers to support the initiative.

Our engagement provider, EOS is also a significant supporter of CA100+, leading or co-leading engagement at 24 of the CA100+ focus companies across Europe, North America, and Asia.

Influencing change

Climate Action 100+ has notched up five years of collaborative engagements with the world's biggest greenhouse gas emitters and is now entering its second phase. Since December 2017 the collaborative engagement initiative has been striving to bring the world's biggest corporate emitters into line with international ambitions for a 1.5 degree world.

By participating actively in the CA100+ initiative, our officers and service providers have influenced real change, including an accelerated timetable for methane emissions reductions and a change to the corporate lobbying practices of companies with significant carbon emissions.

We believe that such collaborative engagement actions have assisted the target companies in becoming better prepared for a net-zero world. Equally, we recognise that CA100+ focus

Company Name	EOS Sector	Participation
Mercedes-Benz Group	Automobiles	Lead
Volkswagen	Automobiles	Co-lead
Dow	Chemicals	Co-lead
Hon Hai Precision Industry	Industrials	Co-lead
POSCO Holdings	Mining & Metals	Co-lead
BP	Oil & Gas	Co-lead
Chevron	Oil & Gas	Co-lead
Kinder Morgan	Oil & Gas	Co-lead
PetroChina	Oil & Gas	Co-lead
Petroleos Mexicanos	Oil & Gas	Co-lead
TotalEnergies	Oil & Gas	Co-lead
Enbridge	Oil & Gas	Support
AP Moller – Maersk	Transportation	Co-lead
Stellantis	Transportation	Co-lead
Lockheed Martin	Transportation	Support

Source: EOS data

companies still have significant work to do to align their businesses to achieve a net-zero world. It seems clear that government policies rather than investors' voting and engagement activities alone are needed to drive change.

Looking ahead

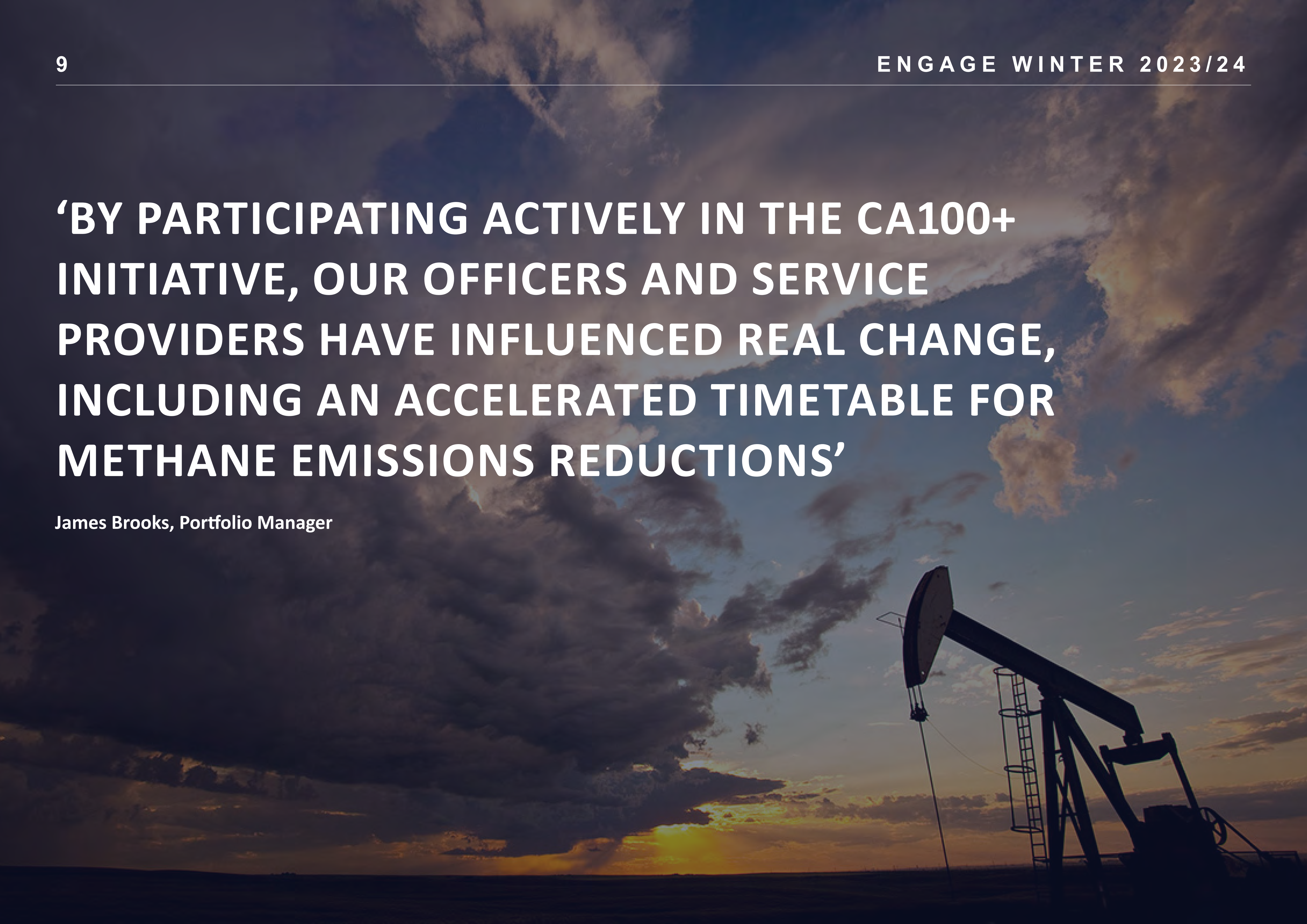
CA100+ aims to move beyond disclosure during its second phase from 2023-30. It will push for focus company action to develop and implement Paris-aligned transition plans backed by credible, sufficient investment.

It's also introducing a significant upgrade to the benchmark to assess progress, with a greater focus on emissions reductions, alignment with 1.5°C pathways and net-zero transition planning, which will include a deeper assessment of capital allocation and asset-level changes.

The second phase will also introduce new measures to enhance collaborative participation from investors and encourage more transparent planning and escalation strategies across the co-leads for focus companies.

We look forward to continuing to collaborate with CA100+ to influence real and positive change in our portfolio.

James Brooks, Portfolio Manager



‘BY PARTICIPATING ACTIVELY IN THE CA100+ INITIATIVE, OUR OFFICERS AND SERVICE PROVIDERS HAVE INFLUENCED REAL CHANGE, INCLUDING AN ACCELERATED TIMETABLE FOR METHANE EMISSIONS REDUCTIONS’

James Brooks, Portfolio Manager

GLOBAL INVESTOR COMMISSION ON MINING 2030

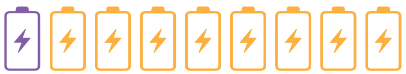
In November, LPF became an investor-supporter of the Global Investor Commission on Mining 2030, also known as the Mining 2030 Commission. It's a multi-stakeholder Commission including representatives from communities, intergovernmental organisations, civil society, academia, law, unions, the mining industry, banking, insurance and investors, who recognise the need for the industry to manage systemic risks which can threaten its social license to operate.

Mining is a sector that we recognise as posing a range of environmental, social and governance issues, while also providing critical minerals for society and the low carbon transition, making the sector systemically important to the economy. The Commission seeks to develop a vision for the future of mining that will specifically consider how investors value, invest and steward the sector to meet future demand in a socially and environmentally responsible manner.

Mined resources underpin modern society, and an expansion of extraction capacity is necessary to achieve the Paris Agreement goals. But the sector can also be undermined by a series of systemic social and environmental issues that challenge mining today and will challenge its future growth if not adequately addressed.

A key example of this is the increasing scramble by governments and companies to secure the supply chains of transition minerals required to deliver on their net zero commitments. For instance, whether auto manufacturers can meet battery demand for new electric vehicles will depend on the supply of sufficient minerals required for these batteries. According to one leading market analyst, this will require lithium mining to increase production by 880% in the decade from 2020 to 2030, while an increase of over 900% is needed for graphite by over 900% over the same period.

Graphite mining for electric vehicle batteries may need to increase by over 900% from 2020-2030



Even with significantly greater recycling, substitution of more abundant key minerals for more constrained minerals and greater efficiency of mineral usage, there is no path to net zero without very considerable expansion of mining.

The Mining 2030 Commission builds on the experience of the investor-led response following the 2019 Brumadinho disaster which contributed to the creation of a Global Industry Standard on Tailings Management, and the effort to establish an independent Global Tailings Management Institute to oversee the audit and implementation of the standard.

Gillian de Candole, Portfolio Manager and Responsible Investment Lead

AWARD SUCCESS

In 2023, we were delighted to have a run of award successes. At LPF, our primary objective is to pay the pensions for our 80,000 plus members, whilst aiming to reduce the costs to employers and investing in a responsible manner. Being recognised by peers and external specialists helps affirm we're on the right path.

In September, we were named winner of LGPS Fund of the Year at the LAPF Investments Awards 2023 (pictured top right). The LGPS Fund of the Year award looks at best practices in pension fund operations, investment performance and thought leadership within the LGPS and is acknowledged throughout the industry as a mark of excellence in the field of pension fund investment.

Shortly after, we were recognised by the Sustainable Finance Disclosure Rewards for Asset Owners (SFDR4AO) as a leading pension fund for our approach and disclosure on gender. Our commitment and the actions we're taking to drive gender diversity and equality was highlighted, both in regard to our own organisation and how we steward (through voting and engagement) the companies in which the fund is invested. The awards celebrate best practice based on reports published last year.

Our positive action approach to gender balance, which is benchmarked externally, is helping to ensure that our HR policies and processes are inclusive and accessible, from how we attract and recruit, to how we reward and engage our colleagues.

In October, Bruce Miller, LPF's Chief Investment Officer (pictured below), received the Lifetime Achievement Award at the LGC Investment Seminar. Bruce joined Lothian Pension Fund in 2006 and back then, we had less than £3bn in assets with a small in-house team and assets predominantly managed externally. Today, LPF has a 20-strong internal investment team with around £10bn in assets and an FCA-registered entity, LPFI. Most of Lothian Pension Fund's assets are now managed in-house.

Under Bruce's tenure as CIO, we've evolved into one of the leading LGPS in the UK, generating peer-leading risk-adjusted returns at industry-leading costs for our employers and members.

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If you'd like more information on our ESG activities, please visit our website www.lpf.org.uk.

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