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RLAM's approach to climate change

Climate change is not a new concept, but is one that is moving higher up investors' agendas. We are increasingly engaging with companies on climate change and the potential impact on their business. We also joined with 414 investors with a total of US$31 trillion in assets to sign a joint investor letter to governments on climate change ahead of the COP 24 summit in Poland. This is the most supported investor statement on climate change to date, and sent a powerful message to governments and regulators about investor concern over climate risk.

Given increased demand from our clients for information on our approach to climate change, this note provides an overview of Royal London Asset Management's (RLAM) approach to climate change within our investment decision-making processes.

Climate change in RLAM's investment process

- Across RLAM's investment portfolios, we integrate analysis of potential climate change risks into our investment decision-making where we feel that climate change might have a material impact on the company. This would encompass areas such as oil and gas, utilities, shipping and mining, as well as other less obvious sectors. And across a number of our funds, we already carry out regular reviews of the material environmental, social and governance factors impacting these portfolios.
- In addition, our range of Sustainable funds invest in companies seeking to invest in companies which will offer long-term net benefits to society, including greater provision of renewable energy and more sustainable infrastructure.

How we engage with companies on climate change

- We are committed to being a responsible investor and to being a good steward of our clients' assets. When choosing whether and how to engage, we will prioritise engagement work by cross-referencing the companies in which we have substantial exposure with those whose corporate governance, environmental or social practices pose a potential future risk and conduct pre-emptive engagement to address our concerns.
- As part of our regular engagement with a range of companies across both our equity and fixed income holdings, we will discuss climate related risks and opportunities where they have a material impact on a company's business model.
- For example, at the end of 2018 and throughout 2019 we have been engaging with our UK utility holdings on their efforts to decarbonise their portfolios. We are also exploring other investments we hold which might indirectly finance these sectors – most notably using meetings with certain financial and banking institutions to ask questions around how they are limiting their lending exposure to sectors materially exposed to climate change.

Our view on divestment from fossil fuel exposed companies

- As investors, we don't believe that having a set of 'one size fits all' red lines is the most appropriate strategy when it comes to climate change risks. In general, we would prefer to use our position as shareholders or bondholders to encourage change at the companies where we invest.
- We would prefer to explore other opportunities for engagement, with divestment available as a final resort. In addition, we don't feel that automatic divestment would capture the journey which many companies are on, particularly in sectors with higher

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carbon emissions that contribute more to climate change. For instance, within the energy sector, there are companies that are decreasing carbon-based energy and investing in renewables. A 'filter based' screening would probably rule out the company, but depending on the individual fund, the direction of travel may be more important.

- For members and clients seeking lower fossil fuel exposure, we also offer an award-winning range of sustainable funds which aim to invest in companies actively contributing to long-term trends affecting society, including investments in renewable energy providers.

Our work with other investors on climate change

- In 2018 we joined with 414 investors with a total of US$31 trillion in assets to sign a joint investor letter to governments on climate change ahead of the COP 24 summit in Poland.
- In addition, we provided feedback to the Investment Association (IA) and Association of British Insurers (ABI) on consultations issued by the Financial Conduct Authority (FCA) and the Prudential Regulatory Authority (PRA) on climate risk in the financial sector.
- As shareholders, we have also worked on joint proposals for company annual general meetings, including co-filing the CA100 climate change resolution at BP's annual general meeting in 2019, pushing for the company to provide a detailed strategy on how it will comply with the Paris agreement.

Specific climate scenario analysis

- We are broadly supportive of the PRA and FCA's guidance to the asset management sector to help us better assess our climate risks. However, we note that the limited availability and poor quality of data could limit our ability to undertake meaningful scenario analysis. This is particularly the case where we hold significant fixed income investments where data tends to be more limited. In day-to-day investment decision-making, where climate risk has the potential to have a material impact on the financial returns of an asset, these risks will be factored into an investment decision-making process.

Investment examples

- For example in our sustainable funds, we've recently added to our exposure to a utility company that would already be considered a leader in the UK market. While it retains some fossil fuel generation capacity, the company is due to invest significant capital which will drastically increase its already considerable exposure in the renewables space over the longer term while it phases out its more carbon intensive generation capacity over the next few years.
- When recently assessing our exposure to a UK-listed cruise line company in the UK equity portion of a number of our portfolios, and having reviewed how the business was responding to IMO 2020 legislation on shipping emissions, we chose to reduce our position as we felt the company's strategy in this regard was contributing to it becoming a higher-risk investment proposition.
- We have increased our exposure to a long-standing private property company, which has been successful in improving the energy efficiency of an estate which includes a large proportion of older, listed buildings. These improvements have increased our conviction over the asset life of the collateral securing our bond investment.
- When looking at new social housing bonds, prior to investment, we are now asking them to provide additional detail on the energy efficiency and environmental footprints of their housing stock as a matter of course.

It is true to say that approaches to climate change are evolving rapidly. Even a few years ago, companies had either not really considered the potential impact or were not engaging with investors on plans to mitigate its effects. We will continue to update clients, through longer reports such as our Stewardship report, as well as occasional articles in the 'Our Views' section of www.rlam.co.uk

Contact us

For more information about our range of products and services, please contact us.

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