BTPS

# Sustainable Investment Summary 2023

www.btps.co.uk

# Contents


| | |
|---|---|
| Introduction | 3 |
| BTPS at a glance | 3 |
| Our approach to sustainable investment | 4 |
| Member views | 5 |
| Managing climate risk | 6 |
| Our net zero progress in numbers | 7 |
| Key activities over the past 12 months | 8 |
| Manager Oversight | 11 |
| Engagement | 12 |
| Future priorities | 14 |


# Introduction

**As one of the largest corporate pension schemes in the UK, we have always been acutely aware that how and where we invest matters. This is a responsibility we take very seriously.**

We firmly believe investing sustainably supports long-term value, reduces risk and contributes towards better outcomes. We also know from the surveys we conduct with our members that they expect us to use our investments to make a positive impact.

In 2020, the Scheme set a 2035 net zero goal recognising that climate change is a clear and present risk to the Scheme meeting its long-term financial commitments.

July 2023 was the hottest month in human history and the effects of the continued increase in temperature around the world are far reaching, for global populations and for the investments held within the BT Pension Scheme (BTPS).

For the Scheme to achieve its net zero goal, we are working on both reducing emissions from the Scheme's portfolio and investing in assets that will support the transition towards a lower carbon economy.

However, achieving the reduction in emissions required to meet our 2035 goal is far from easy. We are reliant on significant decarbonisation of the global economy which involves decisive action from governments, companies and consumers.

We are also conscious of the challenges associated with having a fair transition. There is a need to balance progress on decarbonisation with social challenges such as the current cost of living crisis as well as issues such as greater energy security.

We continue to seek to influence the businesses in which we invest on a variety of sustainability topics, and encourage governments and regulators around the world to drive the transition through collaboration with other asset owners for greater collective influence.

This report summarises some of the key activity over the past year and there's much more detail in our **Stewardship** and **TCFD** reports.


# At a glance

**BTPS is a defined benefit pension scheme for employees, former employees and dependants of BT Group and some of its associated companies. The Scheme closed to new members in 2001 and to future accrual for most members in June 2018.**

263,447 members, of which 210,359 are retired

The average age of BTPS members is 70 years old weighted, by pension amount

Net assets c. £37.5bn

67% of assets invested in the UK

Figures as at 30 June 2023

# Our approach to sustainable investment

### Sustainable investment mission statement

"The Scheme's investments should be managed to create sustainable long-term value, supporting the generation of optimal investment returns to ensure the Scheme can pay all benefits in full".

### This mission statement is underpinned by three beliefs:

#### Long-term investment horizon

Due to the size and longevity of the Scheme, having a long-term investment horizon gives us both a responsibility and an advantage, which we believe will produce better investment outcomes.

#### ESG integration

We believe that integrating financially material sustainability considerations into asset manager and security selection processes will help the Scheme and its agents make more informed and better investment decisions.

#### Stewardship

We believe in strong stewardship because exercising our ownership rights in companies, having our agents and portfolio companies engage with each other, and actively managing physical assets can improve long-term risk-adjusted returns and create sustainable long term value. This ensures our own practices align with our expectation of the other companies and assets in which we invest.

### Understanding sustainable investment terminology

**Sustainable investment:** Aiming to generate long-term financial returns while contributing to positively to society and the planet.

**Environmental, social and governance factors (ESG):** Using ESG or sustainability information to identify companies with good practices and superior business models. Environmental factors consider how a company performs as a steward of nature e.g. climate change, energy emissions and waste management. Social factors examine how a company manages its relationships with employees, suppliers, customers and the community. Governance deals with how a company is governed, and can assess executive pay, shareholder rights and audit.

**ESG integration:** Integrating ESG factors into investment analysis to determine if an investment's risks are outweighed by potential investment returns. This can provide investors with a deeper insight into the quality of a company's management, culture, risk profile and other characteristics, before they invest and make more informed decisions.

**Stewardship:** "The responsible allocation, management and oversight of capital to create long-term value for clients and beneficiaries leading to sustainable benefits for the economy, the society." (UK Stewardship Code, 2020)

# Member views

We believe that a collective understanding of member views helps inform the Scheme's approach to ESG considerations and stewardship. Each year our annual member survey asks members a range of questions so we can understand their attitudes towards sustainable investment. Where appropriate and possible, the Trustee integrates members' feedback into their thinking. Results from our member survey in January 2023 showed around three quarters (76%) of the ~15,000 respondents expect BTPS to continue to take consideration of the environmental and social impact of the investments it makes.

Your views really do matter to us.

**49%**

**agree or strongly agree**

BTPS should prioritise financial performance over the environmental and social impact of its investments.

| 2021 | 2022 | 2023 |
|---|---|---|
| 48% | 47% | 49% |

**63%**

**agree or strongly agree**

I expect BTPS to actively avoid investments that have a materially negative impact on the environment and society.

| 2021 | 2022 | 2023 |
|---|---|---|
| 62% | 63% | 63% |

**66%**

**agree or strongly agree**

I expect BTPS to use the investments to make a positive impact on the environment and society.

| 2021 | 2022 | 2023 |
|---|---|---|
| 65% | 67% | 66% |

**73%**

**agree or strongly agree**

I expect BTPS to continue to take consideration of the environmental and social impact of the investments it makes.

| 2021 | 2022 | 2023 |
|---|---|---|
| 74% | 76% | 73% |

# Managing climate risk - net zero 2035

Climate change has the potential to have a negative impact on the value of the Scheme's investments, for example flooding could damage a property we own. A change in energy policy to reduce emissions could leave fossil fuel investments 'stranded' where they suddenly lose value as a result of external factors. The Scheme's net zero goal seeks to both recognise and address these risks, whilst noting that climate change also offers potential investment opportunities. Achieving the net zero goal means working on both reducing emissions from the Scheme's portfolio and investing in assets that will support the transition towards a lower carbon economy such as renewable energy and low-carbon technologies.

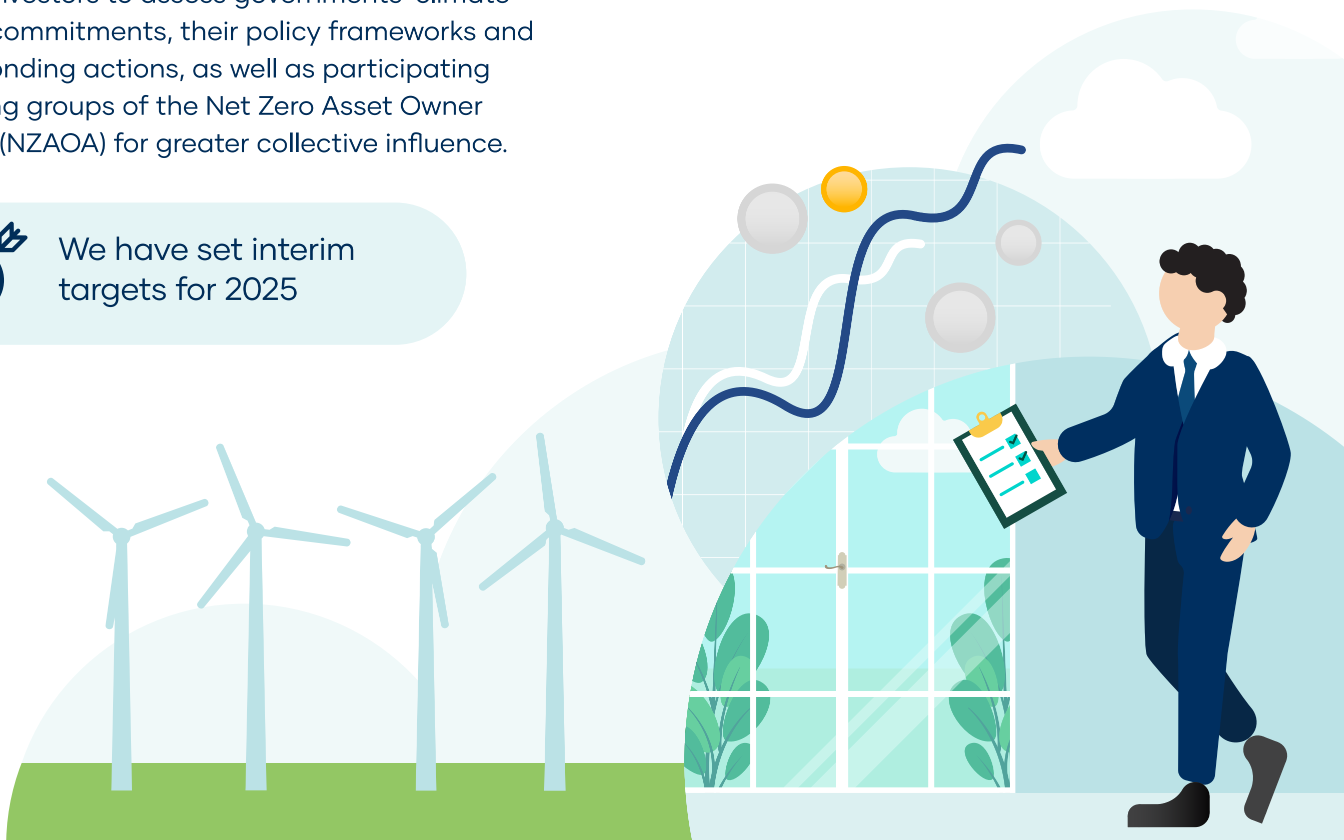
To achieve net zero the entire economy needs to decarbonise and this requires concerted action by governments, companies and consumers.

We continue to seek to influence the businesses in which we invest to drive positive change. We also encourage governments and regulators around the world to drive this transition through collaboration with other asset owners, for example co-chairing the Assessing Sovereign Climate-Related Opportunities and Risks (ASCOR) project which will enable investors to assess governments' climate-related commitments, their policy frameworks and corresponding actions, as well as participating in working groups of the Net Zero Asset Owner Alliance (NZAOA) for greater collective influence.

2035 is still some time away so, to help keep us on track, in 2022, we announced 5-year targets to reduce the scope 1 and 2 carbon intensity of the Scheme's equity and credit portfolio by at least 25%, and real estate by at least 33% by 2025, relative to our 2020 baseline. We are pleased to report that we are currently on track with our 5-year reduction targets.

We are an active and engaged investor

We have set interim targets for 2025



# Our Net Zero progress in numbers

We measure the Scheme's carbon intensity using various metrics. Two that we track in particular are:

### Absolute emissions

Absolute emissions are the primary focus of the net zero goal and reflect the overall investment portfolio emissions and the real world impact.

> **The Scheme's absolute emissions have reduced by 51% over the year.**

The significant reduction in absolute emissions is mostly a result of asset sales, predominantly from the listed equity portfolio in the second half of 2022.

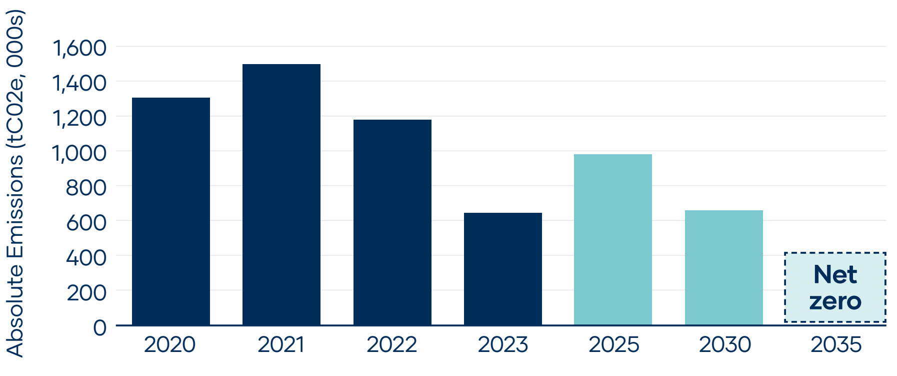
### Weighted Average Carbon Intensity (WACI)

WACI measures the exposure to carbon-intensive companies, expressed in tons of carbon dioxide equivalent per unit of revenue.

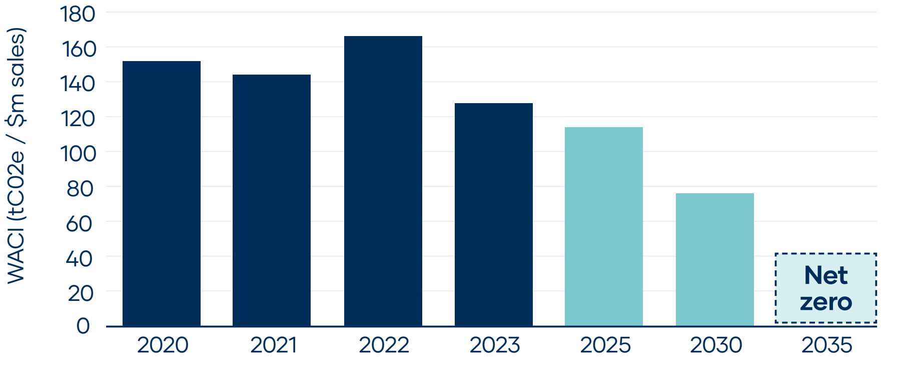
> **The Scheme's carbon intensity reduced by 16% over the year.**

The main reason for this reduction is the sale of some of the higher emissions intensity equity investments. As a result, the remaining equity exposure is, for now, heavily exposed to service companies, which understandably operate with much lower carbon footprints.

**Equity & corporate credit absolute emissions performance vs. net zero targets**




**Equity & corporate credit WACI performance vs. net zero targets**



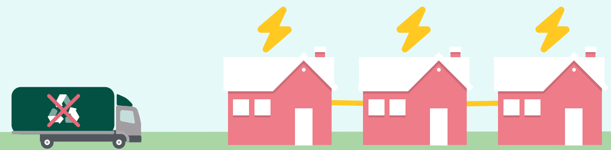
# Key activities over the past 12 months

## Member visit to Viridor

In June 2023, we invited a small group of BTPS members from the member panel to visit one of the Scheme's UK infrastructure investments, Viridor, a leading waste-to-energy and recycling business, in Avonmouth, Bristol.

Viridor's purpose is **"Building a world where nothing goes to waste"**. It is a leading resource recovery and recycling business focused on recovering energy from waste, and plastics recycling and reprocessing.

Annually, the Avonmouth site diverts **320,000 tonnes** of non-recyclable household waste from landfill and uses it to generate over **300 Gigawatt hours (GWh)** of electricity. That's enough electricity to power **84,000 homes** a year.



The plastics reprocessing facility, at the same location, is powered by the electricity created from the energy-from-waste recovery process, to repurpose **80,000 tonnes** – more than **1.6 billion bottles, tubs and trays** a year – creating recycled raw material to return to the economy.

Making new plastics products out of recycled plastics uses **126,000 tonnes less carbon** than creating new plastic. That's the equivalent of taking over **67,000 diesel cars** off the road every year.

Viridor is a good example of one of BTPS' investments which has good sustainability credentials and the appropriate risk and return profile for the Scheme. We invested in June 2020 and since then (to 31 December 2022) **we've seen a return of around 30%**.

Watch the video from the day **here**.

# Key activities over the past 12 months

## Developing of knowledge of biodiversity with Cambridge Judge Business School

Over the past year biodiversity has become a key area we have sought to develop our understanding in. We have engaged with managers to establish how we can better tackle biodiversity loss within the BTPS portfolio and the corresponding risk to the ecosystem, people and ultimately, the global economy that could harm the future value of the portfolio.

We are mindful that preserving natural ecosystems is our strongest natural defence against climate change and therefore imperative to help achieve our Net Zero 2035 goal.

To help develop our understanding, we undertook a research project with MBA students from the Cambridge Judge Business School on biodiversity to better understand its impact on the Scheme's portfolio.

An article summarising our learnings can be found on the Brightwell website **here**.

# Key activities over the past 12 months

## Supporting better insight on sovereign debt

Sovereign debt remains a challenging asset class for investors decarbonising their portfolios. The data is inconsistent and opportunities to engage with governments on climate change are limited.

We need a publicly available tool and database on sovereigns' climate action and alignment. This is the aim of the **Assessing Sovereign Climate-related Opportunities and Risks (ASCOR)** project which BTPS is involved with via Scheme manager Brightwell.

ASCOR will enable investors to assess governments' climate-related commitments, their policy frameworks (including carbon pricing, energy subsidies, the phase-out of combustion vehicles, deforestation and land use policies) and the actions they are taking to ensure that the benefits of the low carbon transition, and of adaptation, are shared fairly.

ASCOR will not be scoring countries, nor giving investment advice or direction – it is a tool to enhance investors' decision- making capabilities and to support investors working towards Net Zero goals.

The ASCOR Consultation report was launched in February 2023 requesting feedback on the framework – this included 800+ attendees at global webinars, 200+ responses to the online consultation survey, 140+ attendees at regional roundtables and 15+ bilateral meetings with countries and organisations. 25 pilot countries are being assessed and the issuer feedback process got underway in Q3 2023.

**Significant progress has been made since ASCOR's launch in June 2021.**

### What is sovereign debt?

Sovereign debt is issued by governments in order to borrow for public investment such as infrastructure and other government priorities. Governments acquire sovereign debt by issuing bonds (sometimes referred to as gilts) which investors such as pension funds can invest in. Sovereign debt is appealing to pension funds as gilts are typically lower risk and provide a steady income stream through regular income payments.

## Asset Owner Diversity Charter

BTPS is a signatory to the **Asset Owner Diversity Charter (AODC)** and is committed to holding asset managers to account on diversity and inclusion to improve the asset management industry's performance on this important issue.

Diversity, equity and inclusion (DE&I) forms part of the manager selection process and the Scheme monitors its managers' efforts on an ongoing basis to encourage positive broader industry change.

Since becoming a signatory to the Charter, managers have responded to the annual AODC questionnaire and we have analysed their responses. Whilst there is of course room for improvement, we are encouraged by the constructive conversations we have had with managers on this important topic. In particular, their willingness to engage and their efforts to drive real change across the industry whether, for example, through joining initiatives such as the Diversity Project, or setting targets to improve senior female and ethnic diversity representation.

# Manager oversight

**We believe that all financially material considerations, including sustainability factors, must be integrated throughout the investment process. BTPS predominantly outsources investment management to externally appointed asset managers.**

Asset managers are selected to align with our beliefs, policies and objectives. This is a fundamental part of the appointment process of a new manager and the ongoing oversight of our managers' activities.

Before appointing an asset manager, Brightwell seeks to understand their philosophy and approach, to determine if they are suitable for the Scheme. This includes an assessment of the alignment between our beliefs and goals, the investment time horizon, approach to sustainable investment, and engagement with underlying companies. Assessment of our asset managers' stewardship capabilities forms part of a wider focus on their approach to integrating sustainability considerations. Over the past few years, Brightwell has developed and improved its approach in this area with the introduction of our Manger Net Zero & Stewardship scorecard. We share tailored scorecards with the Scheme's managers which outline areas of improvement we would like to see against our Sustainability Best Practice Expectations document. This aids transparency and is a helpful way to engaging with managers on key sustainability areas.

# Engagement

Meaningful engagement with companies' management teams and boards helps hold management to account and drive positive change. Corporate engagement is done on BTPS' behalf in two ways: through our asset managers but predominantly through EOS at Federated Hermes on behalf of the Scheme. Corporate engagement is the practice of shareholders entering into discussions with company management to change or influence the way in which that company is run. Engagement can be successful across many different asset classes, including equities, bonds, property, private equity and infrastructure.

## Corporate credit engagement via Wellington Management

**Monitoring progress against science-based targets with a fossil fuel company**

**Issue:** Wellington engaged with one of the largest producers of fossil fuels which has a higher-than-average weighted average carbon intensity. It was necessary to engage and discuss the company's strategic outlook, their emissions reductions targets, provide feedback on their client perspective, and speak to their Net Zero Asset Manager's involvement.

**Action:** The engagements focused on how the company planned to meet its science-based target of a reduction in carbon emissions by 70% from a 2017 base. Wellington noted that the company was differentiated by its willingness to share data and specific plans for closing coal plants and reducing emissions over time. Nevertheless, Wellington remained aware of the details regarding plan closures and plans for transitioning to a green future.

**Outcome:** Engagement has continued over the year, and the company was able to provide further detail about the coal plant closures over the next five years, along with details on how it is working with its suppliers to manage their Scope 3 carbon emissions. Wellington believes the company is a leader in the industry in terms of thinking about the Scope 3 transition, which will accelerate in the coming year.

# **Engagement** continued

## Corporate credit engagement via M&G

**Improving bioethics within a US medical technology business**

**Issue:** M&G engaged with a US medical technology and analytical equipment business to ensure it had effective policies and procedures in place to help avoid the misuse of its equipment. In recent times, there were reports regarding human rights violations with speculation that the company's DNA products were being potentially used in a manner inconsistent with human rights principles.

**Action:** M&G engaged with the company at the time and continues to do so to encourage better governance around bioethics issues. The company has adopted and implemented a Code of Business Conduct and Ethics. It has also implemented a multi-level purchasing process designed to prevent the ordering and resale of human identification products to help ensure that no products or services are sold that could potentially be used in unintended ways to violate human rights. The company has an approved network of authorised distributors that agree to comply with this purchasing process under the terms of their contract.

**Outcome:** M&G is satisfied with the progress and improvements that have been made to the company's policies and procedures over the past few years. It now has in place a cross-functional Bioethics Committee that regularly assesses the ethical and social implications of scientific developments in biotechnology. M&G will further engage with the company on matters of bioethics.

## Corporate credit engagement via Insight

**Encouraging a more diverse Board at a Mexican telecommunications company**

**Issue:** Insight engaged with a Mexican telecommunications company to discuss the controlling ownership of the firm due to the multiple-equity class structure where the company's major shareholder, and family, hold over 80% of the voting rights. Insight had concerns over this as well as the Board's limited diversity, independence, and skills.

**Action:** Insight encouraged progress on diversity to bring the board's female representation to 30%. In addition, Insight recommended establishing additional quantitative targets for the overall workforce or at the leadership level, like global industry leaders have done.

**Outcome:** Following these discussions, Insight was pleased that the company had established a new target to increase board diversity to three female directors, representing 21% of the board, which it achieved by appointing a female as a new director. This board-level diversity target is integrated into the company's strategy as it was added as a target within the company's Sustainability Linked Loan structure. The company also refreshed their Board Diversity Policy, which includes the ambition to "set measurable objectives to achieve gender diversity with the ultimate goal of having a composition of the Board where each gender represents at least thirty percent (30%)".

# Future priorities

**We continue to develop our thinking on sustainable investment which is a rapidly evolving and fast-moving area.**

Over the next five years, the Scheme will continue to explore the sustainable investment risks and opportunities posed and our exposures to them. This will include how to address new systemic risks identified by the Trustee. Via Brightwell, we will engage with our asset managers and work with them to enhance our understanding and to improve outcomes.

### Work closely with our managers

We will continue to work with our managers to encourage best practice stewardship in line with our manager expectations document, monitoring their progress over the year through our regular meetings and information provided by them. We believe transparency on both sides is crucial for achieving our ambitions.

### Strengthen ESG integration

It is important that the Scheme continues to strengthen ESG integration into its investment processes and further embed being a good steward of capital into its corporate objectives. A significant part of this is exploring how to further integrate ESG data into their investment and risk systems. This will help enhance portfolio analysis, providing a wide range of sustainability metrics we can monitor across portfolios.

### Active members of industry initiatives and collaborations

We will also continue to be active members of various industry initiatives and collaborations. These are particularly helpful in sharing best practice on various sustainable investment related topics, from biodiversity to advancing our thinking on achieving our Net Zero 2035 goal, policy advocacy work such as the ASCOR Project and DE&I through the Asset Owner Diversity Charter.

### Member engagement

To ensure we make it as easy as possible for members to understand their BTPS pension, and having taken on board member feedback from our recent surveys, we will be creating more videos on a variety of investment and sustainability related topics. These will sit on the BTPS website here. We will continue to host visits for members to a variety of the Scheme's sustainable investments. **Look out for emails to get involved!**

BTPS

www.btps.co.uk