PARLIAMENTARY CONTRIBUTORY PENSION FUND

Review of managers' compliance with the Trustees' investment policies – July 2019

GROWTH MANAGERS – MFS, BlackRock

MFS	Managing the Fund's mandates in line with its policies In its responses MFS states: "We believe our long-term investment approach in the Global Equity portfolio, which seeks to own companies with sustainable above-average growth prospects and below-average risk at reasonable valuations, and tends to invest in highly liquid securities, is supportive of PCPF's investment principles, although the portfolio's investment objectives are defined relative to the benchmark index rather than as a function of a discount rate and/or the CPI."
MFS	Assessment of ESG-related risks MFS allocates responsibility for integrating all factors that could potentially impact the outcome of the investment process – including ESG considerations – on its research analysts and portfolio managers. It reports that: "We also have investment staff dedicated solely to ESG research, who support and enhance the research on ESG topics that is performed by our team of fundamental industry analysts and portfolio managers. Our ESG analysts have developed a detailed and comprehensive ESG integration strategy designed to enable the broader investment staff to better understand how ESG issues can impact their decision-making process." The team's strategy includes both analytic and systematic elements, as set out below: Analytic • Direct collaboration with analysts and portfolio managers to assess the materiality of ESG factors for specific securities as part of the fundamental research process • Thematic, sectoral, and regional research, both regular and periodic, disseminated and presented to the broader investment team in a variety of settings

	• Regular communication of ESG in Depth series of insights containing research on current ESG topics that are impacting the securities we own • ESG sector maps that highlight ESG risks and opportunities within each sector <u>Systematic</u> • MFS' semiannual portfolio risk reviews include ESG ratings and trends in each portfolio • ESG ratings changes are also disseminated on an ongoing, systematic basis • Research notes for each company and issuer are housed in our global research system and include a tab dedicated to ESG information • Low rated securities are highlighted to covering analysts and portfolio managers via automated reports	
MFS	<u>Largest exposure to carbon risk, and why?</u> Based on Trucost carbon intensity data from Style Research, the Global Equity portfolio has historically had lower carbon intensity than the benchmark MSCI All Country World Index. As of 31 March 2019, the Global Equity holdings with the highest contribution to relative carbon intensity versus the MSCI All Country World Index are industrial gas companies Linde and Air Liquide. While we recognize that these industrial gas companies have relatively high carbon intensity, a substantial portion of their revenue streams are generated by products used by their customers to reduce their own carbon footprint. As a result, we feel a simple carbon footprint does not accurately measure their true climate-related impact.	<u>Examples of investment 'engagement'.</u> In its response, MFS set out its engagement framework, which includes: Formal proxy voting led engagement, Informal and Formal investment team led engagement and Collective and other forms of engagement, the latter including participation in industry working groups and thought-leadership groups. MFS outline how a combination of voting and engagement with two companies has led to positive change: "In recent years, our engagement activities have contributed to positive changes to the compensation structure at a US-based pharmaceutical company. Collaboration between our proxy voting team and

	While ESG considerations often weigh heavily in our investment decisions, we do not generally decide to invest or not invest in a company solely based on certain ESG factors. Despite their carbon risk, we believe the industrial gas companies should benefit from a favourable industry environment with high barriers to entry, a consolidated market, long term contracts and a diversified customer base; we feel they offer high quality defensive earnings with above-average growth prospects through cycles, and their shares are trading at reasonable valuations.	investment team identified concerns that certain metrics underpinning the company's short-term executive incentive plan could potentially result in an excessive pay package. Over the course of multiple engagement calls we communicated our concerns and discussed the specific components of the compensation structure that were potentially problematic. The company has since made meaningful revisions to the compensation structure in response to shareholder feedback.” “we voted against the members of the technology committee in light of concerns with oversight at a data and analytics company after a major data breach. The company has since made sweeping changes to board composition and the executive team, including separating the role of chairman and CEO and the hiring of a new chief technology officer. The company has also incorporated cyber security risks into the long-term compensation program and has focused heavily on employee training and monitoring.”

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<table>
<tr><td>BLACKROCK</td><td colspan="2"><u>Managing the Fund's mandates in line with its policies</u>

In its responses, BlackRock confirmed that it is "contractually obliged to comply with the Investment Management Agreement (IMA) between us and the Trustees. I can confirm that the IMA has been complied with. It is our understanding that it is the Trustees' responsibility to ensure that the Investment Management Agreements are in line with the Statement of Investment Principles (SIP). So, to confirm, the fund will be managed around the agreements within the IMA, which will have been agreed with the trustees."</td></tr>
<tr><td>BLACKROCK</td><td colspan="2"><u>Assessment of ESG-related risks</u>

We believe that companies with sound corporate governance practices, including how they manage the environmental and social aspects of their operations, better mitigate risk over the long term, and offer better risk-adjusted returns. We engage with companies held in our full range of mandates that includes alpha-seeking, factor, indexing, and sustainability strategies alike to encourage them to adopt robust business practices consistent with sustainable long-term performance. Our Investment Stewardship efforts, including our direct engagement and voting activities, encourage companies to deliver long-term, sustainable growth and returns for our clients. As a large investor, we are able – and feel a responsibility – to monitor the companies in which we invest and to engage with them constructively and privately where we believe that would help protect clients' interests. As a fiduciary investor, BlackRock evaluates how companies manage the material sustainability-related risks and opportunities within their businesses. Engagement helps build mutual understanding on any issues where we are concerned that a company's practices fall short of operational excellence. It also helps us assess a company's approach to governance in the context of its specific circumstances. We have committed to increase the size of the investment stewardship team over the next few years, which will enable BlackRock to significantly increase its engagement activities and foster more effective engagement by building a framework for deeper, more frequent, and more productive conversations.</td></tr>
<tr><td>BLACKROCK</td><td><u>Largest exposure to carbon risk, and why?</u></td><td><u>Examples of investment 'engagement'</u></td></tr>
</table>

	As an index manager, it states: “we do not assess which stocks have the biggest exposure to carbon risk when constructing the portfolio as we do not have discretion to do so.” “Because index portfolio managers do not have discretion to add securities outside of those in the benchmark index, nor remove securities that continue to be held in the relevant index, our approach to ESG integration in index investment mandates emphasises our investment stewardship activities. Direct engagement with companies, including proxy voting, is the mechanism we use to integrate and advance material sustainability insights to enhance long term risk adjusted return.”	“Engagement is core to our stewardship program as it helps us assess a company’s approach to governance, including the management of relevant environmental and social factors. We see environmental and social issues as corporate governance issues, integral to successful company management. To that end, we conduct approximately 2,000 engagements a year on a range of ESG issues likely to impact out client’s long-term economic interests. We meet with executives and board directors, communicate with the company’s advisors, and engage with other shareholders where appropriate. As a long-term investor, we are patient and persistent in working with our portfolio companies to build trust and develop mutual understanding. We do not try to micro-manage companies, or tell management or boards what to do; we present our views as a long-term shareholder and listen to companies’ responses. Engagement helps better inform BlackRock’s voting and investment decisions. We will vote against management when we judge that direct engagement has failed.”

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INCOME/GROWTH MANAGERS – M&G, Schroders, UBS

M&G	<u>Managing the Fund's mandates in line with its policies</u> M&G confirm that they have assessed the PCPF's prescribed Voting & Engagement Policy and Statement of Investment Principles, the allocation continues to be aligned to your investment belief in respect of an allocation to alternatives, namely: *"The Trustees believe that diversification across asset classes can help reduce the volatility of the Fund's overall asset value and improve its risk-return characteristics. The Trustees believe that investing across a range of asset classes (including (but not restricted to) equities, government bonds, corporate bonds and property) will provide the Fund with diversification benefits"*
M&G	<u>Assessment of ESG-related risks</u> To deal effectively with ESG risks and opportunities, an extensive level of investment analysis is required. Our credit analysis team is large and well-resourced. It is also private-side, meaning that the level of engagement with portfolio companies can be higher than would be the case in public markets. Since 2013, specific items, issues and/or risks relating to Environmental, Social or Governance matters for each company are now explicitly recorded in a separate section of all credit papers and monitored on an ongoing basis. Where matters may not be addressed in detail, at inception of a loan, say (for example owing to a company only recently having been incorporated), then follow-up questioning will be conducted, with a view to supplementing our information, with updates being recorded, including at our portfolio review sessions, held twice a year. In addition, we conduct a regular calling programme with private equity sponsors, typically the owners of our portfolio companies, the better to understand *their* approach and commitment to ESG and to make the case for improved disclosure for debtholders. In the minority of cases where we lend to a listed company, MSCI ESG analysis is recorded. These can also give valuable insight into potential areas of investigation for unlisted peers that may form part of our portfolio.

	Lastly, though nothing that may formally be described as 'stewardship' is afforded to lenders, the ability to *engage* on ESG topics exists, thanks to an active relationship with company management and owners. This is the result of the lender-borrower relationship that arises from being a large, longstanding, private-side market participant.	
M&G	Largest exposure to carbon risk, and why? M&G explains "While it has limited coverage for the M&G European Loan Fund, owing to the private nature of the underlying issuers, across the M&G Group, we utilise the MSCI carbon analytics tool as a means of assessing carbon risks within our portfolios." M&G also disclosed a proxy carbon intensity contribution for each sector within the European Loan fund as at 31 May 2019 in its response.	Examples of investment 'engagement' As a credit investor, our access to management and ability to engage is somewhat different compared to our equity counterparts. However, we rely upon our market size and reputation to ensure we secure favourable terms that meet our long-term ESG objectives. As a private-side lender, we have active, iterative relationships with our borrowers, providing a conduit for engagement and lobbying. It should be acknowledged that our position as a secured lender puts us in a position of very limited influence over the policies of our portfolio companies from a formal perspective (no right to 'vote') so the power of influence is derived from the frequent interaction that comes from our private-side status and long-term relationships. M&G takes its responsibility as market participant seriously, being a Board member of the Loan Market Association. Inter alia, this allows for advocacy or a 'nudge' effect at market level with our firm having been involved in some important initiatives, including in 2018 the publication of Green Loan Principles.

		In partnership with UNPRI, in 2018, M&G wrote an article on ESG matters in private debt, including a case-study of loan issuer, Flora Foods (now known as Upfield). Exposure to the company is a conviction position for the fund, it being part of the Top 10 holdings, owing to its strong market position and responsible approach to ingredients sourcing. We have attached this article for PCPF’s reference.

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Schroders	Managing the Fund's mandates in line with its policies In its responses Schroders states that it has "reviewed the scheme's SIP but note that this is not directly relevant because the scheme is a direct investor in our pooled real estate fund, Schroder UK Real Estate Fund. As such it is bound by its own legal prospectus and investment processes. I also note that the SIP and related questions appear more appropriate to investment in equities and bond investments than real estate".
Schroders	Assessment of ESG-related risks Schroders UK Real Estate Fund Annual Sustainability report for the year ending 31 March 2018 states that: "A good investment strategy must incorporate ESG issues alongside traditional economic considerations. At Schroders we believe a complete approach should be rewarded by improved investment decisions and performance." In their sustainability policy, April 2019, Schroders state that they "understand social and environmental changes occurring across our geographies. Recognising the impact of these is integral to our investment process and applies to all aspects of real estate investment including acquisition due diligence, asset management, property management provided by third parties, refurbishments and developments. Understanding and improving our impacts sits alongside our priority to maximise returns for our clients in a manner consistent with our funds' risk profiles. We believe that a sustainable investment programme should deliver enhanced returns to investors, improved business performance to tenants and tangible positive impacts to local communities, the environment and wider society for the long term." They also state that "Property managers play an integral role in supporting the sustainability programme. Schroder Real Estate has established a set of Sustainability Requirements for property managers to adhere to in the course of delivering their property management services. This includes a set of key performance indicators to help improve the property managers' sustainability related services to the Fund and which are assessed on a six-monthly and annual basis at December and June respectively."

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Schroders	Largest exposure to carbon risk, and why? Schroders UK Real Estate Fund Annual Sustainability report for the year ending 31 March 2018 acknowledges that "Through its construction, use and demolition, the built environment accounts for more than one-third of global energy use and is the single largest source of greenhouse gas emissions in many countries." And that "The industry's potential to cost-efficiently reduce emissions and the consumption of depleting resources, combined with the political imperative to tackle issues such as climate change, means the property sector will remain a prime target for policy action." They also recognise that "Energy is an important element of landlords' responsibilities for buildings where the landlord has operational control. Schroder Real Estate has continued to develop the monitoring of the Fund's energy usage and efficiency as well as water and waste with analysis and reporting on a quarterly and annual basis."	Examples of investment 'engagement' "Wenlock Works is 130,000 sq ft of new office space due for completion in 2019. It is located in the area of Old Street Station which has become the epicentre of London's vibrant tech scene. Tenant wellbeing has been an extensive consideration throughout the extensive refurbishment. Wenlock Works cleverly reinterprets the warehouses of Old Street's industrial heyday to inspire new ways of thinking and working for its community of visionaries today. The building has good natural light, cycle facilities and a green terrace. The building is expected to achieve a BREEAM Excellent rating under the 2014 Refurbishment and Fit Out scheme." "Our sustainability programme involves driving continual improvement in building operations. To help this we set energy targets and for the UK portfolio we targeted a 6% consumption reduction over two years to 2018. Over the period we implemented a number of initiatives identified through auditing assets including LED lighting, voltage optimisation and improving efficiency of heating, ventilation and air conditioning (HVAC) systems supported improvements to building management. The programme achieved an 8.1% reduction which equates to 3.8 million kWh, 930 tonnes CO2-equivalent avoided and a saving of £340,000. This achievement led to being finalists for the 2019 Edie Sustainability Awards Energy Efficiency

		category together with our sustainability consultants Evora Global.”

UBS	<u>Managing the Fund's mandates in line with its policies</u> *In its response UBS confirm that they "have reviewed the Voting & Engagement Policy and Statement of Investment Principles. It should be noted that this is not all directly relevant given the scheme invests in our pooled real estate fund, Triton Property Fund LP, and much of the policy and SIP focus on traditional asset classes, such as equity. That being said, sustainability and consideration of ESG related-risks is a key component of our investment process as evidenced by the Fund's 1st placed ranking in its GRESB peer group for the second consecutive year."*
UBS	<u>Assessment of ESG-related risks</u> We have a well-established approach to assessing ESG risks. UBS' Real Estate and Private Markets (REPM) Sustainability Workgroup was established to develop a responsible investment policy and identify and implement industry-leading strategies. The workgroup sets strategies and objectives at a global level and ensures our sustainability objectives are incorporated into all of our fund's investment strategies and property operations. The workgroup comprises professionals from several countries and disciplines including, engineering and construction, operations, research, asset management, fund management as well as business management and has regional representation from the following: United Kingdom, Switzerland, Continental Europe, Japan and the United States. We achieved a perfect 100% in Property in the 2018 UN PRI Assessment Report, demonstrating the strength of our responsible investment strategy. *"The REPM Sustainability Workgroup is involved at each stage of the asset management lifecycle. As such, climate change resilience and risk is considered in each of the following ways:* • *Investment Decisions (Acquisition and Disposition):* *We incorporate environmental, climate change and social risks into the evaluation criteria when making investment decisions at both an asset and fund level.* • *Development and Refurbishment (Engineering/Construction and Development):* *-We incorporate responsible investment, climate change and resilience strategies into the design and financial analysis of all new developments, property renovations and infrastructure projects.*

	-We evaluate obtaining certifications applicable for each property type and location to expedite approval process and maximize occupancy, rental rate, tenant quality, occupier wellbeing and value. *-We engage with planners, developers and other external project partners and consultants to achieve objectives.* *-We implement energy saving devices/upgrades or improve operations of inefficient equipment.* • *Operations and Maintenance (Asset Management):* *-We define and implement best practice measures to improve energy efficiency, water conservation and waste management to promote sustainable practices, reduce operating expenses and increase asset values.* *-We evaluate green building certifications applicable for each investment type and location to enhance the investment's competitive position, maximize occupancy, rental rate, tenant quality, occupier wellbeing and value.* *-We monitor changes in regulations and laws in order to adopt and implement responsible investment strategies, collaborate with tenants, property managers and suppliers of services and materials to achieve objectives, measure energy consumption and monitor energy performance.* *-We ensure infrastructure assets have in place and are in compliance with all environmental and operational permits.* *-We monitor fund performance in GRESB and green building certification progress in fund investments for fund-of-fund products.*

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PROTECTION/CASH MANAGERS – PIMCO

PIMCO	<u>Managing the Fund's mandates in line with its policies</u> In its responses PIMCO stated: "We can confirm that we have read and considered the engagement policy and statement of investment principles. We also confirm that the Fund's mandates are managed in line with these policies."
PIMCO	<u>Assessment of ESG-related risks</u> PIMCO summarised its approach in the following terms: "We are constantly evolving and improving our ESG processes and capabilities. PIMCO's ESG Leadership provides business leadership for further developing the firm's ESG thinking and capabilities. The group sets objectives and evaluates strategic initiatives on a continuous basis throughout the year. Similar to the long-term orientation of PIMCO's investment process, the firm's ESG Leadership team establishes long-term strategic objectives which are not likely to change month-to-month or quarter-to-quarter." PIMCO outlined its key ESG milestones below: · **UN PRI score of A+**: We believe that the UNPRI is a leading force in the ESG conversation within the investment management industry. PIMCO signed on as a UNPRI signatory in 2011. · **Designed and implemented ESG evaluation capabilities** within our municipal bonds and securitized assets. · Additionally, we have **continued to grow our credit research team coverage** with respect to ESG factors. · **Launched new ESG dedicated products** in the including a Global Investment Grade Credit ESG commingled fund and municipal bond ESG solutions. · **Hired more ESG specialists,** including Samuel Mary, a climate expert and ESG integration analyst, and Gavin Power, our Chief of Sustainable Development and International Affairs. · **Grew our dedicated ESG AUM by over 50% to $10.5bn** as of May 2019. · **Updated our ESG Investment Policy Statement** to include our updated ESG integration and increased inclusion and diversity efforts.

	· **Launched 2018 ESG Annual Report**: Our second annual ESG Investing Report takes a closer, quantifiable look at our engagement with issuers, integration across broad fixed income sectors and commitment to developing solutions for our clients.	
PIMCO	Largest exposure to carbon risk, and why? In its response, PIMCO identified 4 issuers as having the biggest exposure to carbon risk within the portfolio: Innogy Finance, Duke Energy, South Eastern Power Networks, and Solvay Finance. Their commentaries, explaining how they assessed two of these issuers, are included below for information: "Innogy Finance is a Germany based utility with operations in renewables, regulated grid and supply. Innogy was spun-off by RWE in 2016, which holds a 76.8% ownership in Innogy. E.On will acquire Innogy and keep supply and grids. Following the creation of Innogy and the separation from RWE, we believe the carbon intensity of Innogy has improved strongly. The change in the ownership structure that was announced on March 11th, 2018 means that Innogy and E.On will no longer own any generation activities as the renewables activities of both companies will be handed to RWE." "Duke Energy has exposure to carbon risks via its generation activities. We view the company's CO2 reduction targets to 2020 and 2030 as supportive in the company's ability to manage carbon intensity and carbon risks and those targets together	Examples of investment 'engagement' PIMCO's objective of engagement is to influence change, improve returns and reduce risks for clients. PIMCO's engagement process is driven by three guiding principles: - *Think like a treasurer*: We seek to identify issuers which can benefit from engagement, then develop a set of core engagement objectives tailored to each issuer. - *Engage like a partner:* We do not take an activist investor approach, believing that successful bondholder engagement is based on collaboration, productive dialogue and mutual agreement on objectives. - *Hold to account as a lender:* Our engagement process measures progress against a pre-defined benchmark, which is customized by issuer. At the outset of the process, we determine appropriate remedies if underperformance is material and are willing to divest if necessary. Engagement typically will include a combination of ongoing inquiry and periodic dialogue with issuer management. Relevant engagement topics will differ from sector to sector

	with investments in generation with low-GHG intensity supports the company’s carbon intensity position on an absolute basis and also when compared to peers. The company furthermore benefits from its activities in transmission and distribution which account for ~38% of total assets, and by its activities in low and non-GHG-emitting power generation assets which also account for ~37% of the group’s total assets.”	and company to company. With respect to ongoing inquiry, a dedicated engagement analyst creates a questionnaire tailored to each issuer, which contains questions such as: - Is your company planning to issue green bonds in the coming year? - Are you mapping your revenues and business model to the UN’s Sustainable Development Goals? - Are matters of culture and conduct reviewed by the board? - Are you developing a framework for climate risk reporting and stress testing? PIMCO has a dedicated ESG Engagement Analyst, who is integrated into the broader PIMCO Credit Research Team. PIMCO’s proprietary Company Engagement Tracking (COMET) tool enables the ESG desk to systematically flag ESG risks and objectives for coverage analysts to raise in meetings with issuers. COMET is then used to document outcomes that reduce credit risk and effect positive change, while tracking progress over time. Specific milestones are used to measure progress on ESG engagement, with varying levels of concern (“criticality”) and engagement objectives.