Greater Manchester Pension Fund starts on the path to fossil fuel divestment.

But there is still a long way to go.

Fossil Free Greater Manchester is pleased to report some progress in our campaign for the Greater Manchester Pension Fund to cease investment in fossil fuel companies. In a fourteen page letter to councillors and MPs who had written to the Fund at the request of our supporters, the Fund demonstrates that it has taken on board arguments of the Fossil Free campaign, with a commitment to move to a fossil-free investment portfolio, but its strategy for getting there still leaves a lot of room for improvement. Most critically, it has yet to take the decisive step to move its money from financially risky, planet burning investments into something better.

> *"...**climate change** poses a key financially material environmental risk*
> *"The Fund's long-term goal is for 100% of assets to be compatible with the net zero emissions ambition by c2050 in line with the Paris Agreement.*
> *"A key strategy ….. is investments in low carbon and renewable energy opportunities.*
> *"The Fund recognises that ... it has assets ... that are at risk of becoming '**stranded**' in a 2 degree scenario. It will address this risk through a suitable decarbonisation plan … a plan for re-balancing the portfolio that substantially reduces exposure to this intensity.*
> *"The decarbonisation plan may involve a partial **divestment** of carbon intensive assets."*
>
> Letter from Greater Manchester Pension Fund[1].

Background

Greater Manchester Pension Fund (GMPF) is the largest local government pension fund in the UK, providing pension services to the ten Greater Manchester councils and a number of other employers. It has the largest investments of all local government pension funds in fossil fuel companies, in terms of both the scale of the investments (£1.2Bn shares in fossil fuel companies and a further estimated £0.5Bn indirect investments via, for example, managed investment funds) and as a proportion of its total investments (10.23%, or which 7.22% are direct holdings). It is indeed the dirtiest of the council pension funds[2].

1 Quotations from a fourteen page letter from Greater Manchester Pension Fund in response to Fossil Free Greater Manchester's call for divestment from fossil fuels (our emphasis) 28 November, 2017.

2 Figures from March, 2017: *Fuelling the Fire*, a joint report from 350.org, Community Reinvest, Friends of the Earth England Wales and Northern Ireland, Friends of the Earth Scotland and Platform.

In 2015, our campaign, Fossil Free Greater Manchester (FFGM) called upon the GMPF to:

1. Immediately freeze any new investments in fossil fuel companies;
2. Divest from companies involved in the exploitation of coal and unconventional oil or gas within two years and all fossil fuel companies within 5 years;
3. Work with the Greater Manchester Combined Authority to develop and fund a low-carbon investment programme for Greater Manchester.

We collected more than 5,000 signatures to our petition supporting our call and presented it at the Fund's Annual General Meeting in October, 2017.

The Fund has now responded to our call with a fourteen page letter. In the interests of brevity and clarity, we will not answer every point in the letter, but respond to the main statements and arguments it presents.

We welcome the Fund's commitment to openness and we aim to respond constructively.

Fossil Free Greater Manchester's Response

Key points

There is a lot to welcome in this letter, including,

- Multiple statements about risks from climate change.
- Statement that "there is a place for disinvestment", and that Fund has done it before together with the mention (three times in all) that their evolving approach could be called "partial divestment".
- Positive, large investments in green infrastructure.
- The commitment to transparency.

But there remain significant points that we must challenge, particularly the very weak case against divestment (or rather, against full divestment, since the principle of at least partial divestment is accepted by the Fund). In this regard, two statements are made without any substantiation:

- It is asserted that divestment "creates an unacceptable risk", but no evidence is presented to justify this.
- It is stated that "the pace of decarbonisation must be consistent with our risk framework", with the implication that going faster would not be consistent with that framework. Again, no evidence to support this is presented.

Since risk is cited as the chief reason for not moving to a managed programme of full divestment, we might have expected some kind of an analysis of the risks of divestment. None is provided. Indeed, the only information presented on risks (risks from climate change and risks of asset stranding) is consistent with our proposal.

https://gofossilfree.org/uk/fuellingthefire/

What the Fund says

The letter from the Fund helpfully summarises its present positions and arguments. We use them to structure our response, making additional reference to more detailed material in the Fund's letter where appropriate.

Detailed response

1) We recognise that climate change poses a key financially material environmental risk, and the Fund is committed to working towards a 2 degree warming scenario and were a signatory to the Paris Pledge for action.

This is a good start but what does it mean in practice? Here and elsewhere the Fund is vague when it comes to its plans in terms of time-scales and specific actions. To evaluate this commitment of the Fund we need to know just what constitutes "working towards a 2degree scenario. However, the clarificatory text[3] also states that: "Paris Pledge for Action supporters are explicitly committed to limiting global warming to under 2 degrees" and "Supporters of the Paris Pledge for Action can now be guided by the Paris Agreement to pursue their own efforts to limit temperature increases to 1.5 degrees." The Fund's statement is, perhaps inadvertently, weaker.

2) We wholly support the Bank of England Governor Mark Carney's statement that 'Financial decarbonisation of our economy is a major opportunity for long-term investors'. If pension funds are genuine long term investors, then they may be well placed to benefit.'

We welcome this acknowledgement that the Fund, and hence its members and the people of Greater Manchester, can benefit from decarbonisation of its assets. But the Bank's message was also about the wider risks of investors not acting to decarbonise portfolios. The crucial passage from the Bank of England's report on climate risk (p 104 [8]) noted that,

"While the risk of a sudden and significant system-wide adjustment may not be immediate, the financial risk from an abrupt transition to a lower-carbon economy can increase if, over the coming years, portfolios are not aligned with climate targets. If governments push ahead with climate policies, but investors do not adapt their investment strategies accordingly, misallocation will grow. This could ultimately lead to a 'climate Minsky moment' — a rapid system-wide adjustment that threatens financial stability, as discussed by Governor Carney in 2015."

3) We welcome the recommendations of the Financial Stability Board's Taskforce on Climate-related Financial Disclosures (recently presented formally to the G20) to which we were a signatory and commit to including a TCFD statement in our financial reporting from 2018 as part of our on-going climate risk assessment and disclosure.

3 http://www.parispledgeforaction.org/wp-content/uploads/2015/08/Paris-Pledge-for-Action-FAQs-2016.pdf

We welcome this and the statement later that climate risk matters will be integrated into the Fund's standard reporting arrangements. However, climate risk assessments are complex and contested: we therefore suggest that the precautionary principle be applied, in effect erring on the side of caution.

The Fund refers to its collaboration with with ShareAction on a European-wide project led by the World Wide Fund for Nature (WWF) that aims to foster the alignment of investment portfolios with a below 2°C scenario through developing “Sustainable Energy Investment (SEI) metrics”. The WWF report that t he Fund cites notes: "In addition, Greater Manchester pension fund discloses its holdings but includes a disclaimer that reproduction or use is not permitted without the express prior written consent of the copyright holder: such consent was not provided upon request by WWF." We call on the Fund to permit the publication of this information in keeping with its stated commitment to transparency and to help stakeholders form their own view on the Fund's approach to risk.

> 4) The Fund has an excellent long term investment track record, over the last 30 years; the value of its **returns has been over £3 billion more** than would have been the case if it had achieved the average LGPS fund return. This has meant that every household in Greater Manchester has not had to pay an additional £2,500 to meet pension liabilities.

The implication here seems to be that the Fund's success is a result of its heavy fossil fuels loading. If that is the intent, then the point should be explicit and supported by clear evidence. But “past performance is not a guide to future returns”, and while fossil fuel investments were traditionally regarded as safe, “defensive” holdings, this situation is changing. At a recent talk in Manchester[4], the founder of Carbon Tracker, Mark Campanale, claimed that some oil majors are now borrowing in order to pay dividends. Or maybe this point is included as a “trust us” appeal, and again the standard investment caution is pertinent. Either way, the argument is not made clear.

> *5) The Fund’s long-term goal is for 100% of assets to be compatible with the net zero emissions ambition by c2050 in line with the Paris Agreement. The decarbonisation goal will be regularly evaluated in line with our objective of maintaining long term financial performance*.

This we welcome but the far more important issue is “what are the shorter-term intentions?”. We know that it is the cumulative emissions that count, since all the time CO_2 is being put into the ecosystem through burning fossil fuels. Time is something we do not have. And what are the steps to meeting that longer term goal? That too implies rapid change. Again the Fund makes the right noises but fails to substantiate them with clear, quantified plans.

> 6) As a Local Government Pension Fund we are long-term investors with liabilities reaching way beyond the year 2100. The objective of the Fund is to meet the

4Hosted by ethical investment advisors, Castlefield, 27 June, 2017.

current and future pension benefits of public sector workers now and when they fall due.

We have never disputed that the Fund's primary role is to fund and pay pensions. Consideration of the financial consequences of climate change and asset stranding is material with respect to this mission.

7) Independent Analysis by True Cost have found that the active decisions of the Fund managers have resulted in a less carbon intensive fund, which is better aligned with 2 degree scenario. This is because overall the equity holdings possesses lower fossil fuel proportion than the benchmark as we are less exposed to oil and coal, whilst the natural gas exposure is considerably higher than the proportions under IEA's 2 degree scenario for 2030 globally.

This summarises information given in more detail on page 11 of the letter and it is not at all clear. It would seem that the TruCost analysis is solely of the power sector: that is not the largest source of fossil fuels in the GMPF portfolio. The oil and gas majors are. For anyone to understand properly what is being claimed here, they would need to see the TruCost report. Would the Fund please share that with us, in the spirit of transparency noted above?

8) The Fund acknowledges that it is transitioning and that this needs to be an orderly process to avoid stranded costs and ensure that we continue to deliver affordable and sustainable pensions for employers and taxpayers alike. The companies we invest in already produce more power through renewables than they do from coal and oil.

Firstly, we have been clear that divestment needs to proceed through a responsible management plan, hence the proposed time-scales in our 2015 call (quoted above). But prevarication means that the eventual reckoning is ever less likely to be orderly.

Secondly, we are puzzled by the second sentence: it would appear to refer to electricity generation which is not highly oil intensive. If we misunderstand the claim, then please provide the data.

9) Within the last two years, the Fund has increased its strategic allocation to infrastructure to 10%, unlocking over £2 billion of assets for this purpose. A key strategy within this allocation is investments in low carbon and renewable energy opportunities.

The green infrastructure investments are obviously good, but what proportion of the total do they represent? We have not been able to find the figure. As for the rest of the infrastructure investments, what are they? How many are carbon intensive? Just because it is infrastructural, it doesn't mean it is green. While announcing the good investments, no mention is made of the astonishingly high investments in the Fund's two biggest holdings, Shell and BP, nor that GMPF is the only UK pension fund with holdings in what the Fossil Free Indexes[5] identifies as the (non State-owned) company with the biggest carbon footprint worldwide, Adani, whose latest investment will add to

5 http://fossilfreeindexes.com/

the damage already sustained from climate change by the Great Barrier Reef[6]. We appear to be being offered a bit of greenwash here.

> 10) The pace of decarbonisation must be consistent with our risk framework, and not detract in any way from our fiduciary responsibilities to pay our pension promises to public sector workers which are affordable and sustainable to the taxpayer. All employers and the taxpayer have benefited from this outperformance through lower employer contribution rates and the Fund being better funded than most LGPS funds, which will provide more long term benefits to the employers in the Fund and enables more to be spent on local services.

Firstly, we are not given any information about the "risk framework", and as we have said above, the precautionary principle should frame it.
Secondly, the statement implies that more than a leisurely pace of divestment would be inconsistent with this framework: no evidence is provided to support this contentious statement.
Thirdly, a narrow definition of fiduciary duty is implied. Changes to understandings of fiduciary duty in the recent years and months[7] indicate that a wider frame of reference should be taken, IF the Fund is to discharge its duties to beneficiaries now and in the future as well as to others affected by the funds actions, in Greater Manchester and worldwide. There are far greater risks to the funds' beneficiaries of actual climate change at 2 or 4 degrees – and not just ones about pension fund value.
Fourthly, the appeal to the Fund's good performance is made again. Let us quote from the Fund's statement on tobacco divestment, where it showed both sector leadership and a good understanding of its wider responsibilities: *"Tobacco stocks have performed exceptionally well over the long term relative to the market, but this is not a guide to future performance."* If the Fund could divest totally from tobacco given the health impacts, and the role of local government in defending and improving Public Health, then why not apply the same standard to fossil fuels, with their far wider Public Health and well-being impacts?[8]

> 11) The Fund is not adopting this approach from a standing start as regards climate-aware investing and much of the task now involves a scaling-up of activities. We have led the way and are the biggest direct investor in green energy.

6 https://theecologist.org/2017/nov/16/biggest-uk-pension-fund-backs-coal-mine-set-destroy-great-barrier-reef

7 The Pensions Regulator: http://www.thepensionsregulator.gov.uk/trustees/investment-management-in-your-dc-scheme.aspx The recent government announcement on dropping the "best return" rule will have been noted by the Fund: https://www.theguardian.com/environment/2017/dec/18/boost-for-fossil-fuel-divestment-as-uk-eases-pension-rules

8 The 2015 ***Lancet Commission on Health and Climate Change*** concluded that, *"climate change threatens to undermine the last half century of gains in development and global health".* They noted that, *"The direct effects of climate change include increased heat stress, floods, drought, and increased frequency of intense storms, with the indirect threatening population health through adverse changes in air pollution, the spread of disease vectors, food insecurity and under-nutrition, displacement, and mental ill health."* http://www.thelancet.com/journals/lancet/article/PIIS0140-6736(15)60854-6/fulltext

We agree there is a need for a major scaling up of what remains a small relative proportion of the Fund's investment activity – in comparison to the truly enormous commitments to the fossil fuel industry.

The body of the letter advocates for engagement with the fossil fuel majors as perhaps the preferred approach to climate-aware investing. We have explained elsewhere that this is unlikely to yield any significant climate-friendly results[9]. Briefly, engagement is a legitimate tool, for example where there is the prospect of a company yielding to pressure in an aspect of its practice. Intervention regarding company pay ratios is a good example. But the Fund confuses the viability of engagement in such cases with the entirely different case of changing the fundamental business model of a company. In reality, engagement objectives with the fossil fuel majors have been limited to cosmetic questions such as reporting and research and development. Shareholder actions have been blocked in some cases and in others, neutralised by adoption and prevarication. This is clearly the case in relation to the Fund's two biggest holdings BP and Shell as documented in reports by Share Action this autumn[10]. We have previously asked what the aims of engagement with these companies are and received no answer. We have carefully reviewed the reports on engagement produced by the Local Authority Pension Funds Forum and found no evidence of any significant impacts on fossil fuel emissions through engagement. Nor have we found any evidence that engagement is linked to an appropriate repertoire of actions including, as Share Action advise, divestment should prevarication and non-compliance continue.

The letter also devotes space to arguing against divestment, having already, on page 4 stated, "*We agree that there is a place for disinvestment*". The letter goes on to suggest that, "*However, we believe that divestment is a blunt tool and doesn't necessarily improve or change matters*". But we are saying there is an ethical case to not invest in them. The Fund did not try to change the behaviour of tobacco companies for that reason. It was just wrong to hold such stocks. And we contest the assertion that divestment would not change matters: it is the snowball effect of more and more investors pulling out from the sector that sends a strong signal to the market that these companies cannot rely on investment streams, and therefore their financial model is under threat. It also sends a message directly to those companies. Is the Fund saying that it knows better than investors like Zurich Insurance, Lloyd's of London, New York City, the Norwegian Sovereign Wealth Fund, and GMPF's pool partners Merseyside Pension Fund?

9 Our response to the Fund's consultation on its Draft Investement Strategy Statement http://fossilfreegm.org.uk/wp-content/uploads/2017/11/FFGM-response-to-GMPF-Investment-Strategy-Statement-v2.pdf

10 Shell: https://shareaction.org/wp-content/uploads/2017/10/InvestorReport-AimingForA-Shell.pdf BP: https://shareaction.org/wp-content/uploads/2017/10/InvestorReport-AimingForA-BP.pdf

A further questionable statement is, "*A major influence on investment strategy is the time taken to make the transition to sustainable sources*.". However, this is not relevant. The Fund does not have to replace holdings in, say, Shell with wind farm (or similar) shares. As we note in our briefing paper for councillors and others, given the scale of the investments, it will probably not be possible (and probably not desirable) to switch just to renewable energy. There are many other investments available that are not carbon-intense, the other ~90% of the Fund's holdings are a case in point. Of course we advocate local and green investments where possible, but we are realists too: the pressing priority is to dump these toxic fossil fuel stocks.

> 12) The Fund recognises that like all pension funds it has assets within its investment portfolio that are at risk of becoming 'stranded' in a 2 degree scenario. It will address this risk through a suitable decarbonisation plan that measures the Fund's ownership responsibility for emissions; locates the areas within the public equities portfolio of highest carbon and reserves intensity; and implements a plan for re-balancing the portfolio that substantially reduces exposure to this intensity. The decarbonisation plan will be similar to those being carried out by other leading European asset owners, such as ABP (Netherlands), AP4 (Sweden), FRR (France) and the Environment Agency Pension Fund (UK).

This is really positive step-forward and as the Fund acknowledges, this is actually a partial divestment approach. To be convincing the strategy must be strong, transparent and fast as possible. The Fund should be explicit that it is not just being made for reasons of financial risk but for other ethical reasons: to reduce the risks to lives and livelihoods of beneficiaries as well as those other people affected who may be in Greater Manchester, or far away, in time and in space. On the specifics, what is the time-scale? What sectors will be divested first? We have produced an analysis suggesting a methodology for picking the "worst companies"[11], and this could be built on.

Conclusion

We welcome the Fund's initial moves to a climate-safe investment strategy but are concerned that a) it remains vague, without targets, priorities nor time-scales and that b) unsubstantiated assertions are made about the risks of more ambitious divestment.

We therefore make the following requests to the Fund:

1. Other pension funds and public authorities have chosen to plan for full divestment and found the risk palatable. Why does GMPF find full divestment an unacceptable risk?

11 http://fossilfreegm.org.uk/index.php/2017/09/03/companies-worst-gmpf-fossil-fuel-holdings/ see also the report from Schroders which suggests a different approach: http://www.schroders.com/en/lu/professional-investor/featured/climate-change-dashboard/carbon-var/

2. What time-scales, priorities and targets does GMPF have for progressing its current partial divestment strategy? Will it commit to divest from coal within 2 years and from all fossil fuels by 2023?

3. Why did the commitment to transparency not result in giving WWF permission to publish data on the fund, and will more frequent and detailed data on holdings bought and sold be made public?

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Fossil Free Greater Manchester
c/o Manchester Friends of the Earth
Green Fish Resource Centre
46-50 Oldham Street
Manchester
M4 1LE