Case study: Supporting the climate transition

FTSE Russell

# FTSE TPI Climate Transition Index

## Capturing companies' readiness for the low-carbon economy

## About the customer

### Profile

The Church of England Pensions Board manages over £2.8B in assets and serves over 40,000 beneficiaries.*

The Pensions Board is an active owner and is committed to ethical and responsible investment.

The Church of England Pensions Board is a co-founder of and continues to co-Chair the Transition Pathway Initiative (TPI), which helps assess companies' preparedness for the low-carbon economy.

The TPI is supported globally by 71 investors with over $19T** in assets under management as of January 2020.

*Church of England website, February 2020

** Transition Pathway Initiative website, January 2020

### Objectives

- Respond to the financial risk of climate change to protect the interests of future retirees.
- Integrate the insights of the TPI into the Pensions Board's passive equity portfolio.
- Reward and incentivize companies whose public targets are aligned with the 2015 Paris Climate Change Agreement.
- Significantly underweight or remove those companies whose public targets are not aligned with 2DC/Below 2DC outcomes, and those with insufficient climate related disclosure.
- Support the Pensions Board's climate engagement goals for net zero through initiatives such as Climate Action 100+.

### Index criteria

- FTSE Russell has launched the FTSE TPI Climate Transition Index Series.
- The index captures companies' exposure to five climate change parameters (fossil fuel reserves, carbon emissions, green revenues, management quality, carbon performance).
- Under the new index, the Church of England's Pensions Board portfolio will have a c.50% lower carbon intensity than its current passive allocation.
- The FTSE TPI Climate Transition Index will form the basis of a £600M passive (index-tracking) portfolio run on behalf of the Church of England Pensions Board.

## The need

In 2018, the Church of England Pensions Board made a commitment to the Church's General Synod that it would disinvest by 2023 from those companies that have not set themselves on a path to alignment with the landmark Paris Climate Agreement ("COP21"), reached in December 2015.

Under COP21, signatories agreed to limit global warming to a maximum of 2°C during the current century and to reach carbon neutrality (net zero emissions of greenhouse gases) by the end of the century.

Recently, the Church of England Pensions Board has also signed up to the United Nations' supported Net-Zero Asset Owner Alliance whose members are committed to align their portfolios to become net zero by 2050. The Board is also a leading member of the global engagement initiative Climate Action 100+ where the Board co-leads the negotiations with Royal Dutch Shell.

The Pensions Board has stated that it has made these commitments to ensure that its beneficiaries' funds are managed in a way that delivers the necessary returns and mitigates the financial risk posed by the transition. The Board is committed to supporting the transition and recognises that companies are able to put in place strategies to do so with publicly verifiable targets.

A key tool in supporting the Board's understanding of climate transition risk has been the Transition Pathway Initiative (TPI) which it Co-Chair's with the Environment Agency Pension Fund. To help meet its stated goals, during the last 18 months the Church of England Pensions Board worked closely in an innovative partnership with FTSE Russell and TPI to integrate TPI's insights into its passive investments.

As a sign of its commitment to supporting the climate transition, in January 2020 the Pensions Board announced it was making a £600 million allocation (January 2020) to a portfolio tracking the new FTSE TPI Climate Transition Index. This represents all of the fund's developed market passive equity assets.

*"Our beneficiaries need to retire into a world that isn't impacted by the extremes of climate change. We need to manage their funds in a way that ensures we continue to deliver a return whilst mitigating climate risk and supporting the transition to a low-carbon economy. This will ultimately shape the world that our future beneficiaries retire into."*

*Adam Matthews, Director (Ethics and Engagement), Investment Team, The Church of England Pensions Board*

### The Transition Pathway Initiative

The Transition Pathway Initiative (TPI) is a global initiative led by asset owners.

It assesses how individual companies are positioning themselves for the transition to a low-carbon economy.

The TPI is backed by 71 funds with over $19T of combined assets under management or advice as of March 2020.

The TPI was co-founded and is co-chaired by the Church of England Pensions Board and the Environment Agency Pension Fund, in partnership with the Grantham Research Institute at the London School of Economics and supported by the UN backed Principles for Responsible Investment (PRI).

FTSE Russell is the TPI's data partner.

# The index solution

FTSE Russell has launched the FTSE TPI Climate Transition Index, which will form the basis of a £600M passive (index-tracking) portfolio run on behalf of the Church of England Pensions Board.

The index is a collaborative effort: it has been developed jointly by FTSE Russell, the Church of England Pensions Board and the TPI. The index has 4 objectives:

1. To form the basis of a DM equity passive allocation (i.e. deliver global equity beta)
2. To explicitly incorporate the TPI's company assessments
3. To deliver significantly improved "climate characteristics" vs. the market cap benchmark
4. To provide a tool for investors to reinforce climate engagement objectives, through initiatives such as Climate Action 100+, seeking commitments from companies to align to the "Paris goals"

It incorporates analysis by both FTSE Russell and TPI on companies' exposure to five climate change parameters: green revenues, fossil fuel reserves, carbon emissions, management quality and carbon performance assessments (see the chart below).

| | |
|---|---|
| **Fossil fuel reserves** | • Underweight companies with fossil fuel reserves |
| **Carbon emissions** | • Over or underweight companies according to their GHG emissions<br>• Sector neutrality |
| **Green revenues** | • Overweight companies engaged in the transition to a green economy |
| **Management quality** | • Over or underweight companies according to their management quality ("climate governance") score<br>• Regional industry neutrality |
| **Carbon performance** | • Over or underweight companies according to their carbon performance ("2DC pathway") assessment |

## For more information about our indexes, please visit ftserussell.com.

## About FTSE Russell

FTSE Russell is a leading global index provider creating and managing a wide range of indexes, data and analytic solutions to meet client needs across asset classes, style and strategies. Covering 98% of the investable market, FTSE Russell indexes offer a true picture of global markets, combined with the specialist knowledge gained from developing local benchmarks around the world.

FTSE Russell index expertise and products are used extensively by institutional and retail investors globally. For over 30 years, leading asset owners, asset managers, ETF providers and investment banks have chosen FTSE Russell indexes to benchmark their investment performance and create investment funds, ETFs, structured products and index-based derivatives. FTSE Russell indexes also provide clients with tools for asset allocation, investment strategy analysis and risk management.

A core set of universal principles guides FTSE Russell index design and management: a transparent rules-based methodology is informed by independent committees of leading market participants. FTSE Russell is focused on index innovation and customer partnership applying the highest industry standards and embracing the IOSCO Principles. FTSE Russell is wholly owned by London Stock Exchange Group.

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