

Whitbread Group Pension Fund

Task Force on Climate-Related Financial Disclosures (TCFD) Report

For the scheme year end 31 March 2023

Table of Contents

- 1. *Introduction* 3
- 2. *Governance*..... 5
- 3. *Strategy* 8
- 4. *Risk Management* 17
- 5. *Metrics and Targets* 18

1. Introduction

The Trustee of the Whitbread Group Pension Fund (hereinafter referred to as the “Trustee” or “We” and the “Fund”, respectively) presents its annual report to adhere with our responsibilities under the Department for Work and Pensions (“DWP’s”) new climate regulations, set by the Task Force on Climate-Related Financial Disclosures (hereinafter referred to as “TCFD”) for the year ended 31 March 2023.

The Fund is now subject to the requirement to produce disclosures in line with the recommendations of the Task Force on Climate Related Disclosures (TCFD), as transposed into UK law in 2021. We fully support the TCFD’s aim of improving and increasing reporting of climate-related financial risks and opportunities. The Fund is subject to the TCFD requirements with effect from 1 October 2022, with the first formal report required to be published by 31 October 2023.

This climate disclosures report provides information on how we have considered climate-related risks and how we manage these risks as part of the ongoing management of the Fund.

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 scheme 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 report sets out the Fund’s approach to compliance in each of these four areas.

This report is the first TCFD report for both the Defined Benefit and Defined Contribution Sections and its content is expected to evolve over time as the quality and availability of data for reporting and monitoring purposes improves, given the increasing focus on climate change and its lasting impact as both a significant risk and opportunity.

The Defined Benefit Section (“DB Section) is at the mature end of its lifecycle – having reached full funding on the secondary funding target in April 2022, at which point the DB Section conducted its de-risking implementation process down to a new return target of Gilts+0.75% p.a. This involved the divestment of the liquid assets of the portfolio, such as the equity, alternative credit, hedge fund and alternative beta asset classes in order to complete the de-risking in a timely manner. Therefore, the portfolio has a current asset allocation of Liability Driven Investment (“LDI”, the majority of the DB Section), and illiquid assets across the private markets and secure income alternatives asset classes. In addition, the DB Section invested in a Bulk Purchase Annuity (or BPA) in June 2022, which insured approximately 50% of the Funds pensioners. The DB Section’s ultimate goal, determined by the Trustees, is to target fully covering its liabilities through an insurance policy. As a result, there is reduced flexibility for the DB Section to significantly alter its investment strategy or current investments in order to capture more climate-related opportunities. Despite this, the Report details how the DB Section is very resilient, and even benefits from, different climate change scenarios. It is however important to appreciate the limitations of the analysis throughout the report, such as the reliance on third parties for the maintenance and reporting of accurate data, validation of our assumptions, and the

information available at the date of the analysis. However, we expect the accuracy and accessibility of data to improve and evolve over time. We have signposted these limitations within the report.

The Defined Contribution Section (“DC Section”) of the Fund provides benefits to members based on the value of savings built up through ongoing contributions and investment returns. We are responsible for setting a default investment strategy which is intended to be appropriate for most members of the DC Section. The membership of the DC Section is distributed across a range of ages, with most members many decades from retirement. This means investment policy, and consequently the climate policy, is set with a long-term time horizon in mind.

The investment arrangements are implemented by Mercer who are responsible for the day-to-day management of assets along with climate change and wider ESG considerations.

This report sets out the resilience of the Fund to different climate change scenarios.

2. Governance

As a Trustee, we view climate change as both a critical risk (alongside other risks in the Fund) and an opportunity, which requires ongoing oversight and management. As a result, we have in recent years assessed the Environmental, Social and Governance (ESG) characteristics of the Fund's investment portfolio, including an assessment of climate related metrics. We wish to maintain an appropriate level of oversight and practice in this area and have increased the amount of time and governance budget assigned to this topic over time, acknowledging that this is a fast-moving and rapidly evolving area.

We have received investment training provided by our Investment Consultant ("WTW") on climate risk and the requirements of the Taskforce for Climate Related Disclosures (TCFD) requirements. Given the pace of progress around sustainable investment, Trustee training on climate and ESG has increased over recent years and is expected to remain a priority going forwards. In conjunction with our DC advisor, Hymans Robertson, we continue to prioritise climate related matters alongside other financial considerations when reviewing the investment arrangements for the DC section.

Our key overarching investment policies are detailed in the Fund's Statement of Investment Principles which can be found online at the following links:

<https://www.whitbreadpensions.com/pdfs/Defined%20Benefit%20Scheme%20Statement%20of%20Investment%20Principles.pdf>

<https://www.whitbreadpensions.com/pdfs/Defined%20Contribution%20Scheme%20Statement%20of%20Investment%20Principles.pdf>

Whilst we have delegated certain investment activities, we retain ultimate decision-making responsibility for all investment matters including identifying, assessing, and monitoring climate-related risks and opportunities, and we have oversight policies and procedures in place to ensure that such third parties are monitored and held accountable for the work they do on behalf of the Fund. The main parties to whom some form of responsibility for implementing our Sustainable Investment policies is delegated to, include:

- **Funding and Sub-Investment Committee (the "FISC")** – To ensure the effective management of the Fund, we have established a number of sub-committees including a Funding and Investment Committee (FISC). The FISC is responsible for implementing our investment strategy including the selection, retention, and removal of investment managers. The FISC acts within a Terms of Reference, which set out its duties and reporting obligations. The membership of the FISC currently includes two professional trustees who bring a wealth of wider industry expertise and experience.

Under its terms of reference, the FISC is responsible for carrying out tasks as appropriate under the four pillars of the TCFD requirements, to assist us in meeting our obligations. This includes (but is not limited to) setting the overall approach for climate risk management, working with the Fund's advisors to agree reported metrics and targets, and monitoring the underlying managers' policies in relation to Sustainable Investment (including climate). The FISC has received additional training in this area to ensure it is suitably qualified to discuss and take decisions about sustainable investment. The FISC typically meets four times per year and reports to us following these meetings.

DB Section Investment Consultant – we have appointed an Investment Consultant, WTW, to assist us in managing the DB Section's investment arrangements. As part of its mandate, WTW is responsible for ensuring ESG matters including climate change are considered as part of its advice and assistance to us including portfolio construction and the selection, retention and removal of underlying investment managers.

WTW holds membership of important industry bodies such as the Net-Zero Asset Managers Initiative as well as being a signatory to the UK Stewardship Code. The consideration of

sustainable investment is fully embedded in their investment processes. WTW works closely with the FISC and provides regular assessment of its views on the underlying managers' capabilities and performance in relation to ESG and stewardship, and a quantitative assessment of the DB Section's portfolio across a number of ESG criteria, including climate.

Our view of WTW's credentials in this area is a factor in our ongoing retention of them as our investment advisor and we have set specific objectives for them in relation to ESG and TCFD. The FISC assists us in monitoring the performance of our investment consultant on an annual basis.

DC Section Investment Consultant – we have appointed a DC investment Consultant (“Hymans Robertson”) to assist us in overseeing the Fund's DC arrangements which are implemented by Mercer. As part of this, we consider how Mercer are incorporating climate change considerations in their processes and use our role as an asset owner to hold them to account with the aim of supporting financial value over the long term.

Hymans Robertson is a signatory to the UK Stewardship Code and participated in several industry initiatives aimed at solving some of the challenges in understanding climate related issues and taking action to address associated risks and opportunities. More can be found on their website: <https://www.hymans.co.uk/services/climate-change-services/>

Our view of Hymans Robertson's credentials in this area is a factor in our ongoing retention of them as our DC advisor and we have set specific objectives for them in relation to climate change. The FISC assists us in monitoring the performance of our DC consultant on an annual basis.

- **Investment Managers** – The investment managers are responsible for managing climate change risks and opportunities within their mandates as per their guidelines. This includes the selection of assets as well as the managers' stewardship activities. The FISC receives reporting from WTW on an annual basis which includes their assessment of the managers' capabilities and performance in this area. This helps the FISC to assess the managers' approach to ESG integration and stewardship activities. As a Trustee, we expect managers to consider ESG criteria and sign up to their local stewardship code, as appropriate to their mandates. The investment managers are also expected to assist us in meeting our regulatory obligations through the provision of data in a timely manner. The FISC similarly receives reporting from Hymans Robertson and reviews the investment arrangements implemented by Mercer for the DC Section on an annual basis.
- **Other advisors** – We also takes advice from the Scheme Actuary (WTW) and Covenant Advisor (Penfida) regarding the extent to which climate change may affect the funding strategy of the Fund and the ability of the sponsor to support the Fund. We also receive updates from our Sponsoring Employer on evolutions to their strategy to manage climate change risks and opportunities, such as their commitment to Net Zero by 2040.

Case Study – EOS at Federated Hermes

We recognise that the long-term financial success of the companies that we invest in is influenced by a range of factors which includes appropriate management of environmental, social and corporate governance issues (including climate). As such, we typically invest with investment managers with the expectation of a long-term relationship, and we expect investment managers to take a similar approach with the companies that they invest in. Our Investment Consultant, WTW, engages with our investment managers where appropriate on their approach to stewardship and engagement. We have identified climate change and human and labour rights as two key priorities in this area.

In addition to the engagement that WTW undertakes directly, it has also appointed EOS at Federated Hermes (EOS) to provide engagement activities and voting recommendations. As part of its role, EOS supports the efforts of a number of the DB Section's investment managers in their company level

engagement and provides voting recommendations where applicable. EOS also carries out public policy engagement on behalf of WTW.

WTW engages with EOS on behalf of us and other investors to help shape their engagement approach and voting policies. For example, in late 2021 they discussed how to better incorporate real world impact within company net zero transition plans to help avoid the practice where higher emitting assets are offloaded to third parties who may have a worse record in the management of greenhouse gas emissions.

Through WTW and EOS, we encourage our investment managers to actively engage with companies (and other types of issuers) to improve these risks – for example, pushing a company to deliver a climate change report which sets out clear pathways to carbon neutral operations. Doing this reduces investment risk and benefits the environment. Whilst the practices of investment managers in this area have improved, the scope of the issues is complex and wider engagement with key industry bodies or regulators is also needed. Therefore, the additional public policy engagement work by EOS further supports the appropriate management of climate risk. EOS often co-leads collaborative industry efforts.

One example is Climate Action 100+ (CA100+), an investor initiative aiming to ensure the world's largest corporate greenhouse gas emitters take necessary action on climate change. It specifically targets 167 companies globally. EOS works alongside 615+ investors, with c\$65tn of assets, who have signed up to CA100+. EOS led or co-led the engagement on over 25 focus companies and is collaborating with other investors on over 30 companies as part of this initiative. CA100+ issued its net-zero benchmark for the world's largest carbon emitters in March 2021. This defined the key indicators of success for business alignment with a net-zero emissions future and the Paris Agreement goals. EOS helped to design the benchmark, which set clear engagement priorities to drive faster climate action. The plan is to refine and expand the benchmark over time and it is likely to become a key test for companies.

3. Strategy

Appropriately managing climate change risks and opportunities from a strategic perspective is an important part of our role. We recognise that climate change could have a material impact on the potential success of the overarching funding strategy and therefore we ensure that this is given sufficient consideration. In order to support this, we will conduct climate change scenario analysis on at least a triennial basis to test the resilience of the Fund’s funding strategy under a range of plausible climate scenarios. Importantly, we recognise that climate change could have a material impact on the investments of the Fund, the life expectancy of the Fund’s members and the support provided by the Sponsor’s covenant, all of which will affect the funding strategy in the future. This scenario analysis was undertaken for the first time in 2022. Our intention is to repeat this analysis at least every three years or sooner should there be a material change in either the Fund’s circumstances or the assumptions underlying the analysis.

Starting with the DB Section and given the Fund’s significantly mature funding position and short time horizon, there are limited to no new investment opportunities. However, we will continue to consider climate opportunities when making investment decisions to help identify any suitable opportunities.

We have considered what a short, medium and long-term timeframe for the DB Section could look like in relation to climate risks and opportunities:

- **Short term** - 4 years (to 2026): This time period covers the next actuarial triennial valuation and results period.
- **Medium term** - 10 years (to 2032): This time period covers expected changes in climate change data quality and regulations. In addition, the DB Section is currently expected to be at a full buyout funding level by 2032. We considered the climate change mitigation credentials of the Bulk Purchase Annuity provider when the initial BPA (in June 2022) was completed, and we will continue to assess the climate change mitigation capabilities of any future settlement provider. If this is not possible, new liability data should also be available following the 2032 actuarial valuation.
- **Long term** - 15 years (to 2037): This time period is approximately in line with the duration of the DB Section’s liabilities and the point at which a significant proportion of member benefits will have been paid out.

We have identified the following climate-related risks and opportunities:

Regulatory risk	Reputational risk	Transition risk	Physical risk
<ul style="list-style-type: none"> • Regulators are increasing pressure on pension schemes to explicitly consider climate change • Example: <ul style="list-style-type: none"> • Implementation Statement • DWP Pensions bill • Mandatory TCFD reporting 	<ul style="list-style-type: none"> • The increasing spotlight on pension schemes and climate change increases the risk of being “named and shamed” • Example: <ul style="list-style-type: none"> • 2018 EAC report on 25 biggest UK schemes 	<ul style="list-style-type: none"> • The indirect impact arising as a result of changes in society and economies to combat or adapt to climate change • Example: <ul style="list-style-type: none"> • Assets: Some industries become obsolete (e.g. coal), reinvent themselves or others emerge (electric vehicles) • Liabilities: Improvements in mortality from healthier lifestyles 	<ul style="list-style-type: none"> • The direct impact arising as a result of chronic and/or acute changes in climate and extreme weather events • Example: <ul style="list-style-type: none"> • Assets: Damage to physical assets underpinning securities (e.g. real estate and infrastructure) • Liabilities: Excess deaths arising from extreme weather

	Short Term	Medium Term	Long Term
Timeframe	To next Triennial Actuarial Valuation (2026)	Beyond expected timeframe to full buyout funding level (2032)	Broadly in line with the duration of the liabilities and beyond expected timeframe to full buyout funding level (2037)
Primary types of risk	<ul style="list-style-type: none"> Regulatory Reputational Transition 	<ul style="list-style-type: none"> Reputational Transition 	<ul style="list-style-type: none"> Transition Physical
Key risk exposure	<p>We are exposed to regulatory risks, including fines, if it does not comply with evolving regulatory requirements.</p> <p>We (and the sponsor) are exposed to reputational risks if the Trustee's policies are misaligned with peers and/or sponsor.</p> <p>We are predominately exposed to transition risks and opportunities through its illiquid assets.</p>	<p>We (and the sponsor) are exposed to reputational risks if the Trustee's policies are misaligned with peers and/or sponsors.</p> <p>We are predominately exposed to transition risks and opportunities through its illiquid assets.</p> <p>We are exposed to the impact on insurer pricing of climate risk, including the impact on future expected returns and other financial and demographic assumptions.</p> <p>Given the long-term nature of these risks, there is a high level of uncertainty in terms of the likely effect and the potential magnitude of their impact.</p>	<p>The insurer may be exposed to transition risks through its holdings in various asset classes (including equity, credit, property and infrastructure).</p> <p>The insurer may be exposed to physical risk through its holdings in various assets, in particular real assets including property and infrastructure.</p> <p>In an extreme left-tail event, exposure to, and poor management of these risks may weaken the strength of the insurer and ability to meet pensioner benefits.</p> <p>Given the long-term nature of these risks, there is a high level of uncertainty in terms of the likely effect and the potential magnitude of their impact.</p>
Potential opportunities	Encouraging existing funds to consider and where possible reduce exposure to transition risks engage with companies to develop a strong transition plan.	Aligning any new investments with the ESG policies of leading insurers may increase the likelihood of assets being taken in-specie, marginally reducing the cost of any full buyout.	N/A – Fund no longer in existence

We have conducted climate change scenario analysis by modelling the long-term horizon (15 years) over which climate risks and opportunities should be considered, given that a 15-year time period is approximately in line with the duration of the DB Section’s liabilities and covers the Fund’s expected time frame to a full buyout funding level. These time horizons, risks and opportunities are key inputs into our climate scenario analysis. We, in conjunction with the WTW and Hymans Robertson, have conducted this scenario stress testing and presented the results within this section. The key climate scenarios that we have considered are:

	Lowest Common Denominator (LCD)	Inevitable Policy Response (IPR)	Climate Emergency (CE)
Description	A ‘business as usual’ scenario where current policies continue with no further attempt to incentivise further emission reductions. Socioeconomic and technological trends do not shift markedly from historical patterns.	A delay in meaningful action but a rapid shift in policy in the mid/late 2020s. Policies are implemented but not in a completely coordinated manner, resulting in a more disorderly, but still just, transition to a low carbon economy.	An immediate, ambitious and coordinated response in which aggressive policy is pursued and more extensive technology shifts are achieved.
Approximate temperature rise vs pre-industrial levels	3.5°C	2.0°C	1.5°C
Renewable energy by 2050	30-40%	80-85%	80-85%
Transition risk level (shorter term)	Low	High	Medium – High
Physical risk level (longer term)	High	Low – Medium	Low

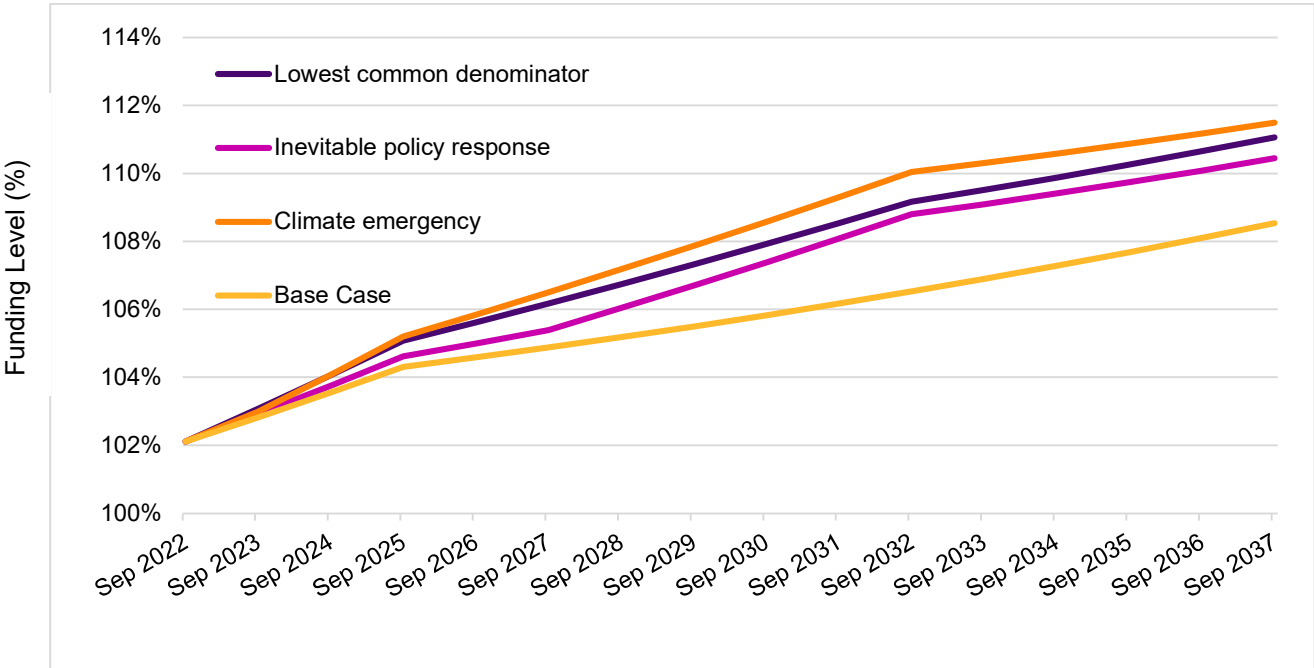
These scenarios were compared to a base case scenario, which is that climate change is currently priced into markets as a “business as usual” outcome but with no physical risk expected from climate change. The scenarios were created to reflect the differing paths that could be taken to meet, or fail to meet, the Paris Agreement target. The Paris target is to limit global average temperature increases to 1.5°C above pre-industrial levels, foster climate resilience and facilitate capital flows. 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. We are aware of the limitations of the climate scenario analysis, such as the reliance on third parties for the maintenance and reporting of accurate data, validation of our assumptions, and the information available at the date of the analysis and recognize that there is the potential for more extreme outcomes than reflected in the chosen scenarios.

Below we have illustrated the impact of the three climate change scenarios on the DB Section’s funding level over the long-term horizon (15 years), relative to the funding projection as at 30 September 2022 (based on the asset allocation as at that date).

In some climate scenarios, our modelling process implies reduced life expectancies (relative to other scenarios and/or schemes’ central mortality assumptions) and therefore a relative reduction in the DB Section’s liabilities. This is a plausible potential outcome arising from the negative impacts of increasing climate change. This can suggest a relative improvement in the expected funding position even when combined with associated reductions in the value of the assets (given their low-risk nature). However, it is important to recognise that an assessment of what is in the best interests of the

DB Section and its members is a much broader question than the impact on funding level alone. Key considerations may be a reduction in the quality (and length) of members’ lives, and the quality of the environment that they will retire into. Consequently, the results of any such modelling should not be assumed to reflect any complacency or acceptance (either implicit or explicit) that we consider global inaction or business-as-usual with respect to climate change to be in the best interests of the DB Section or its members. We believe that climate change is a systematic risk of unprecedented scale and severity. Actions to address it are a collective priority, given the risks it presents to individual pension schemes, the ongoing resilience of the savings universe, and the planet as a whole.

DB Section – Funding Level Impact (Long Term Horizon)



DB Section – Funding Level Impact	Lowest Common Denominator (LCD)	Inevitable Policy Response (IPR)	Climate Emergency (CE)
Annual impact on asset return (weighted average across time horizon)	-0.1%	+0.0%	+0.2%
Annual impact on liabilities (weighted)	-0.2%	-0.1%	0.0%

Given the DB Section’s low level of investment risk and relatively short time horizon, there is limited impact on asset returns from climate change in the three scenarios shown. The allocation to Secure Income Assets (SIAs) means that the DB Section is resilient to, and even could benefit from, transition risk as these assets are expected to be positioned well for a transition to net zero. Given the level of transition risk in each scenario this leads to an increasingly positive impact to the asset return (in the Climate Emergency scenario), up to the medium-term horizon (10 years). Increasing beyond 10 years, the impact of physical risk on these SIAs starts to negatively impact the asset returns.

<p>average across time horizon)</p>	<p>The economic and social consequences of the disorderly transition and failure to address the risks of climate change results in a limit to future improvements in mortality. The impact on liabilities stays constant across the 0 to 15 year time horizon.</p>	<p>Whilst the direct impacts in mortality may be similar to those under an orderly transition, the transitional effects and imbalance between the activity of different individuals and organisations result in a deterioration in expectations for longevity improvements relative to typical pension scheme funding assumptions. The impact on liabilities stays constant across the 0 to 15 year time horizon.</p>	<p>The changes required to address climate change in an orderly and coordinated manner require substantial changes in the actions of individuals and organisations and are such that people follow a healthier and more active path with the economic activity generating an improvement in living standards. The impact on liabilities stays constant across the 0 to 15 year time horizon.</p>
<p>Funding Level impact</p>	<p>The impact of the negative shock to liabilities leads to a strong positive impact on funding as of a result of transition risks, which is then partially negated with the negative impact of the physical risks impacting asset returns post the 10 year point. Despite this, the funding level increases at a faster rate than the base case scenario.</p>	<p>In the earlier years, the reduction in liabilities dominates the improvement in funding level whereas in later years, the improvement in asset returns contributes positively to the funding position too. Post 10 years, there is a slight negative drag on asset returns as a result of the physical risk impact, however, overall across the 15 year time period, the funding level still increases at a faster rate than the base case scenario.</p>	<p>The impact of the most positive asset returns on the funding position leads to an improvement in the funding position, outweighing the impacts on the liabilities. The physical risk impact on the assets from 10 to 15 years means that the journey plan is marginally less upward sloping, but similar to the other two scenarios, across the whole period, the funding level increases at a faster rate than the base case scenario.</p>

Overall, the DB Section appears to be resilient under the three scenarios to climate risks as a result of its remaining asset allocation to SIAs which are expected to fare well in the climate transition and strong funding position with an associated low target return. The resilience of the Fund to these climate scenarios, combined with the DB Section nearing its goal of a full buyout funding level within the medium-term horizon, means that the DB Section’s investment strategy is unlikely to change as a result. The DB Section is already invested in some climate-related opportunities, and we expect the portfolio of illiquid assets to reduce over time as the Fund reaches a full buyout funding level. For the purpose of the modelling, the Pension Funding Partnership (PFP) asset value was removed (although retained the income stream assumptions) due to complications in the modelling of climate impacts of contingent assets, and the low likelihood of the Fund receiving the asset value.

As part of the above analysis, we have also considered how the Sponsor could be impacted under the above climate scenarios considered. Whilst the Sponsor’s own risk assessment of climate risk identified a number of transition and physical risks whose impact is expected to increase over time, it is noted by the Covenant advisor (Penfida) that the Sponsor is seeking to mitigate the potential impacts of these risks by focusing on the reduction of the use of natural resources, incorporating physical risks into its planning decision and improving the resilience of its estate to extreme weather events.

Given the significant headroom in the covenant and the relatively short length of covenant reliance of the Fund, and the actions that are currently being undertaken or considered by the Sponsor to address potential climate change risks, Penfida believes that climate change related risks from a covenant perspective are low. Given the very strong funding position of the DB Section, we have a relatively low likelihood of reliance on the Sponsor in the future combined with a short-time horizon as well.

As a result of the combined analysis, our assessment is that the investment and funding strategy of the Fund is resilient against climate risk, and that it is expected to be relatively well protected against the impact of climate change. This was driven by four key factors:

- **The DB Section's very strong funding position** – This was 102% (on a gilts+0.5% basis) at the date of the analysis conducted
- **The DB Section's very low-risk asset portfolio** – The DB Section has a low level of 'return-seeking' assets targeting a small investment return of Gilts+0.75% per annum.
- **The allocation to climate positive investments** – The DB Section has a reasonable allocation to investments which are expected to benefit from the transition to a low-carbon economy. These include investments in renewable energy investments.
- **The DB Section has a BPA asset** – We have already mitigated some of the life expectancy risk within the Fund, with a large BPA which was completed in June 2022.

Although the analysis provided us with some reassurance on the robust nature of the DB Section's funding strategy, it did clearly highlight that climate change could have a material impact on the Fund's outcomes. This reiterated to us that it warrants continued focus as part of our broader SI strategy and should remain a priority area for portfolio monitoring, stewardship activities and manager engagement. In terms of next steps, we are focusing on the following:

- Ongoing training for the Trustees to ensure effective decision-making in relation to consideration of climate risk
- Engagement with fund managers through the Investment Consultant
- Pursuit of securing all the DB section's liabilities through purchase of one or more BPAs

As mentioned earlier, we intend to update this analysis at least every three years and will be testing annually whether this needs to be done more frequently, including if there have been material changes to the scenarios used or the DB Section's funding strategy.

DC Section – Climate Scenario Analysis

Climate-related risks can be broadly classified into two categories:

Transition to a low carbon economy, including (but not limited to):

- **Policy changes**, e.g. carbon pricing, seek to create the changes needed in society;
- **Technology development**, e.g. renewable energy, and adoption enable the changes to be adopted.

Physical impacts, including (but not limited to):

- **Chronic changes**, e.g. sea level rise, agricultural systems impact economic and social systems;
- **Acute changes**, e.g. storms, wildfires create damage and give rise to costs of adaptation and reconstruction.

Scenario analysis

We are required to undertake analysis to explore the potential impact of different future climate scenarios on the Scheme, which can capture the impact of transition and physical impacts. The Task Force recognises that the use of scenarios in assessing climate related issues and their potential financial implications is relatively recent and that practices will evolve over time, but believes that such analysis is important for improving the disclosure of decision-useful, climate related financial information. At least two of the scenarios must be aligned with the objectives of the Paris Agreement (i.e. a reduction in global warming potential to between 1.5°C and 2°C above pre-industrial levels), and one scenario should be based on a more pessimistic outcome. With the support of our advisors, we have undertaken climate scenario analysis at the asset class level to estimate the effect of different climate scenarios on retirement outcomes for different members of the DC Section. We have explored the following real-world scenarios as part of this analysis:

Scenario	Description
<p>Green revolution</p>	<p>Concerted policy action starting now e.g. carbon pricing, green subsidies. Public and private spending on “green solutions”. Improved disclosures encourage market prices to shift quickly. Transition risks in the short term, but less physical risk in the long term. A relatively high expectation of reducing global warming to <2°C.</p> <p>When modelling this scenario, we have assumed a greater likelihood of market disruption in the short term driven by mainly transitional impacts. The likelihood of material long-term physical climate impacts is lowest under this scenario.</p>
<p>Delayed transition</p>	<p>No significant action in the short-term, meaning response must be stronger when it does happen. Shorter and sharper period of transition. Greater (but delayed) transition risks but similar physical risks in the long term. A relatively high expectation of reducing global warming to <2°C.</p> <p>When modelling this scenario, we have assumed a greater likelihood of market disruption in the medium term driven by mainly transitional impacts. The likelihood of material long-term physical climate impacts is slightly higher under this scenario.</p>

Head in the sand

No or little policy action from governments for many years. Growing fears over ultimate consequences leads to market uncertainty and price adjustments. Ineffective and piecemeal action increases uncertainty. Transition impacts exceeded by physical risks. Little or no expectation of reducing global warming to <2°C.

When modelling this scenario, we have assumed a greater likelihood of market disruption in the long-term driven by transitional impacts and material physical climate impacts.

These scenarios were chosen as they satisfy the guidance provided by the Department for Work and Pensions, and provide an intuitive way to help us understand the range of potential impacts different climate scenarios may have in terms of member outcomes. By taking a broad view, across a range of stressed scenarios, we feel we will be well placed to take action (where appropriate) to manage the most severe potential impacts.

At the time of writing there is no industry consensus on how to model different climate scenarios. We have therefore relied on the views of our advisors for the DC Section, underpinned by their research and development. We expect our advisor to continually test whether their approach represents good practice relative to the wider industry and to be proactive in suggesting revisions to improve over time.

The main limitation is that the future is unknown, and as for any forward-looking modelling, requires assumptions to be made. These assumptions may or may not be borne out in practice, so the outputs from this analysis should not be relied upon as an exact assessment of potential member impacts which could be better or worse than indicated. This limitation cannot be removed, but managed over time by monitoring

For Defined Contribution arrangements such as the DC Section, impacts should in the first instance be considered as the impact on retirement outcomes for different cohorts of members. This is in line with the requirement to define short, medium and long-term in the context of assessing climate risks. These time periods are defined as follows:

- **Short-term:** Members who are between 5 and 10 years from their retirement;
- **Medium-term:** Members who are between 15 and 20 years from their retirement;
- **Long-term:** Members who are more than 35 years from their retirement.

The following table sets out the results of the climate scenario analysis for different cohorts of members. It should be noted that these are all stressed scenarios, and therefore generally reveal a 'worse' position relative to central expectations. For the purpose of the analysis, a representative 22 year old and a 39 year old member have been considered:

Impact on retirement outcomes for different climate stresses	22-year-old member	39-year-old member
Green revolution	-4%	0% to +1%
Delayed transition	-3% to -4%	-1% to +1%
Head in the sand	-2% to -3%	-2% to -4%

In general, older members are expected to be relatively well shielded from wider market disruptions caused by emerging transition and physical climate risks. This is because they are invested across a range of markets, providing diversification. Conversely, younger members will be more exposed to a delayed climate transitions because the timing of transition and physical climate risks will be borne when they have accumulated sizeable levels of retirement savings.

We have concluded that strategic asset allocation decisions (particularly use of illiquid assets) could impact real-world climate risks and opportunities for members, and consequently their long-term retirement outcomes. In the short to medium term, we believe that there is substantial scope to make progress through more traditional building blocks such as equities and bonds.

We believe that climate risks and opportunities will be better managed through implementation decisions, which could improve financial outcomes within asset classes, and effective stewardship, and engagement, with underlying companies to drive real world changes.

It is challenging to determine which climate-related risks and opportunities are likely to be most significant, particularly given these are likely to materialise over different time horizons. We believe that transition-related risks, such as the impact of policy intervention, are likely to impact more significantly in the short to medium term, and by nature could trigger sudden shocks or impacts in markets. For this reason, we encourage our investment manager to engage with underlying companies to ensure they are planning appropriately for the transition to a lower carbon world, with the expectation that this will help to limit more severe impacts from policy intervention. Our investment manager has demonstrated a strong track record for engaging on climate issues and we will continue to monitor and hold them to account via our advisors.

With improved availability of data, and evolution of analytical techniques, we believe that we'll be in the position to evaluate the potential impact of discrete climate-related risks in more detail and put in place further refined plans to manage these.

4. Risk Management

Climate change is an important risk and opportunity and therefore is considered as part of the Fund's ongoing risk management processes. Having a robust framework for identifying, managing, and mitigating climate risks enhances the prospects of better member outcomes. We receive regular training and advice on Sustainability and climate risk from the Investment Consultant.

There are three ways in which the risk management processes integrate climate:

Governance

Climate change is included within the Trustee's risk register which is reviewed quarterly and in-depth annually. Over the year the Fund's investment risk register was updated to expand the consideration of climate risk. This clearly details the impact and likelihood of the risk, and the mitigating controls in place and the actions we take to manage, mitigate, and exploit both this risk and opportunity. This includes the consideration for transitional and physical risk (discussed within the Strategy section of the report) and their potential impact on the Fund. The FISC's views on Sustainable Investing and climate factors are incorporated into the SIP.

As mentioned in the Governance section of this report, although we retain ultimate ownership, the risk register sets out the parties (such as the FISC) that assist us and our responsibilities. The FISC take account of risk measurement, mitigation, monitoring and strategic actions as they relate to climate change.

We receive regular training and advice on climate risk from the Investment Consultant. We have included a specific objective on climate risk for our Investment Consultant and we review their performance relative to this objective on an annual basis.

Top-down

The climate change scenario analysis presented to us, mentioned in the previous section, provides us with a holistic overview of the potential impacts of climate change and how they may affect the Fund's funding strategy (across assets, liabilities and covenant) and investment positions. This is an important risk management tool for a top-down risk and opportunity assessment.

Bottom up

As mentioned, we also conduct more granular analysis to manage the risks and opportunities associated with climate change. These include:

Security analysis – We calculate various climate change related metrics for the underlying securities within the portfolio. This includes metrics such as total carbon emissions, carbon footprint, science-based targets as a percentage of assets and data coverage. These provide us with a more detailed understanding of the Fund's exposures and provide useful measures by which to determine the climate change impact of investment, funding and other strategic decisions.

Manager analysis – We also conduct an annual review of the investment managers' and the Investment Consultants' approach to climate, which is incorporated as part of the annual sustainable investment reporting. In addition, engagement with managers (through the Investment Consultant) is conducted on areas including climate risk, as part of manager due diligence. The Investment Consultant challenges the investment managers on their ongoing approach to stewardship matters (including those relating to climate change). A summary of the managers' voting statistics and a selection of the most significant votes cast over the year are disclosed in the SIP Implementation Statement which is reviewed on an annual basis by us.

5. Metrics and Targets

A key facet of our ongoing monitoring and management of climate change is having good data on the Fund's exposure in this area. Although there are limitations with some of the metrics presented and the completeness of data, we still have a strong belief that these can helpfully inform the ongoing monitoring and management of the Fund. We consider metrics across the SI spectrum, but the focus within this statement is those in climate change. The metrics disclosed have been selected from the following categories:

- **An absolute emissions metric** - the total greenhouse gas emissions attributable to the Fund's assets
- **An emissions intensity metric** - the total greenhouse gas emissions attributable to the Fund's assets per some form of unit (such as currency/company revenue)
- **An alignment metric** – a metric to quantify alignment to a 1.5 degree temperature rise in line with the Paris Agreement
- **One additional climate change metric** – an additional metric of Trustees' choice

As this is the first year in which the regulations apply, we are only required to consider Scope 1 and Scope 2 emissions, rather than additionally including Scope 3 emissions. These terms mean:

- **Scope 1 emissions:** all direct emissions from the activities of an entity or the activities under its control
- **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
- **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

Scope 3 emissions are significantly more difficult to calculate than scope 1 or scope 2 emissions for any given entity. It is also the case that, for some assets, even scope 1 and scope 2 emissions are difficult to calculate. We agreed not to include Scope 3 in the calculations because this level of scope is highly estimated, leading to an increased unreliability of the output and because the regulations do not require Scope 3 emissions to be included in the first TCFD disclosure.

We are using best endeavours to make as full a disclosure as possible, subject to overriding constraints of reasonable time and cost for doing so. We (through the Investment Consultants) are working actively with investment managers to improve the quality of the data supplied for these purposes over time.

Overview of analysis

The following table details the rationale for choosing these metrics from the available pool:

Metric	Definition	Rationale
Total Carbon Emissions ("tCO2e")	An 'absolute emissions' metrics which gives a measure of carbon emissions attributable to the Fund. This is calculated in line with the Greenhouse Gas (GHG) protocol methodology and currently includes only Scope 1 and 2 emissions.	Determined by the regulator
Carbon Footprint (tCO2e / \$ invested)	An 'emissions intensity' metric which gives a measure of how many tonnes of CO2 emissions each million invested causes.	It provides a direct measure of absolute emissions, which ultimately impact global outcomes and provides a simple comparable measure across portfolios of different sizes

Percentage of assets with approved Science based targets (“SBTi”)	A ‘portfolio alignment’ metric which is a forward-looking measure of the percentage of assets with targets validated by the Science-Based Targets Initiative.	It provides a consistent verification of a company’s alignment to the Paris agreement.
Implied Temperature Rise	This metric provides us with a measure of how well the underlying holdings of a fund align with global climate goals which is then converted into a degree of temperature rise	Easy to understand to express portfolio alignment with global temperature targets
Data coverage/quality	A measure of the proportion of the Fund’s assets for which we have high quality audited data, proxied data, or no data at all. The data quality % covers both reported and estimated data.	We believe it is important to monitor this as climate metrics are at an early stage and data is currently limited. We also believe that improved data quality and coverage is an area that we (through the Investment Consultant) can most influence our investment managers and improvements would allow better decision making on future carbon metrics.

The following table details the statistics for the 4 selected Metrics:

	DB Section	DC Section
Total Carbon Emissions (“tCO2e”)¹	29,057 tonnes	23,505 tonnes
Carbon Footprint (tCO2e / £m invested)²	31 tonnes	90 tonnes
% of assets with approved Science based targets (SBTi)³	37%	n/a
Implied temperature rise	n/a	2.8 degrees
Data quality (reported / estimated)⁴	83% (0.0% / %) 0.0% / 83%	71.2% (59.5% / 20.7%)

Data Quality: In calculating absolute emissions and carbon footprint, we were only able to obtain data on 83% of the (return seeking) portfolio. As at 31 March 2023 the return seeking portfolio made up c22% of total DB Section assets. All of the underlying carbon emissions data has been sourced from MSCI. CO2e represents a single unit of measurement for total greenhouse gas emissions (often referred to as CO2 and

¹ Total Carbon Emissions have been calculated based on the value of assets for which data is available rather than pro-rating to reflect 100% of the assets. For the DB section this is tCO2e scope 1 + 2 emissions – ex sovereigns. Data as at 31 December 2022. Data quality is provided based on the total actual and estimated data for total carbon emissions

² tCO2e scope 1 + 2 emissions / \$m invested attributed by EVIC for the DB section. Data as at 31 December 2022

³ Percentage of assets with approved Science based targets is weighted by investment manager allocation as at 31 December 2022 excluding investment managers where no data was provided.

⁴ Data coverage is provided based on the total actual and estimated data for total carbon emissions excluding sovereign bonds. All data provided in the DB section covers the return-seeking assets only (i.e. excludes the BPA and LDI portfolio, the latter of which is reported separately)

equivalents) and includes the seven gases mandated under the Kyoto protocol. We (through the Investment Consultants) are working actively with the Fund's investment managers to improve the quality of the data supplied for these purposes over time. We intend to monitor how these metrics evolve over time on an annual basis and understand the drivers for change. We have established a timeframe of four years (in line with the short-term timeframe) to allow its investment managers to reach 95% of data quality (either reported or estimated). We believe this is a stretching but achievable target. We may then look to implement a different target.

The BPA is an insurance policy and not included in the metrics calculations as under disclosure rules it is not included as part of the calculations and it is the responsibility of the insurer. The ESG credentials of the BPA provider were considered as part of the selection process. The above table and target also exclude emissions attributable to the DB section's government, government related and derivative assets. These assets are reported separately below based on information provided by the LDI manager. The reason for the separate disclosure is because the underlying methodology is materially different. We primarily hold UK gilts as assets to hedge the Fund liabilities and as such, even if reducing exposure to these assets would lead to an overall improvement in climate metrics, it would open the Fund up to excessive funding risk. We also have limited capacity and ability to engage with the UK Government on climate related metrics. Whilst we believe it is sensible to exclude liability hedging assets from the target, we believe it is still useful to monitor these figures over time. As such the table below shows the climate metrics provided by the DB Section's LDI manager, Insight.

Metric Description ¹	Insight (As at 31 December 2022)
Total Carbon Emissions ("tCO₂e")	154,000 tonnes
Carbon Footprint (tCO₂e / £m invested)	175.3 tonnes
Data quality (reported / estimated)²	95.9%

Limitations - As part of its formal guidance the DWP recognises potential gaps in being able to obtain data and the challenges that may arise in relation to the qualification of climate risks, and in doing so highlights that trustees should carry out the required analysis under TCFD "as far as they are able". Whilst we have endeavoured to accurately reflect the emissions of the Fund's underlying portfolio in collecting and analysing the data, this remains a developing area, giving rise to a number of limitations, particularly given the illiquid nature of the overall portfolio. As such, we expect accuracy to evolve and improve over time. The analysis excludes the PFP.

¹ Insight have used government and other sources to calculate the figures referenced in this report. Interest rate swaps, inflation swaps, futures, cash and money market fund holdings have all been excluded. Short gilt positions have also been excluded. Scope 3 emissions are not included. Figures cannot be sensibly aggregated with emissions data for non-gilt assets due to the risk of double counting