Climate related Disclosures

Report prepared in alignment
with the recommendations of the TCFD

Money Purchase Section of the Cheviot pension

An authorised Master Trust

July 2022

Approved 28 July 2022

INTRODUCTION

Impact of climate change

Climate change is defined as a change of climate, directly or indirectly attributed to human activity, that alters the composition of the global atmosphere, and which is in addition to natural climate variability, observed over comparable time periods (UN Framework Convention on Climate Change).

The Task Force on Climate-related Financial Disclosures (TCFD) consists of 32 members from across the G20, representing both preparers and users of financial disclosures. The TCFD is chaired by Michael R. Bloomberg, founder of Bloomberg L.P. Its goals are "to develop recommendations for more effective climate-related disclosures that could promote more informed investment, credit, and insurance underwriting decisions and, in turn, enable stakeholders to understand better the concentrations of carbon-related assets in the financial sector and the financial system's exposures to climate-related risks."

The TCFD is committed to market transparency and stability. It believes that better information will allow companies to incorporate climate-related risks and opportunities into their risk management and strategic planning processes. As this occurs, companies' and investors' understanding of the financial implications associated with climate change will grow, empowering the markets to channel investment to sustainable and resilient solutions, opportunities, and business models.

Cheviot's response

This report sets out the actions and analysis undertaken by the Trustee in line with the recommendations for improved reporting and transparency in relation to climate related risks and opportunities as set out by the TCFD in respect of the Money Purchase Section. The Money Purchase Section provides wholly defined contribution benefits and therefore there are no relevant covenant issues.

The report reports on the scheme year January 2021 to December 2021. The Trustee's approach is proportionate to the assets under management (circa £160m as at 31 December 2021) and the use of an investment platform which restricts direct engagement with managers. The use of pooled funds also restricts engagement with the underlying companies. The report meets the requirements of the guidance and requirements set out in relation to climate related risks.

Cheviot's investment beliefs

The report is underpinned by the Trustee's core investment beliefs in relation to climate change:

- The Trustee believes that climate change will be a financially material factor now and increasingly so in the future.
- Failure to meet the Paris Agreement will have a significant negative impact on members, investments and the wider financial structure.
- Long term investors have an opportunity to influence managers and companies in relation to climate change issues.

As a result of its work and improved understanding in this area during the last 18 months, the Board has approved a bespoke net zero commitment by 2050, reflecting the Paris Agreement's objectives. It also reflects the Board's fiduciary responsibilities to members and employers and the need for governments and policymakers to deliver on their commitments to achieve the temperature goals of the Paris agreement.

This, Cheviot's first TCFD report, has been approved by the Investment Committee using delegated powers from the Trustee. The members' factsheet is attached to the end of this document.

Sir Derek Morris

Sir Derek Morris
Chair, Cheviot Trustees Limited

Approved 28 July 2022

Section 1 – GOVERNANCE

Climate oversight[1]

1.1 As an authorised Master Trust, Cheviot has a strong governance structure which is documented in a detailed Governance Policy. Changes were made to the Governance Policy in September 2021 to update the investment beliefs to reflect climate change investment beliefs in more detail and to include a new Appendix setting out the Trustee's climate change policy.

1.2 The policy sets out the Investment Committee's approach to evaluating and monitoring climate related risks and opportunities (CRRO)[1] under delegated powers from the Trustee.[2] The policy covers the four areas identified by the TCFD as crucial to the management of climate change risks.

- Governance structure, including training and assessment of the capabilities of its advisers and service providers on climate related risks and opportunities
- Strategy for assessing the impact of climate related risks and approach to opportunities over different time periods
- Risk management
- Metrics and targets.

Governance

1.3 The Trustee concluded that the Investment Committee was best placed to undertake the level of detailed consideration required in respect of climate change issues. The Investment Committee has delegated powers in this area and provides quarterly updates to the Board. It also consults the Board on key decisions. The Investment Committee met nine times in 2021 and has met monthly during the first six months of 2022. This facilitates detailed discussions about climate-change issues.

1.4 Climate change is a substantive standing item on Investment Committee agendas and its members must have sufficient experience and understanding to review this area. To facilitate this, the members of the Investment Committee have received extensive training in this area during the last 18 months. The Investment Committee continues to receive regular training all aspects of the identification, assessment and management of risks to and opportunities for the Trust from the effects of climate change. The members of the Investment Committee assess their own skills annually and regularly challenge advisers.

Trustee Knowledge and Understanding

1.5 All members of the Investment Committee attended seven and a half hours of climate related training and discussion during 2021. Discussions and training have continued in 2022. Most members have also attended external training sessions provided by alternative providers. Climate change is a standing item on Investment Committee agendas. All Trustees have also attended specific climate related training and have regular updates at each Board meeting.

Assessment of advisers

1.6 The Investment Committee will assess the experience and support of the Investment and other advisers and service providers in this area at least annually against the ISCWG checklist where appropriate. All advisers are required to provide an annual declaration that training consistent with the professional requirements has been undertaken, including adequate climate-related risk training for the activities being undertaken for the Trust. The Investment Committee ensures that information about the scheme that is relevant to the identification, assessment and management of risks and opportunities relating to climate change is shared between the persons tasked with those involved in governance activities that include climate risk management.

1.7 The relevant advisers and service providers assessed by the Investment Committee in this regard are:

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[1] As required by the Occupational Pension Schemes (Climate Change Governance and Reporting) Regulations 2021, Schedule 1, Part 2, 27(a)

Adviser	Role
Cheviot Management	Governance Support and Financial Information
Isio	Independent Investment Oversight
Mobius Life Limited	Platform Provider
PTL	Independent Trustees, in their capacity of supporting with various governance and operational matters
Schroders Solutions[2]	Investment Consultant and Asset Manager

1.8 The key advisers in relation to identifying, assessing and managing any climate-related risks are the Trustee's investment advisers, Schroders Solutions. Schroders have worked closely with the Investment Committee during the last 18 months to identify and quantify as far as possible the climate related risks and opportunities of the current investment portfolio. The investment adviser objectives agreed with Schroders have been revised to incorporate specific items relating to the assessment of climate related risks and opportunities and the provision of relevant climate scenario analysis to ensure compliance with TCFD reporting.

1.9 Schroders are committed to responsible investment and are UN Global Compact and UN Principles of Responsible Investments signatories, for which Schroders has been granted the highest score of A+. Schroders are committed to improving clients' portfolios from a sustainable perspective and the Head of Sustainable Solutions, Barbara Wilson, has been leading on advising the Trustee and Investment Committee in respect of this report.

1.10 Schroders' expertise has been demonstrated throughout the various discussions. The Investment Committee has attended various external seminars on climate change issues and some members have experience of advice from other advisers in the area. The Investment Committee raised questions regarding the information presented to them during the scheme year. The Investment Committee members are confident in their ability to assess and challenge Schroders if required. For example, the Investment Committee:

- asked for specific examples of the potential impact of a drop in US GDP by 60%
- challenged the compatibility of an industry standard net zero commitment with the Trustee's fiduciary responsibilities and concluded that a bespoke commitment was more appropriate
- asked for more information about the impact that any net zero commitment would have on current investment strategy
- challenged the wording proposed in relation to "greenwashing" and
- challenged the appropriateness of the scenarios in terms of likelihood and relevance.

1.11 Going forward, the Investment Committee will encourage and expect all asset managers to provide details of their climate related strategy, recognising that the use of pooled funds and an investment platform limits the Trust's ability to directly engage with managers or underlying companies.

1.12 Other advisers, including the Scheme Actuary, have confirmed that they have sufficient expertise in relation to climate related issues to undertake their role. This declaration will be included in the existing annual process for confirming fit and proper status and competency training and experience.[3]. The previous Finance and Operations Manager attended all the Investment Committee climate related training. The current Finance Manager is now attending all Investment Committee meetings and has access to all the previous papers to provide him with the relevant background.

[2] Schroders Solutions acquired the previous advisers, River and Mercantile Investment Solutions, on 1 February 2022. All references before 1 February 2022 refer to River and Mercantile.
[3] The Occupational Pension Schemes (Climate Change Governance and Reporting) Regulations 2021, Schedule 1, Part 2, 27(b)

Section 2 – STRATEGY

Background

2.1 The Investment Committee considered the Climate Action Tracker 2100 warming projections based on pledges and current policies. It particularly noted that for global warming to peak at 1.5% by 2100, emissions need to reach net zero by 2050. It has also considered the impact of population growth. It has also discussed the Paris Agreement and the actions agreed by Governments whilst recognising that the proposed policies and actions required a broad global response to be effective.

2.2 The discussions concluded that:

- Climate-related risks are systemic and therefore it is not possible to hedge against them
- Climate change will impact the global economy fundamentally
- Climate change risk is an essential part of our strategic investment decision making.

Scenario analysis

2.3 The Investment Committee considered three different climate scenario models which brought together climate science and economics.

2.4 The scenarios align with the TCFD requirements: Orderly Paris, Disorderly Paris and Failed Transition (where Paris refers to a global warming scenario between 1.5% and 2%). These scenarios are in line with the Pensions Climate Risk Industry Group (PCRIG) and cover a spectrum of plausible climate pathways that model potential directions of future climate policies and interventions. The pathways differ in terms of policy and technology changes, physical risks and pricing in mechanisms. The Investment Committee believes that climate change will fundamentally impact on how the global economy performs and identified the key risks as transition risks, physical risks, impact on GDP and the impact on financial markets.

2.5 Climate scenario analysis is a complex and detailed process and there are some important limitations to the modelling. The scenarios are hypothetical and not forecasts or predictions and therefore very sensitive to inputs. Similarly, the analysis assumes that the investment strategy is constant and set. In reality, the strategy will evolve and change in reaction to progress or otherwise towards the objectives of the Paris Agreement.

2.6 The scenario analysis set out the potential relative impact on the core Money Purchase Section funds used in the Cheviot Lifeplan[4] compared to a baseline target return assumption. The climate scenario shocks are the median from a range of possible outcomes. The analysis did not allow for changes in asset allocation over time. The analysis was conducted over three periods: five years (short-term), ten years (medium-term) and forty years (long-term). These time periods were determined appropriate by the Investment Committee taking into account the scheme's liabilities and its obligations to pay benefits. These periods were selected to identify the risks to members close to retirement, members starting to derisk before retirement and younger members with a much long investment time horizon.

2.7 The key outcomes of the scenario analysis were:

- A failed transition[5] provided the most positive outcome in the very short term but as physical risks begin to increase, returns fall significantly in the mid to late term. This will impact members over the forty-year time horizon.
- Paris disorderly[6] analysis indicated that the impact over the short-term could be severe and sudden and pose a real risk to DC members approaching retirement over the next 5-10 years.

[4] The default option under the regulations.
[5] No transition - Paris Agreement goals not met, failure to transition away from fossil fuels, physical climate related risks are severe and increase over time, causing widespread social and economic disruption.
[6] Disorderly transition - Paris Agreement met but an abrupt transition, little climate action in the short term, following by a sudden tightening of policy to get on track with Paris. Policy and technology shock likely.

- Paris orderly[7] had a significantly lower impact over timeframes longer than five years and resulted in better expected returns for members.

2.8 The scenario analysis indicated that across all scenarios long term returns are negatively impacted by the risk posed by climate change. However, the lowest estimated impact was from the orderly transition to 1.5 degrees by 2050 i.e. the Paris Aligned scenario. Therefore, the Trustee concluded that aligning to the Paris Agreement is likely to have the least detrimental impact on long term investment returns. The Trustee concluded that the investment strategy should align to a Net Zero transition to reach Paris Alignment over time and the Investment Committee are working with Schroders to incorporate this within their investment strategy.

2.9 The Investment Committee undertakes an annual review of the inclusion of ESG considerations in respect of the selection of investment manager and the approach of the underlying managers to ESG. Going forward, it will continue to assess mandates from an ESG perspective but also consider the managers alignment to the Paris Agreement.

2.10 These results were in line with the Trustee's belief that supporting the Paris Agreement was the best outcome for members. The strategic implications identified were:

- The primary driver for the difference in impact between funds is the equity allocation, equities being the least resilient asset class with high exposure to US and to sectors that are more exposed to both transition and physical risk. More focus on the composition of the equity is seen as key.
- High yield bonds were more exposed to physical risk over long time horizons compared to investment grade bonds.
- Gilt and cash are the most resilient assets but produce lower returns which are inconsistent with good retirement outcomes for members.
- Transition risks may occur sooner than anticipated (impacting members approaching retirement over the next 5-10 years significantly as they disinvest their funds).

2.11 The Investment Committee agreed to review the allocations in the Cheviot Lifeplan in the context of climate risks and alignment with the Paris Agreement and to consider opportunities to increase resilience with the equity portfolio by allocating to more climate transition/Paris aligned equity funds. It will also focus on engagement with managers (recognising the limitations of pooled fund investment) and consider collaborative engagement initiatives. The high yield bond allocation in the Moderate fund will be considered particularly in the context of assessing the underlying investment managers on their approach to managing risks.

2.12 The Investment Committee concluded that climate change must be an essential part of asset allocation with the potential for regional and sectoral decisions becoming more material. As a result, after much discussion and debate, the Investment Committee agreed to adopt a bespoke net zero commitment rather than an industry standard. The intention is to recognise the interdependency of any individual commitment and government policy and the requirement for Trustee to act in accordance with its fiduciary responsibilities to members.

[7] Orderly transition - Paris Agreement met through emission reductions starting now and continuing in a measured way in line with the Paris objectives and the UK'S government commitment to reducing emissions in the UK to net zero by 2050.

Net zero commitment

As stewards of our members' capital, we have a responsibility to deliver investment returns and manage risk over the long term in line with our fiduciary duties. We recognise the climate crisis that is facing the globe. The transition to a lower carbon world will impact every inhabitant, economy, and investment, either positively or negatively. Our fiduciary duties require us to identify the risks and opportunities that are present and invest accordingly.

A world where global warming is not contained to significantly below 2 degrees above pre-industrial levels is expected to impact overall portfolio returns and risks. Countries across the globe are making Net Zero Commitments. This will be followed by new policies and regulations that will impact the companies we invest in and lend to, and the associated risks and returns our portfolio can deliver.

The Trustee will manage its investments in line with achieving net zero emission greenhouse gas emissions by 2050. Our commitment is based on governments and policymakers delivering on their commitments to achieve the temperature goals of the Paris Agreement.

The Trustee will keep this under review to ensure it aligns with members' interests and trustee fiduciary duties.

Cheviot Trustees Limited
July 2022

Section 3 - RISKS, METRICS AND TARGETS

Background

3.1 Cheviot has a robust risk assessment process in place which assesses the impact and probability ratings. Risks as overseen by the relevant Committee. The climate related risk is assessed as a red risk (impact 5 and probability 4) given the uncertainty of the situation, current likelihood of a failed transition and the financial impact that would result for different sections of the membership over different timescale. The analysis is based on the scenario analysis undertaken which assessed the impact of climate change in the context of transition risks, physical risks, impact on GDP to each asset class and the potential impact on financial markets. As a result of this rating, climate related issues are now an essential part of all asset allocation advice.

Climate change and ESG risks

3.2 The Investment Committee has concluded that climate related risks should be treated as a standalone risk, whilst recognising that they will impact on the scheme's ability to meet its return targets. The climate related risks are rated as red risks. The Investment Committee is considering developing a more granular risk assessment when more data is available, recognising that the assessment needs to be proportionate.

3.3 The Investment Committee oversees climate-change and ESG risks as part of its usual risk management process at every meeting. The risk register is reviewed at quarterly meetings and more regularly if required. It includes a risk relating to the potential for physical and transition risks relating to climate change to have a detrimental effect on investment markets and member pot sizes. Failure to meet the Paris Agreement has a particularly negative effect. The risk register notes the ongoing review of the portfolio against climate risk metrics to understand the portfolio risk and enable mitigation where possible. Resilience to climate risk scenarios is considered as part of the investment strategy portfolio construction (which is reviewed at least triennially).

3.4 The Trustee reviews key risks quarterly. Advisers review risks at least annually but in practice the investment consultants attend all Investment Committee meetings and so are part of the risk assessment discussion. The Investment Committee is mindful of the risks of greenwashing and of the need to ensure that the quality of the data and conclusions reported about funds and the underlying companies is sufficient accurate and granular to provide objective information. The Investment Committee will keep this under close review.

3.5 Reports from the investment adviser include ESG ratings where appropriate. Climate change remains a substantive standing item to enable the Investment Committee to develop its strategy and identify and assess any new opportunities or risks. Improving the data to enable the Investment Committee to assess progress towards a Paris aligned portfolio is the current priority.

3.6 The use of an investment platform makes engagement with the underlying managers challenging. The Investment Committee is considering its options but is likely to engage specifically with the investment platform provider as the most effective and proportionate approach to stewardship.

Metrics

3.7 The Investment Committee have considered the best way to understand how exposed the Scheme is to climate and carbon risk to inform a strategy to mitigate the risks as best as possible and identify any opportunities. The Investment Committee agreed the following metrics as part of their ongoing governance and reporting as being objective and measurable in the context of the assets held.[8]

	Description	**Measurement**
Total Carbon Emissions of the portfolio (Absolute)	Total emissions associated with a portfolio	Tons CO_2e carbon footprint x investment size
Carbon footprint (Intensity)	Total emissions normalized by the size of the portfolio	Tons CO_2e/£m invested

[8] The metrics are consistent with those recommended by the DWP.

	Description	Measurement
Temperature Alignment score of the portfolio	A measure of the global warming temperature outcome implied by companies' activities and targets	Currently very onerous to obtain sufficient information to measure this but the Investment Committee aspires to be able to use this as being more forward looking than the carbon emission metrics.
Improving data	Data reporting scope 1, 2 and 3 emissions[9]. Number of underlying companies with a science-based target.[10]	Percentage

3.8 The Investment Committee considered the available data collated by the investment platform provider, Mobuis Life, presented by Schroders Solutions. Despite undertaking a preliminary review of data earlier in 2021, the data available at the year-end was still disappointingly limited. There are significant gaps in the data required from the underlying managers and investment platform provider, particularly in relation to scope 3 emissions. We have not been able to obtain full information on data coverage or quality. This will be a focus of engagement with our platform provider and the underlying managers over the next year.

3.9 The following metrics report on 86.5% of the Scheme's total assets. No data was reported for sovereign bond funds.

	Scope 1 and 2		Scope 3	
	Metric	Data Coverage[1]	Metric	Data Coverage[1]
Total Carbon Emissions[2]	17,602	82%	38,584	5%
Carbon Footprint (tonnes C02e/£m invested)	126.5	82%	277.3	5%

1. *Where managers have been unable to provide a data coverage metric it has been assumed the coverage is similar to equivalent funds or prior knowledge of the asset class has been used to make a reasonable assumption. Data coverage is reported as a proportion of included assets.*
2. *Where managers were not able to report total carbon emissions, these have been calculated from the Carbon Footprint numbers provided.*

Targets

3.10 The Investment Committee have set an overarching target of achieving Net Zero by 2050, provided it does not conflict with their fiduciary duties to members. The Investment Committee decided not to set absolute emissions reduction targets as these measures are backwards looking but to focus on the forward looking metric of Implied Temperature Rise (ITR) of the portfolio.

3.11 The Investment Committee has not yet been able to obtain consistent data on ITR to allow it to set the baseline for this metric but when this is set, it aims to see the ITR reducing linearly each year. This will allow them to set interim targets related to ITR. In the meantime, the shorter term target is to improve the data coverage and quality, both to include more of the Scope 3 emissions than is currently available, and also ensuring consistency of the ITR metric. The Trustee would like to use Science Based Targets for the ITR metric where possible but will engage with their underlying managers to utilise a consistent metric that is most widely available.

3.12 The Investment Committee set the base date for the emissions based metrics at 31/12/2021. This also aligns with the Scheme's year end. The Investment Committee believed it would not be appropriate to

[9] Scope 1 emissions are direct greenhouse emissions that occur from sources that are controlled or owned by an organisation.
Scope 2 emissions are indirect emissions from the generation of purchased energy
Scope 3 emissions are all indirect emissions (not included in scope 2) that occur in the value chain of the reporting company.
[10] Science-based targets provide companies with a clearly defined path to reduce emissions in line with the Paris Agreement.

measure performance against targets at an earlier date because the impact of the pandemic on global carbon emissions would represent an unrealistic starting point.

3.13 The data provided in relation to Carbon footprint enables the Investment Committee to establish the current position and monitor the position going forward in respect of scope 1 and 2 emissions. Data is not currently available for scope 3 emissions and the Investment Committee understands the Carbon footprint may increase once scope 3 emissions are included.

Performance

3.14The level of data available has not allowed a base line measurement of the scheme's exposure to climate related risks to be established for the Trustee's preferred metric. It has not therefore been possible to report on the performance. The Investment Committee is focusing on improving the data available to improve reporting and measurement going forward and embedding the agreed targets into the governance and risk management processes. This will be the focus of engagement with the service providers over the next year.

MONEY PURCHASE SECTION

THE CHEVIOT PENSION

THE IMPLICATIONS OF CLIMATE CHANGE

Climate change[1] is rarely out of the news. It refers to changes to the climate which result either directly or indirectly from human activity. The recent record breaking temperatures in 2022 are an example of the current impact of climate change caused by carbon emissions

WHAT IS THE PARIS AGREEMENT?

The Paris Agreement was a landmark international treaty on climate change adopted by 196 Parties in Paris, on 12 December 2015 and entered into force on 4 November 2016. Its goal is to limit global warming to well below 2, preferably to 1.5 degrees Celsius, compared to preindustrial levels. To achieve this, counties aim to reduce greenhouse gas emissions as soon as possible to achieve a climate neutral world by 2050.

IMPACT ON RETIREMENT INCOME

The Investment Committee has focused on climate related risks and opportunities over the last 18 months. After considering various different projections of the future impact of climate change, it believes that it will be a financially material factor now and increasingly so in the future.

If countries do not meet the objectives of the Paris Agreement, the impact on your pension savings is likely to be significant in the mid to longer term. This is because the physical risks of climate change such as floods, coastal erosion, rising sea levels, etc are very likely to impact on the wider financial structure and future investment returns.

If countries meet the Paris Agreement objectives but only at the end of the period to 2050, this is also likely to lead to severe and sudden impact on markets. Equities, or company shares, are the assets likely to be most affected by climate change but generally are expected to provide higher returns over the long term. More resilient assets, such as government bonds and cash produce lower returns.

CHEVIOT'S RESPONSE

The impact of climate change is now an essential part of the decision making process about which assets to hold. The Trustee continues to aim to strike a balance between the level of risk and return of the underlying investments and includes climate change issues in that assessment.

The Trustee intends over time to move to funds which take more account of climate change and are aligned to the Paris Agreement.

The investment Committee has also considered the best way to understand how exposed the Money Purchase Section is to climate and carbon risk. It has decided to focus on a forward looking measure of the Implied Temperature Rise of the investments. It does not yet have sufficient data to set a baseline for this measure but will set a target when the data is available. In the meantime, its target is to improve the data coverage and quality.

NET ZERO COMMITMENT

As a result of the analysis completed during the last 12 months, the Board has approved a commitment to target net zero emissions by 2050, reflecting the Paris Agreement's objectives, as it believes this is in members' financial interests. The commitment is based on the Trustee's duty to act in the best financial interests of the members and reflects the need for governments and policymakers to deliver on their commitments to achieve the temperature goes of the Paris Agreement. The net zero commitment can be found here.

DATA CHALLENGES

To measure the scheme's progress towards a net zero commitment, the Investment Committee has agreed to measure the absolute emissions, carbon footprint and temperature alignment (a measure of the global warming temperature outcome implied by companies' activities and targets) of the scheme's investments.

The data available at the scheme's year end was limited and the Investment Committee is engaging with the platform provider to improve the data received in the future.

CLIMATE CHANGE REPORT

The Trustee's full report on its work on the impact of climate change is available here.

1 This factsheet is a summary of Cheviot's first Task Force on Climate-related Financial Disclosures (TCFD) report. The TCFD consists of 32 members from across the G20 and aims to improve the reporting of climate related risks and opportunities. By identifying climate related risks and opportunities, the Trustee can include them in their investment strategy.