RI: Developing net-zero commitments and tools

Meeting Notes

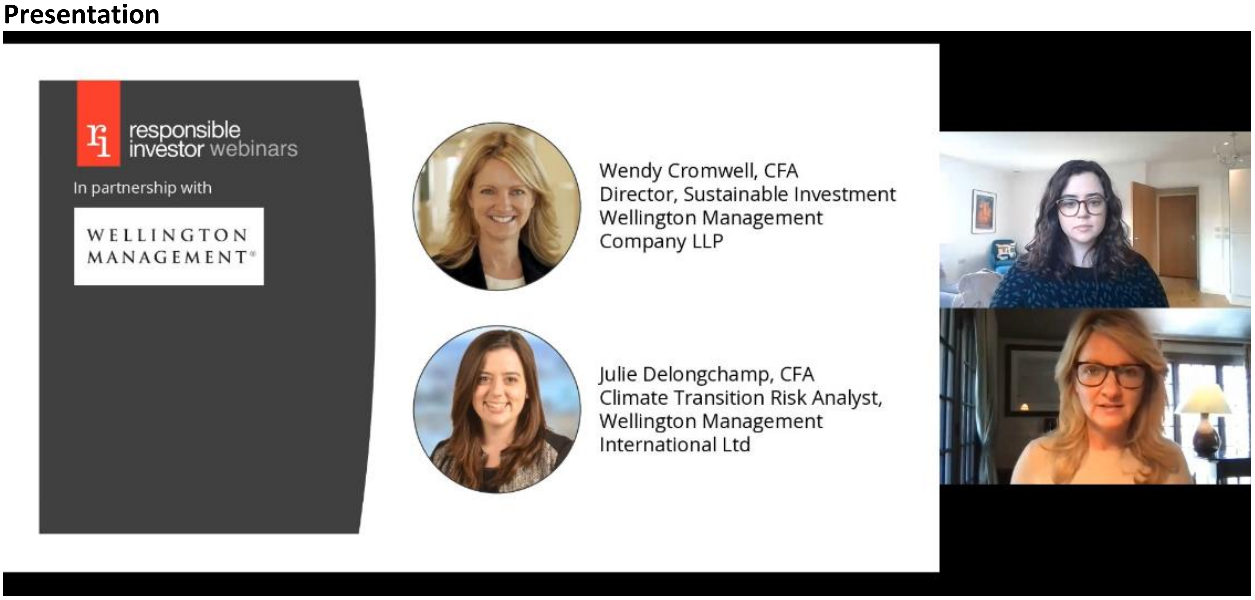
2021.03.09

Speakers

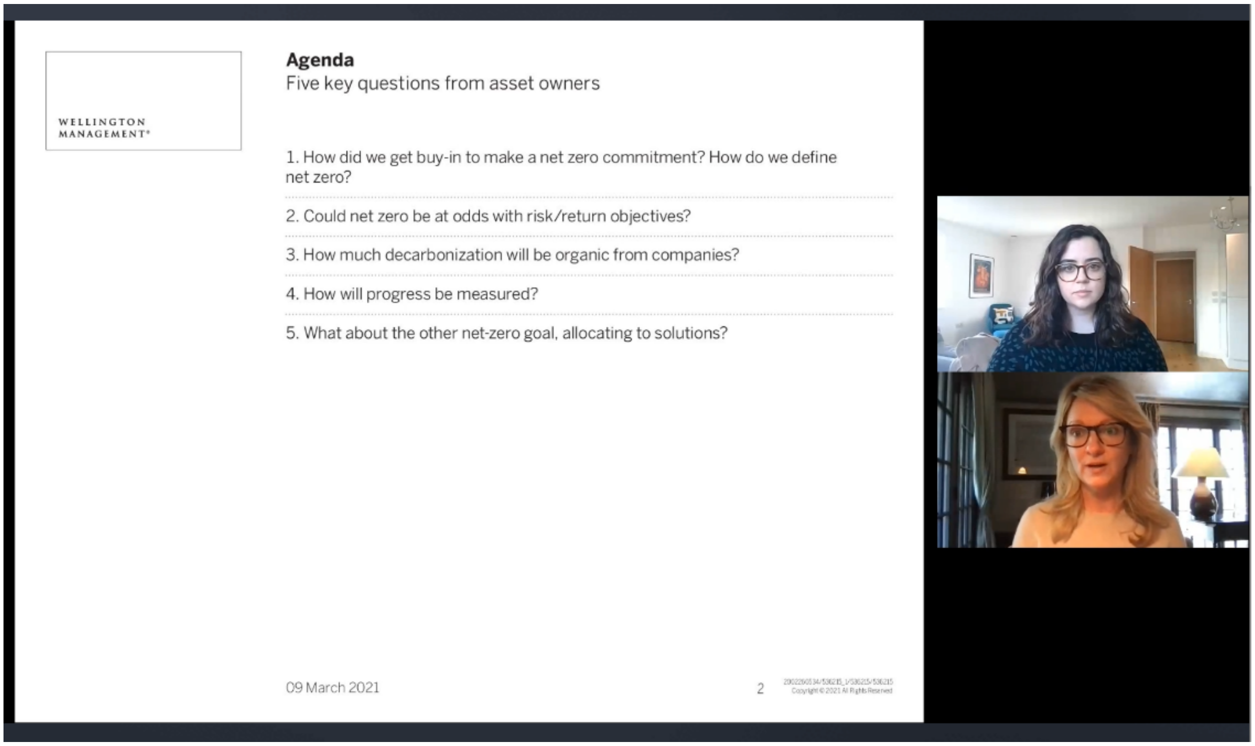
WC – Wendy Cromwell, CFA – Director, Sustainable Investment @ Wellington

JD – Julia Delongchamp, CFA – Climate Transition Risk Analyst @ Wellington

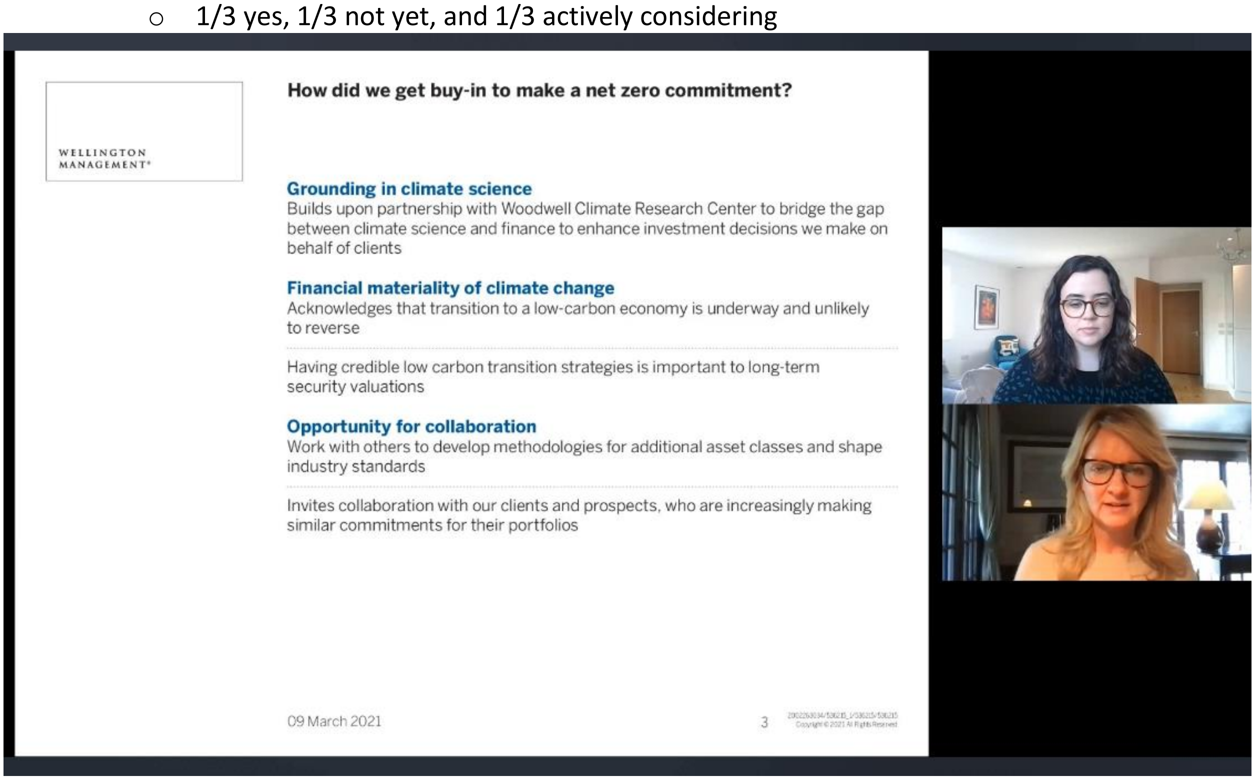
Presentation



- Wellington is proud to be a member of the Net Zero Investment Manager
- Global, 1.3 T in 60 countire across global equities, fixed income, commodities, alternatives, and privates
- One of the hallmarks is deep dive intesnenive research, which over the past several years we've focused on climate giving us a better intrinsic understanding of the need for a low carbon future

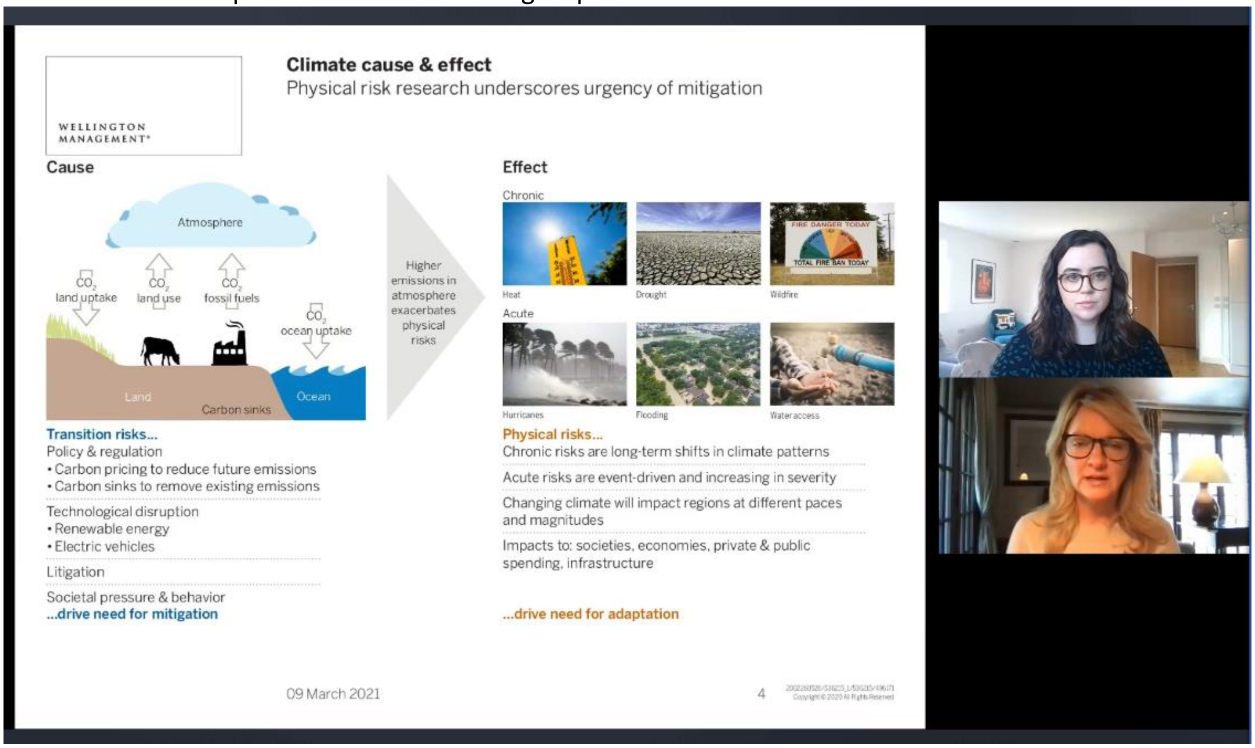


- We'll be running through some of the questions we've been hearing from asset owners
- Poll results for "Has your organization
    - 1/3 yes, 1/3 not yet, and 1/3 actively considering

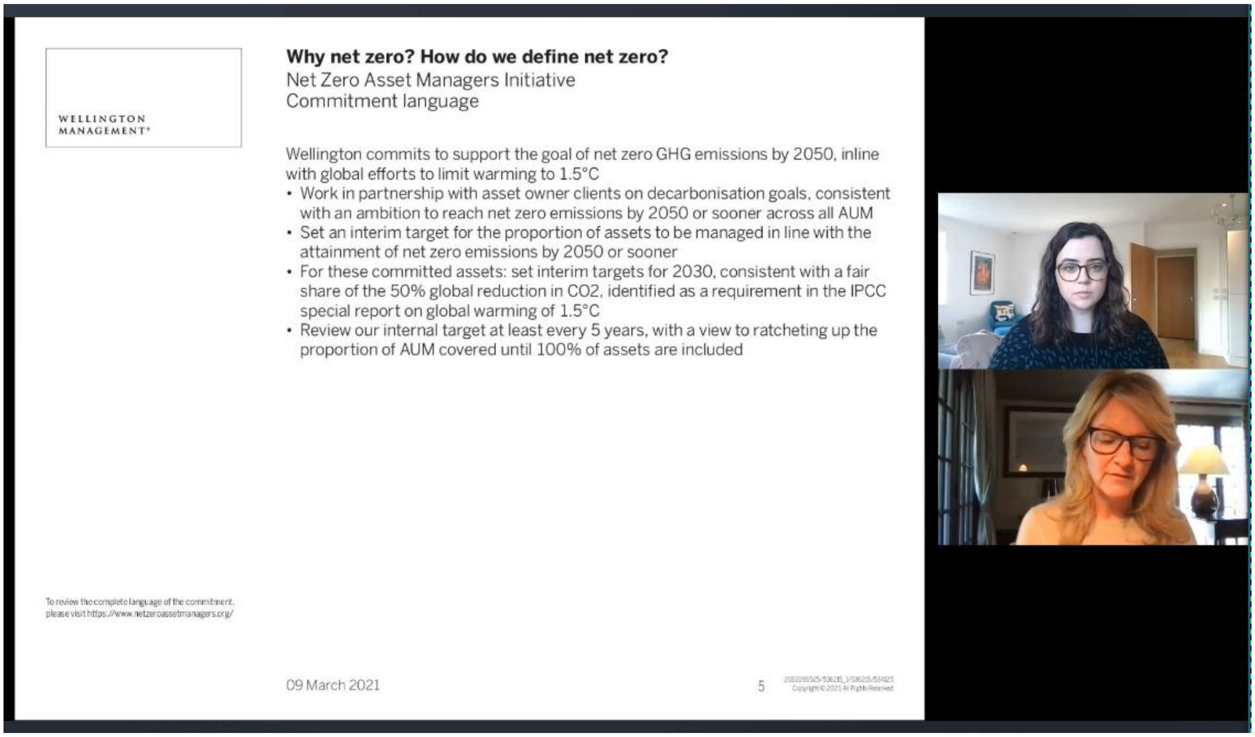


- Collaborating with others
    - There are certain asset classs where there isn't a methodology for transition, rather than receive others research we wanted to get involved in it

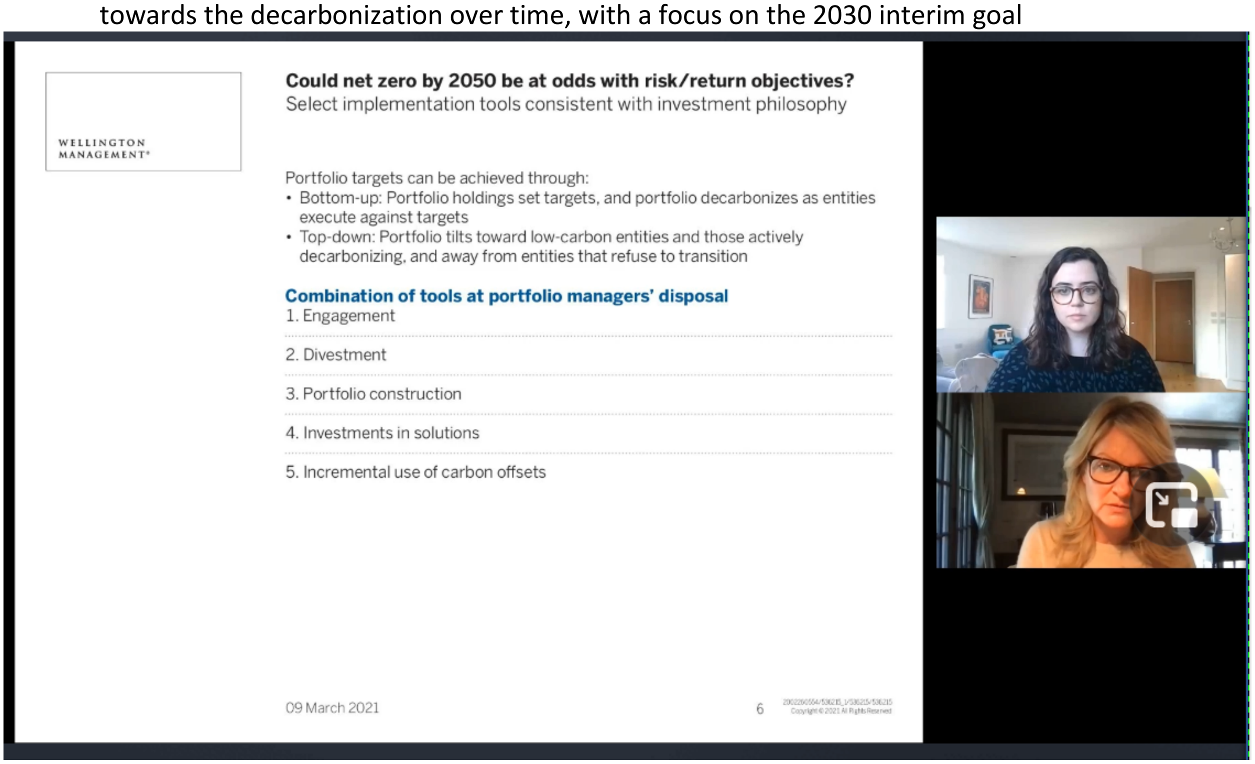
- The partnership and commitment recognizes that most asset managers have a mix of AUM, some of which they have control over and some of which the client controls
- The commitment mandates working with the clients on decarbonization goals, and to help them execute so both groups can transition these trillions over time



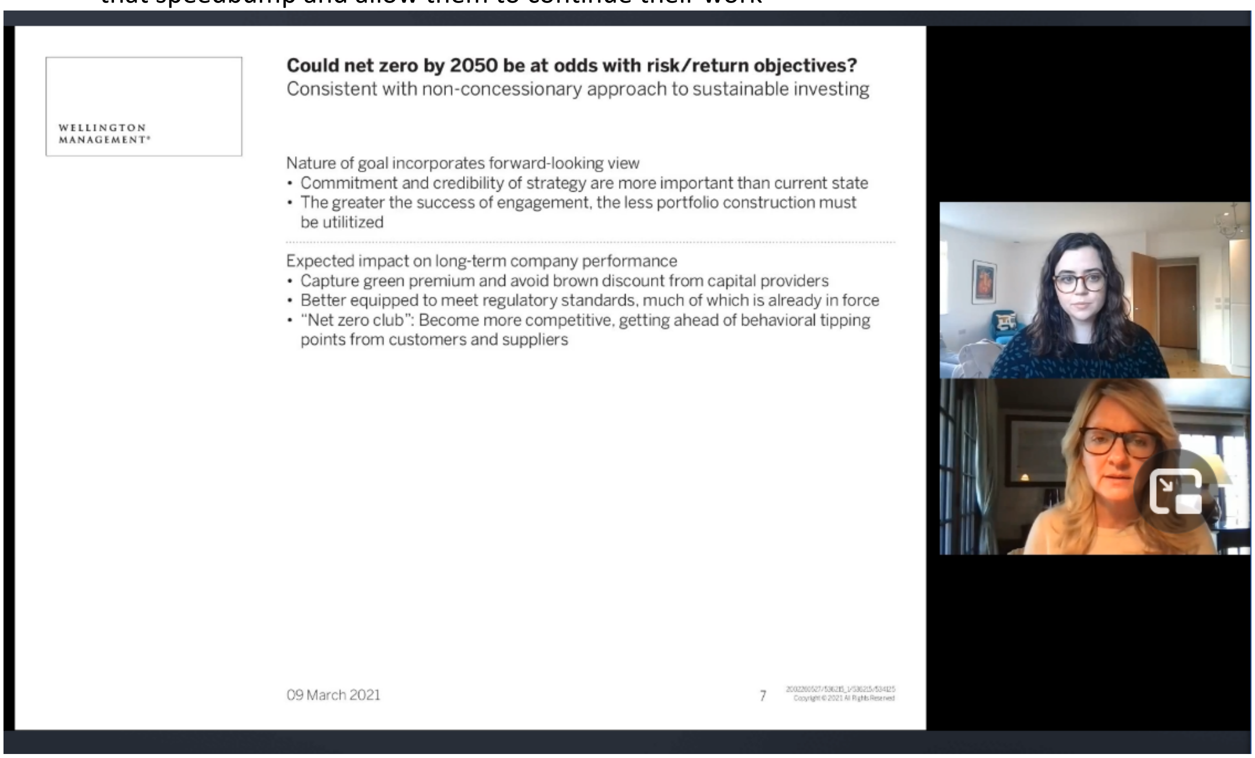
- Here I wanted to remind everybody of thet wo major fields of risks – on the left you'll see transition risks and on the right you'll see physical risks
  - Transition risk really does drive the need for physical risk
  - On the right side we're seeing the effects of those emissions
  - I'm bringing these up in the context of a research collaboration we started with Woodwell Climate Research Center (the #1 climate thinktank) who we partnered with to bridge the gap between climate science and finance
  - Over the past 2+ years we've been engaging in a rigorous process which lays out a way for investors to consider these risks and make these commitments
  - As we understood where and when physical risks were going to happen and effect society, we became more intrinsically aware of the need to decarbonize society
  - We also concluded that the low carbon transition was on its way, and was only going to continue
  - And that companies that are going to thrive in this transition needed to plan for it



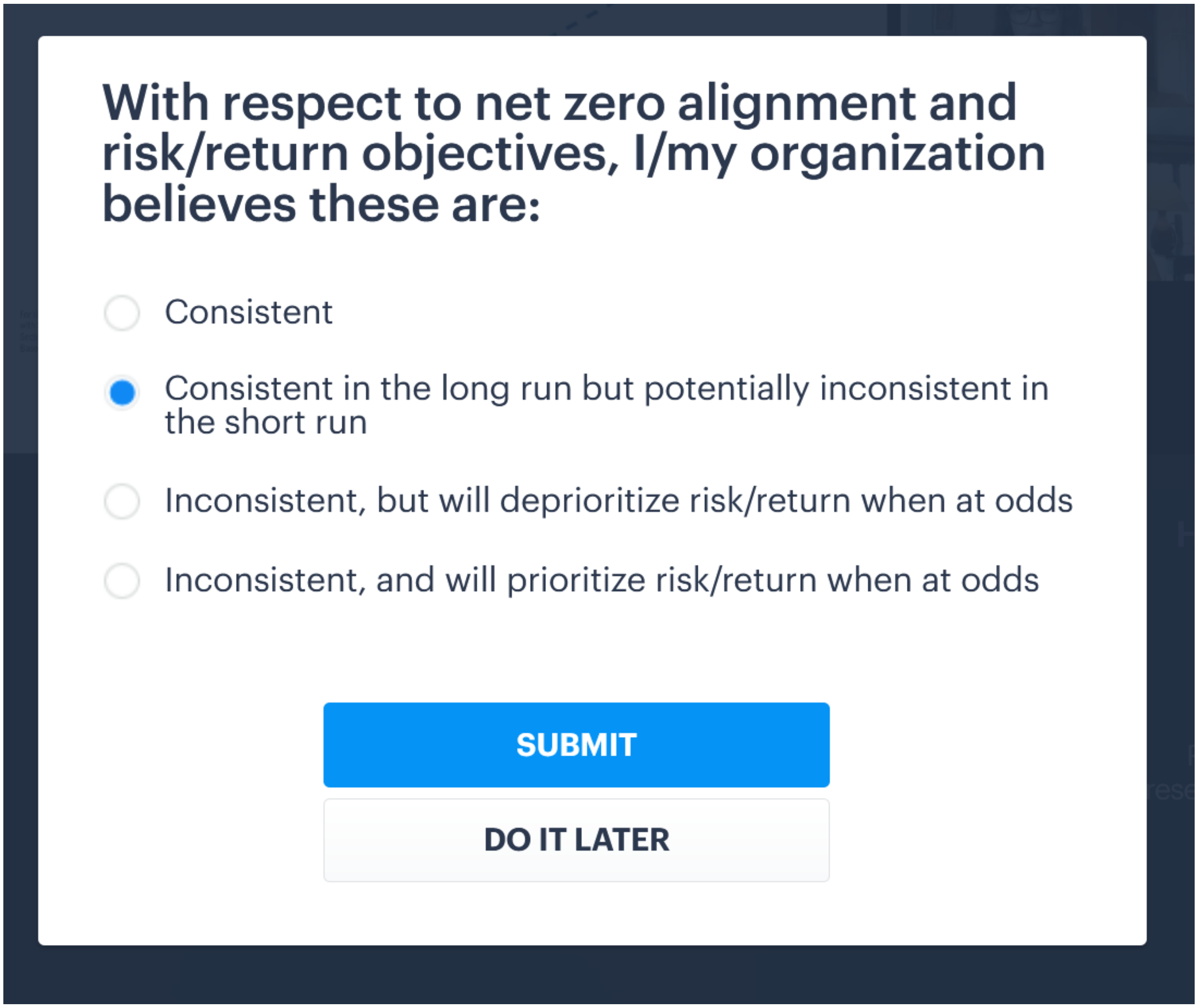
- The three main commitments on the second question are outlined above
- On bullet 2
    - We'll be working on this and making the announcement in the leadup to COP26 in November
- There are two ratchets here – 1) the proportion of AUM that fall in the commitment and 2) towards the decarbonization over time, with a focus on the 2030 interim goal



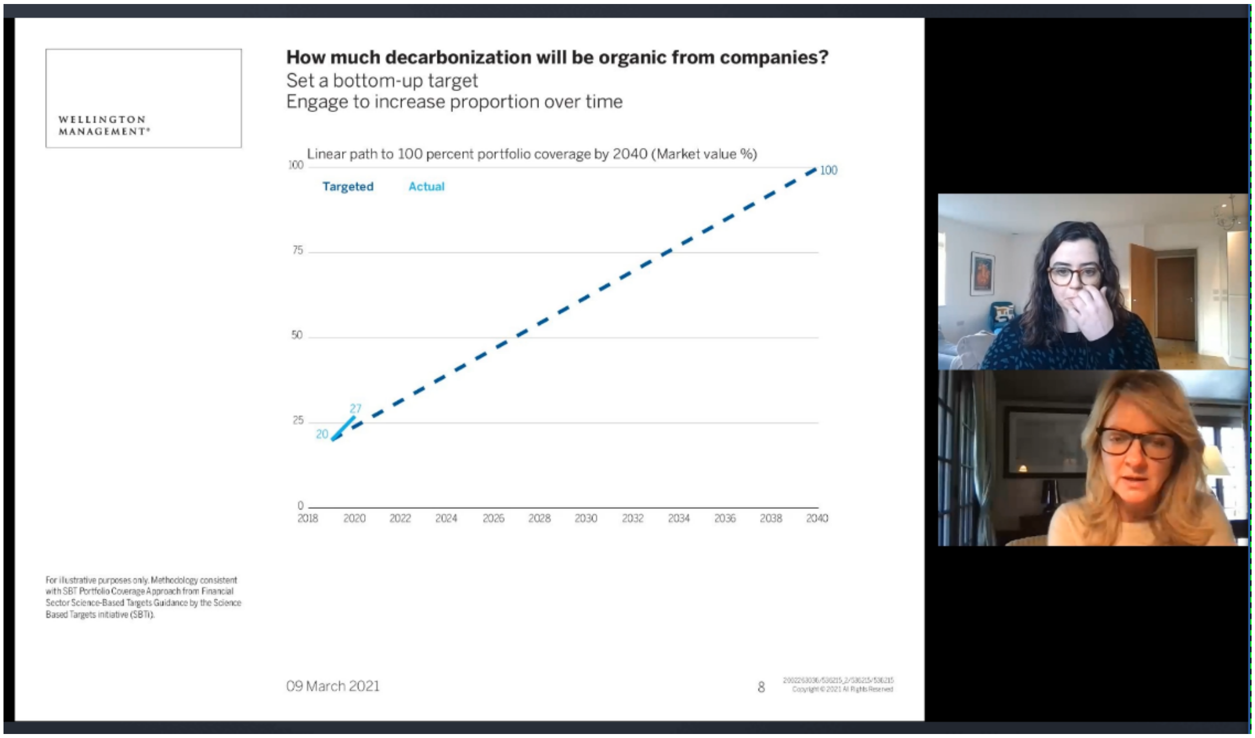
- We believe this is not a concensssionary commitment – it's principals based and there's flexibility in the commitment itself. It's credible by the groups that support it, and each client can look at their own business book
- We imagine each strategy will use a combination of the 5 tools outlined
- Our primary strategy at the outset will be engagement with companies to set science based targets, this is grounded in the research with Woodwell
- If we decarbonize by selling the emitters we're not insulating the portofios by climate risk because we're not decarbonizing the economy and they'll come back and affect the companies in the form of climate risk
- Recognizing that engagement won't always be successful, we believe in having a transition strategy for long term value that involves selling those strategies
- Underweighting and overweighting companies based on their profile is the crux of the portfolio construction
- Carbon offsets really are meant to be incremental – we see the use case scenario being that a manager has been working with a company, seen progress, and they're almost there but not quite where they need to be for the portfolio in that case they can buy offsets to get them over that speedbump and allow them to continue their work



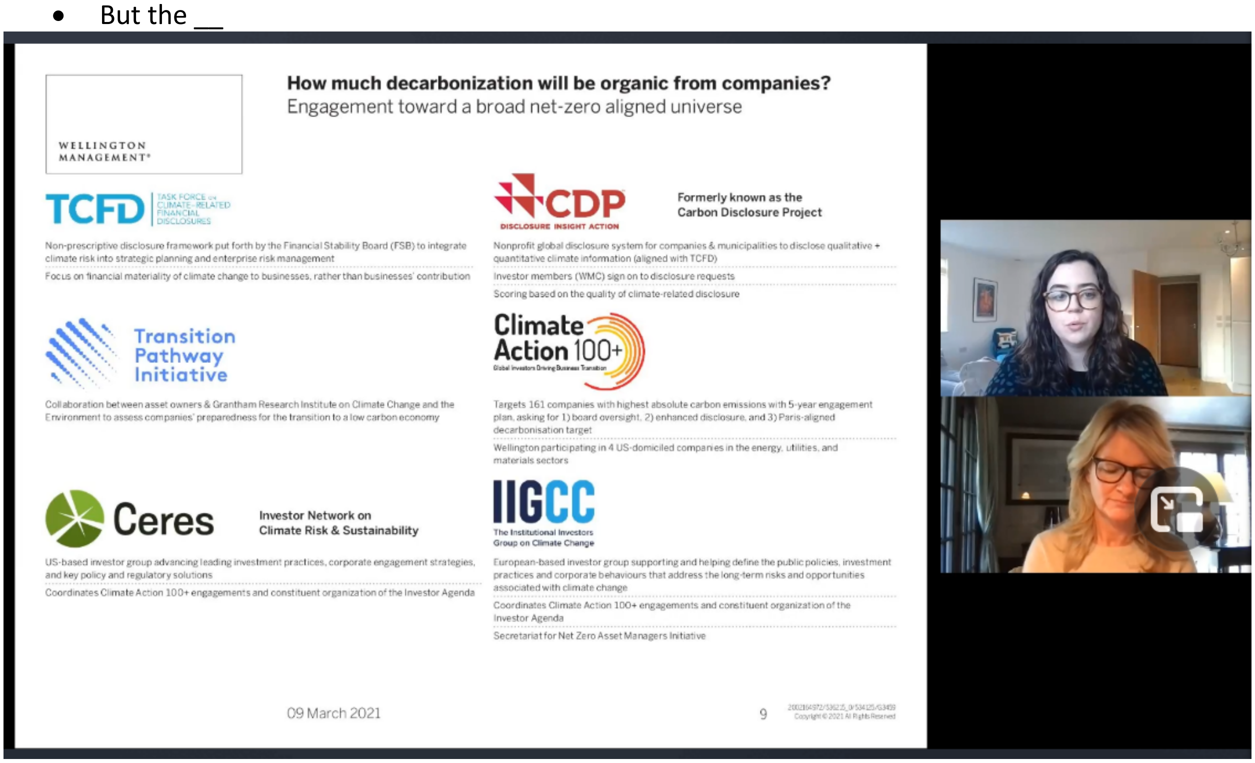
- I want to hit on the idea of a green premium and a brown discount from capital providers
- We have confidence that there is a financial materiality construct – as physical risks become more prevalent and acute we'll see more financial impact on the companies that aren't addressing this transformation
- The other thing we expect to see and are already seeing is the emergence of a net zero club – companies who have made commitments working with others



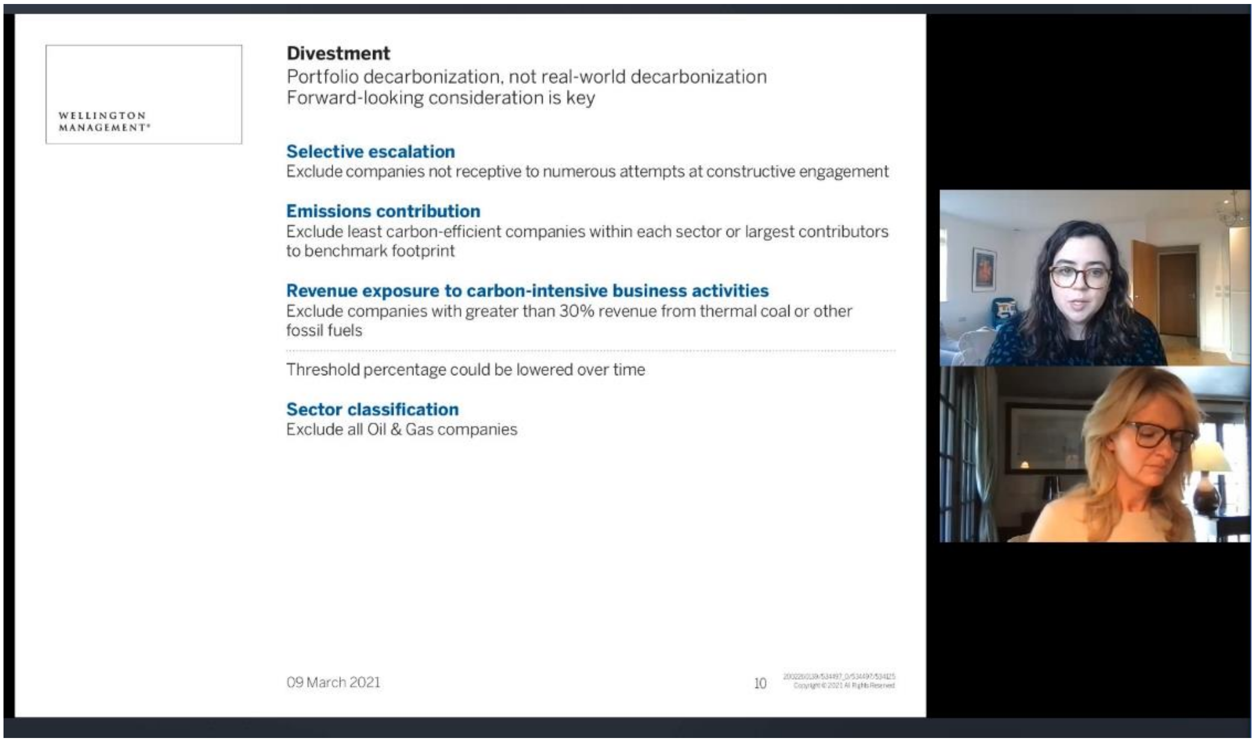
- Poll Results
  - B is the most common answer with 50-60%, followed by consistent at 30% - so most particpants believe we have long term alignemtn with risk/return and climate objectives



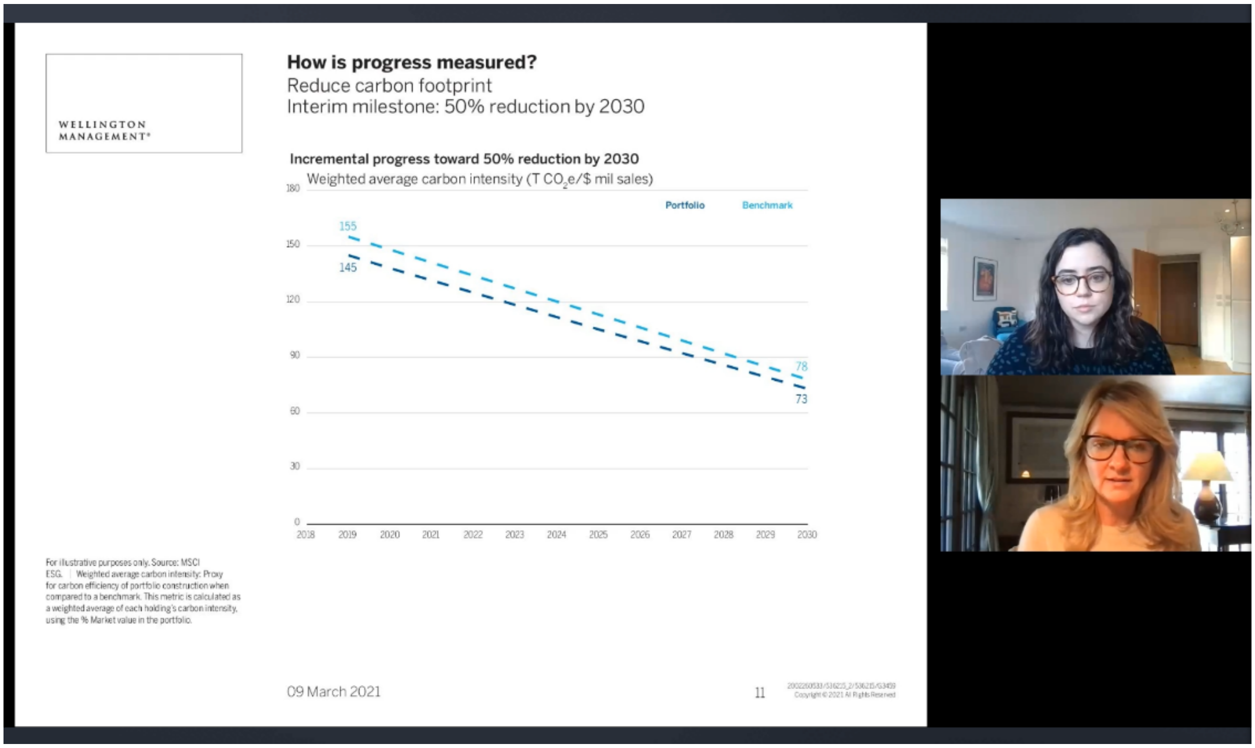
- We've been getting this question about how much natural decarbonization we can expect, more than 1200 companies have science based targets or are committed to setting them
- To measure portfolio alignment using a bottom-up message, we measure this vi
- ________
- While the lineaer target you're seieing on the chart is meant to emulate real projgress, we recognize that actual progress may be lumpier than that linear trajectory
- But the __



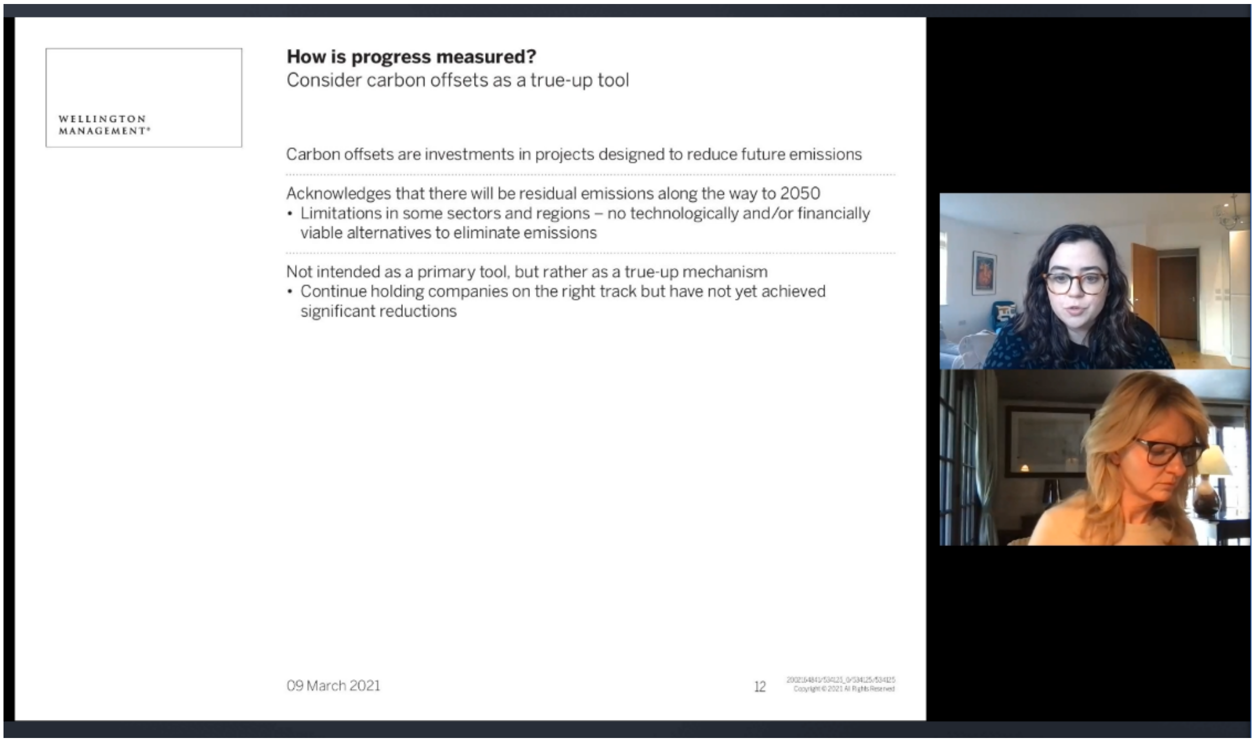
- We have equity, ESG, and _
- In addition to that ongoing private engagement there are an number of organizations that facilitate collaborative engagement
- TCFD
    - has become the recongized standard, so we encourage our companies to adopt that framework
- Climate Action 100
    - The three



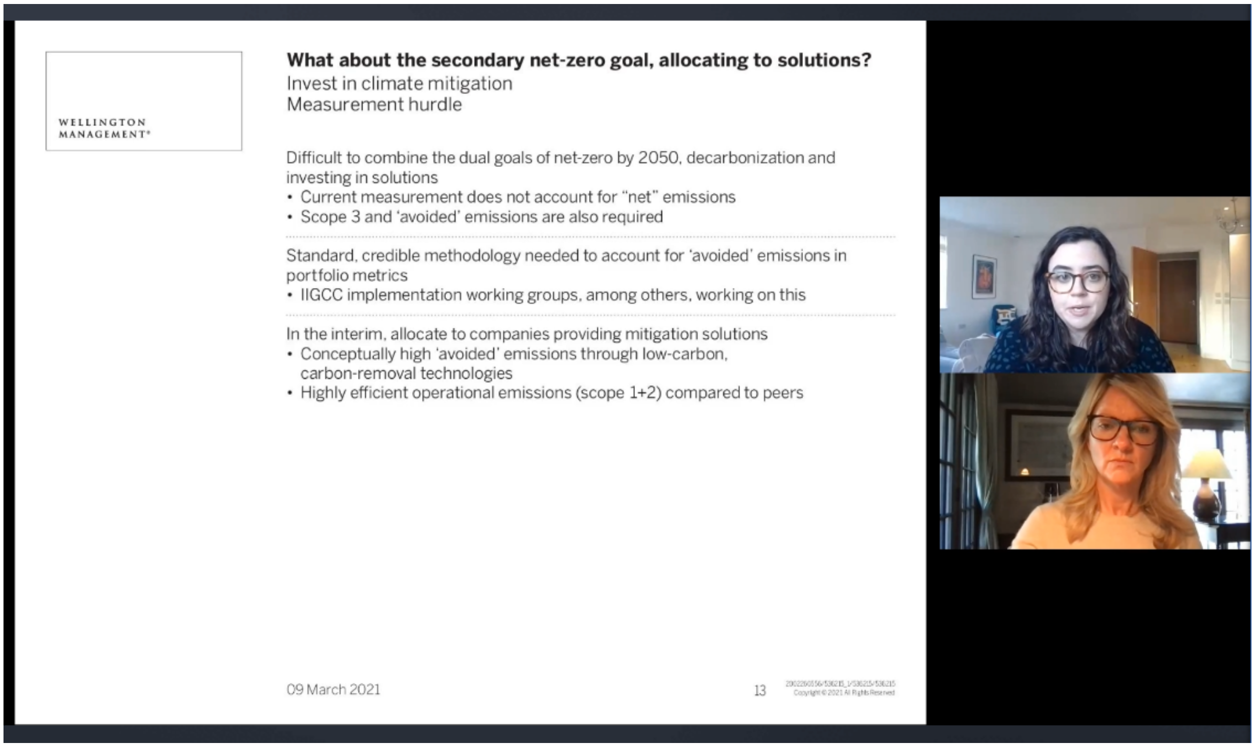
- We often think about divestment as the flip side of engagement, we know that some companies will be unable to successfully transition
- We primarly see divestment as an escalation tool where over time as we make progress to 2030 interim targets where companies are refusing to participate or are unable to keep up with their peers we'll use divestment as an escalation tool
- Audience Q: Why the emphasis on committing to targets as opposed to action?
    - The commitment to a science-based target is a commitment to action



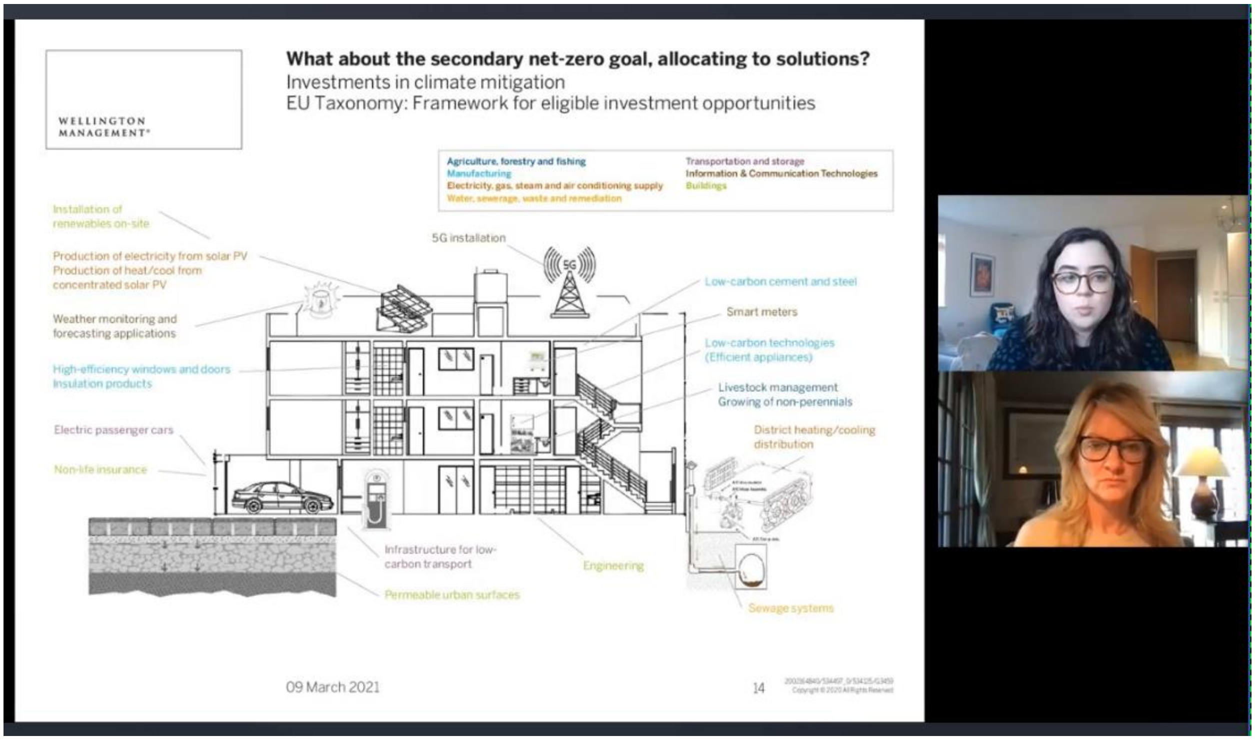
- We have clients who have both divestment and engagement as key parts of their strategy
- Those who lean towards divestment their rationale is that the cost of capital for those companies will go up so that'll force change
- On the engagement side the thought is if nobody is working with these companies to make these plans we're not going to have real reduction in society only in our portfolio
- There's also the question of how we're going to hold ourselves accountable, for the assets we commit to manage in line with 2050 we commit to a 2030 50% reduction identified in the IPCC report, so additional benchmarking details are being discussed among NZAM members
- Its agreed that 2019 is going to be the benchmark year for assessing progress



- It's worth noting each strategy will be assessed independlly
- The NZAM has allowed fo the purchase of credible incremental offsets, but only for those who have made significant progress
- We could have a strategy who's primary tool is engagement which in 2029 is exceeding its requirement on that primary measurement tool but because of the nature of the footprinting they only see 40% instead of 50%, we'll use that incremental 10% to purchase offsets while using _____



- There are two goals in net zero – to debaronbiase and to invest in low carbon solutions
- However it's currently difficult to marry that into a single metric, we're not thinking about net carbon exposure in traditional metrics we're mostly looking at ___
- So avoiding emissions in scope 3 ___
- The market hasn't developed metholdoies for measuring this
- The concern around netting is that fossil fuels will continue to be owned and operated, this should be addressed in a more nuaned way and this where the IIGCC ___



- Putting the hurdle of combining those two goals into one metric aside, there are good tools available
- The EU taxomony is aiming to help identify solutions – it's a classification system intending to provide universal defintiions and sets a high bar for capitalizing the transition towards a sustainable economy – we believe public and private capital will be aligned b ____
- The taxonomy also raises e

AudienceQ&A
- Do you consider scope 3 emission in your NZ calculations?
  - JD Great questions, this was one of the internal hurdles in the specific of the commitment because the inteiont is to cover all three scopes
  - Emissions disclosures ons cope 3 are really in thei rinfacy , but we think about a 30 year horizion we're making the assumption that enhanced measurement tools and data will occur
  - We're currently using scope 3 for research purposes but not for target setting ___
  - These data sets are still quite new and can't caputure company nuances, we don't want to be myopic ___
- WC – One of the things I think is going to unlock potential is investing in technology
- Do you see national governments as a limitor to progress, particularly when looking at sovereing bonds held? What about other asset classes?
  - JD – we know that all of our assets aren't in corporates so this was another hurdle, and its' been acknowelged in the NZAM statement that there's more to develop and sovereign is in those cateogires
  - We have initial guidance from the paris aligned investment intitative but more will be developed and it's part of the main workstream for the implementation working group
  - It's an area where we wanted to be part of the initiative to allow us to work in setting the standard rather than comply withs tandards we didn't have einputs into

    - I don’t think we need to have the plan finlaised now – we know that the first step is to start with egnagementn improve disclosure
    - That can begin even with thise imperfections and question marks
    - WC – one of the tactical things we did that allowed us to make the commitment internally was to create a massive spreadsheet of all of our funds and their potential paths and where they stand today and where they might go, a hypothetical of 2030 and 2050 including science based targets, portfolio construction, divestment, ect.
- Who is purchasing the offsets – Wellington or the investors?
- How can offsets be considered consistent with fiduciary duty?
    - Offsets are only going to be used very incrementally to help aritucal investors who are very close to a particular target because they’re working with a company an ddon’t want to give up on the company just yet
    - In that case wellington would purchase the offsets
    - We don’t expect them to ____
- Ben ____ also the IIGCC doesn’t permit them to
    - Just as a reminder the IIGCC is the sectrariate for the as is CDP,
- Are you findinding that US University and Endowments are more receiptive than before?
    - WC – yes, ___
    - We often saw them divesting from thermal coal which is a start (which they were able to make because it was a small market cap and it wasn’t a big commitment)
    - But we’re also seeing divestment from fossil fuel

Next Steps

- WC – we started working on this in late summer and made the commitment in December, so in AM terms that’s warp speed
- Internally our process involve dlots of focus groups with managers and investment leaders, which helped us frame the decision and dive deeper into the ___
- Acknoweding that weakness up front.
- A
- A
-