

New Zealand Superannuation Fund

Q3 2021

The purpose of the **reo**[®] (responsible engagement overlay) * service is to engage with companies held in portfolios with a view to promoting the adoption of better environmental, social and governance (ESG) practices. The **reo**[®] approach focuses on enhancing long-term investment performance by making companies more commercially successful through safer, cleaner, and more accountable operations that are better positioned to deal with ESG risks and opportunities.

Engagement in review

The latest report from the Intergovernmental Panel on Climate Change (IPCC) has served as a stark reminder of the need for urgent and bold action on climate change. The landmark study, which the UN Secretary General called “a code red for humanity”, warns that we are at imminent risk of hitting the internationally-agreed threshold of 1.5 degrees above pre-industrial levels in the near term. Unless rapid and deep reductions in carbon and other greenhouse gas emissions occur in the coming decades, achieving the goals of the Paris Agreement will be beyond reach.

We continue to dedicate significant resources to our engagement efforts on climate change, particularly through investor collaborations, pushing companies to pursue the most ambitious emissions reduction paths. We remain hopeful that deep cuts in emissions could help stabilise rising temperatures.

Finally, we would like to remind our readers that we have been and will continue to be part of the collective investor voice calling on governments to be visionary and ambitious in the way they approach the upcoming Glasgow COP26 negotiations. Strong action now is essential to set the world on a trajectory to a more stable climate and a healthier planet.

Setting best practice in managing physical climate risks

Investor collaboration

BMO Global Asset Management joined investors representing US\$10 trillion in assets to contact 50 highly-exposed companies in industries including food, consumer goods and transportation, setting out our expectations on the management of physical climate risks. This was accompanied by a new report published by the Institutional Investors Group on Climate Change (IIGCC), ‘Building Resilience to a Changing Climate’, which sets out investor views on best practice in this area.

The four key areas for action highlighted in this publication are:

- Establishing a climate governance framework which considers physical risks and opportunities alongside transition risk;
- Undertaking physical climate risk and opportunity assessments;
- Developing and implementing a strategy for building climate resilience; and
- Identifying and reporting against risk, opportunity and impact metrics to demonstrate progress over time

Decarbonising the steel industry

Investor collaboration

Steelmaking is highly relevant to the decarbonisation agenda, due to its dual role of supporting the low carbon transition and being an emissions-intensive sector. The uncertainty of low carbon technology development and the high capital cost to deploy them are two pertaining issues often mentioned by companies in the industry.

Recognising these challenges, the Institutional Investors Group on Climate Change gathered a group of investors, including BMO GAM, to develop a net zero steel strategy. In a dedicated publication, Global Sector Strategies: Investor interventions to accelerate net zero steel, the investor group highlighted several key measures that should be taken by the steel companies in the future, including investing in low emission steelmaking capacity that utilises green hydrogen and/or carbon capture and storage technology. On the other hand, the strategy also calls for systematic investor engagement on the steel value chain, for example to engage downstream customers on “green” steel purchasing, to accelerate technological advancement.

Engaging on ‘net zero’

In the run-up to COP26, we are continuing to focus our climate change engagement on the objective of achieving net zero global greenhouse gas emissions by 2050, in line with the goal of limiting the average temperature rise to 1.5 degrees Celsius.

We expect that the analysis of net zero alignment will support the deeper integration of climate risks and opportunities into investment portfolios, through the use of new data sets and analytical techniques. The emphasis on engagement coming out of the methodologies so far developed will add further impetus to investor stewardship, particularly beyond the Climate Action 100+ companies already under intensive focus. Whilst encouraging companies to take on a ‘net zero’ ambition is important, this alone has little value without a robust implementation strategy. A key framework here is the Climate Action 100+ Net Zero Company Benchmark, which sets out best practice expectations – including setting net zero-aligned short and medium-term targets; implementation of strategy; and governance oversight of climate actions.

Finally, efforts to address data gaps, including through our participation in the CDP’s annual Non-Disclosure Campaign should support better company disclosure, also building on progress made by the Task Force on Climate-related Financial Disclosures.

China's oil majors join forces to tackle methane emissions

Investor collaboration

Methane emissions are the second-largest cause of global warming today. These emissions, which have a significant warming potential, come from a range of anthropogenic and natural sources, including from the energy sector – mainly from oil, natural gas, coal and biofuel combustion. Emissions remain high as implementing abatement options quickly and at scale remains a challenge. While methane tends to receive less attention than carbon dioxide, reducing methane emissions will be critical to avoid the worst effects of climate change.

In this context, we welcome the **China Oil and Gas Enterprises Methane Emissions Control Alliance**, jointly initiated by oil & gas exploration and production majors **PetroChina**, **Sinopec** and **CNOOC**, with four other companies in the industry, including **China Resources Gas**, as its founding members. The Alliance will help support China's efforts to meet its 2060 carbon neutral target.

New agreement to protect garment workers in Bangladesh

Multi-stakeholder collaboration

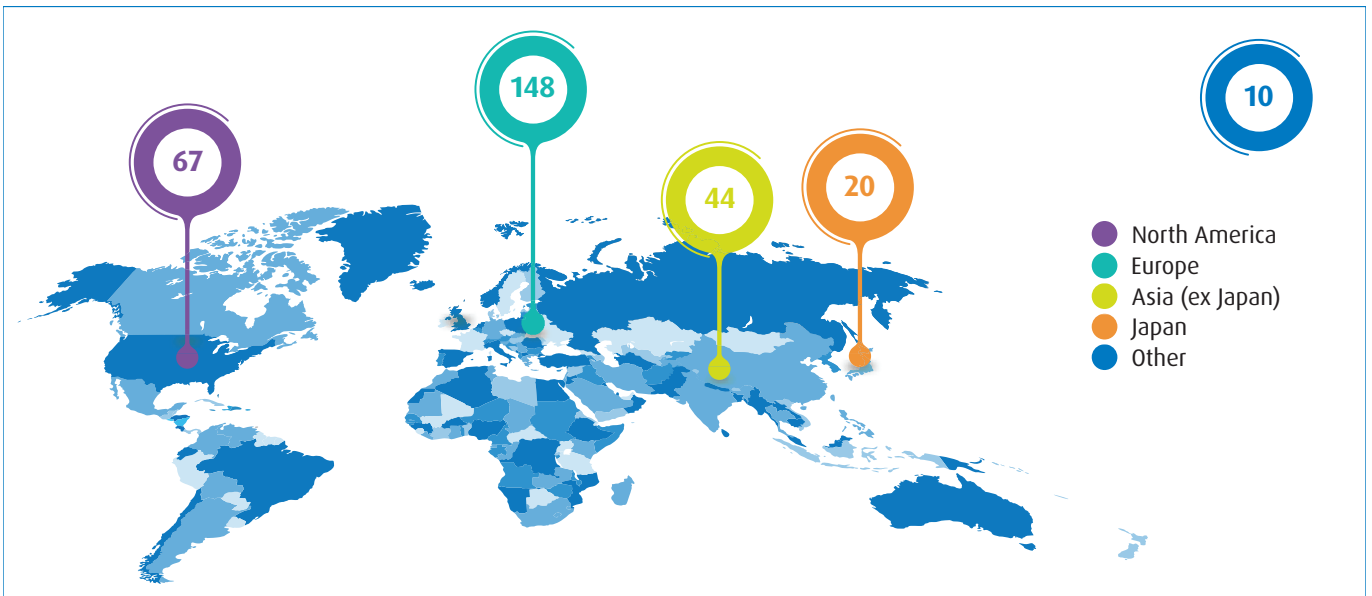
In August 2021, international brands, unions and the Bangladeshi garment industry came together to enact the **International Accord for Health and Safety in the Textile and Garment Industry** ("International Accord"). In the run up to the signing of this initiative, we wrote to nineteen companies that were signatories to the original **Bangladesh Accord on Fire and Building Safety** that was launched in 2013 right after the Rana Plaza factory collapse. We asked companies that they reaffirm their commitment to the Accord model.

The new agreement commits to focus on the health and safety program in Bangladesh, and to build a credible industry wide compliance and accountability mechanism. It also intends to extend the International Accord model to other regions, streamline the arbitration process that enforces the Accord's terms, and expand the scope of the agreement to address human rights due diligence.

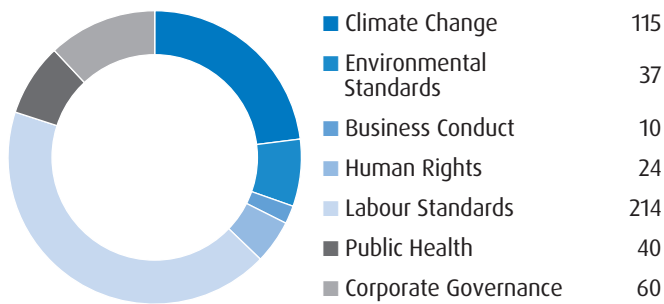
Companies engaged this quarter

Number of Engagements	Companies Engaged	Milestones achieved	Countries covered
394	289	82	30

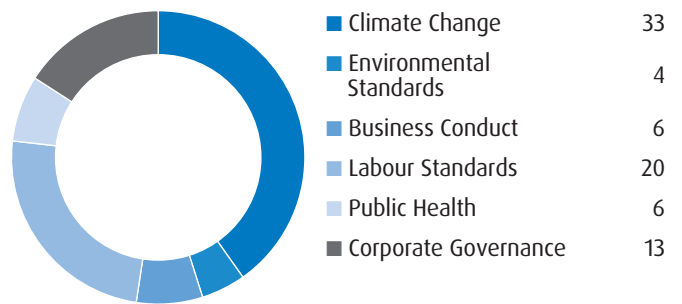
Companies engaged by region



Companies engaged by issue **



Milestones achieved by issue



* reo® is currently applied to €414.439bn / £355.671bn / US\$490.986bn* as at 30 June 2021.

** Companies may have been engaged on more than one issue.

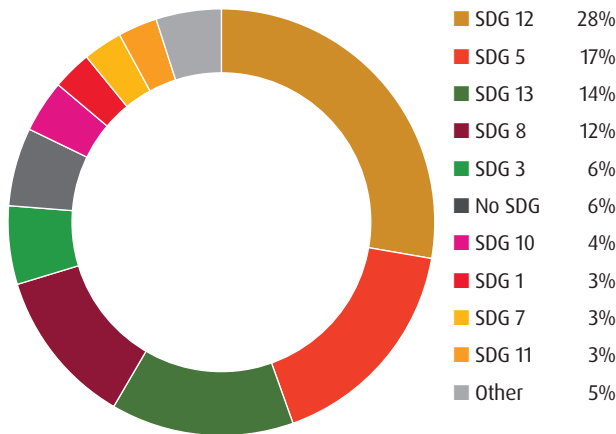
*** This report has been compiled using data supplied by a third-party electronic voting platform provider. The statistics exclude ballots with zero shares and re-registration meetings. Meetings/ballots/proposals are not considered voted if: ballots have been rejected by voting intermediaries (e.g. where necessary documentation (such as Powers of Attorney, beneficial owner confirmation, etc.) was not in place); instructed as "Do not vote" (e.g. in share-blocking markets); or left uninstructed. Past performance should not be seen as an indication of future performance. Stock market and currency movements mean the value of, and income from, investments in the Fund are not guaranteed. They can go down as well as up and you may not get back the amount you invest.

Engagements and Sustainable Development Goals (SDGs)

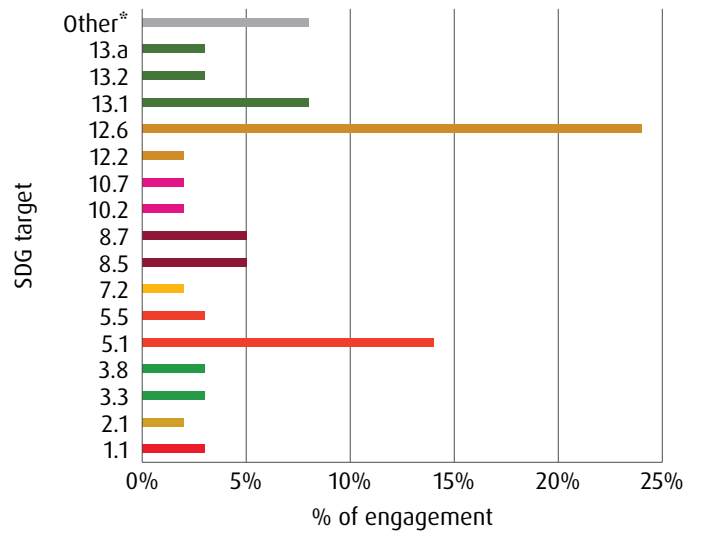
The 17 Sustainable Development Goals (SDGs) were developed by the UN and cross-industry stakeholders with a view to providing a roadmap towards a more sustainable world.

We use the detailed underlying SDG targets to frame company engagement objectives, where relevant, as well as to articulate the positive societal and environmental impacts of engagement. Engagements are systematically captured at a target level, to enable greater accuracy and achieve higher impact.

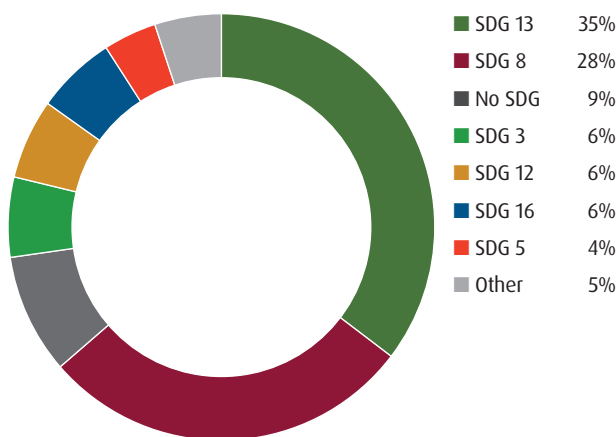
Engagement: SDG level



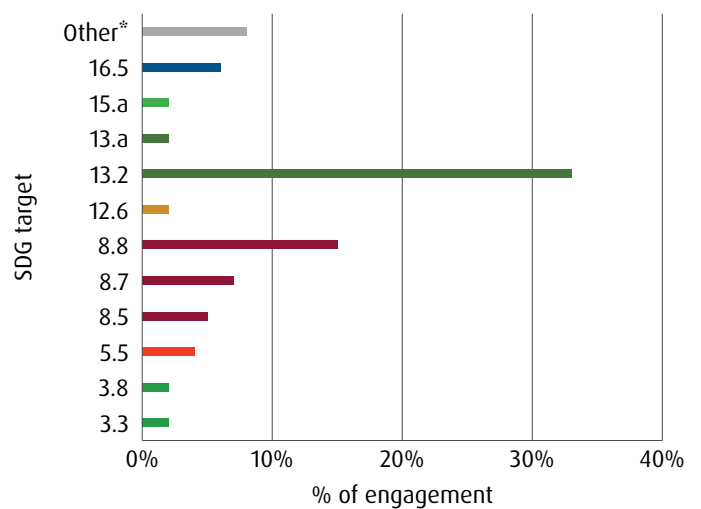
Engagement: SDG target level



Milestone: SDG level





Milestone: SDG target level



*Other represents SDG targets less than 2% of the relevant SDG Goal.

Engagement case studies

Company: Eli Lilly & Co	Country: United States	Sector: Health Care
Priority Company: ✓	ESG Risk Rating: 	Response to engagement: Good
Theme: Public Health	Issue: Access to Healthcare	
SDG:  3.8		

Background



Eli Lilly is one of the world’s largest pharmaceutical companies, with a market cap of c. USD 230 billion. In recent years we became increasingly concerned about the company’s approach to and disclosure on access to medicine, which we regard as a highly material issue for the pharmaceutical industry. Following the publication of the Access to Medicine Foundation’s 2018 Access to Medicine Index (ATMI), in which Eli Lilly ranked last, we resolved to ramp up our engagement with the company.

Action

We continue to recognise the value of engaging Eli Lilly both collaboratively and on a one-to-one basis. In November 2020, we participated in a collaborative call with other investors about access to medicine – among other issues – and were positively surprised by the participation of the newly appointed Head of ESG Strategy at Eli Lilly. We discussed the company’s approach to expanding access to insulin against the backdrop of the pandemic, including the introduction of the Lilly Insulin Value Program in April 2020, enabling people in the U.S. – regardless of their insurance status – to fill their monthly prescription of insulin for only \$35. We took this opportunity to encourage the company to disclose metrics to facilitate analysis of the company’s access to medicine initiatives. Subsequent to this joint investor call, we had a one-to-one meeting with the Head of ESG Strategy. We commended the company’s efforts to address insulin access and affordability, but expressed our concern about its poor performance in the ATMI, and highlighted the reputational risks of failing to be transparent about access to medicine initiatives. In our most recent meeting with the company, we were informed that Eli Lilly is seriously considering participating in the data collection process for the next ATMI, which would help to bolster its credibility.

Verdict

The appointment of a Head of ESG Strategy has undoubtedly resulted in positive change at Eli Lilly from an access to medicine perspective. The company has already improved its reporting on not only access to medicine but also other material ESG issues, and we are hopeful that this increased willingness to be transparent will translate into an enhanced reputation and a higher ranking in the next ATMI. Moreover, Eli Lilly can more clearly demonstrate its alignment with Sustainable Development Goal (SDG) 3 – Good health and well-being – by continuing to strengthen its access to medicine initiatives.

ESG Risk Rating: Rating of a company’s ESG risk exposure and risk management compared to industry peers. Source: MSCI ESG Research Inc.
 Top quartile:  GREEN Second quartile:  YELLOW Third quartile:  ORANGE Bottom quartile:  RED

Engagement case studies

Company: Mondelez International Inc

Country: United States

Sector: Consumer Staples

Priority Company: ✓

ESG Risk Rating: 

Response to engagement: Good

Theme: Environmental Stewardship

Issue: Pollution Impacts, Natural Resources – Biodiversity, Oceans

SDG:  14.1

Background

Plastic waste is a serious environmental issue and part of pollution that is a key driver of biodiversity loss. Lots of plastic is ending up in the ocean, which we have previously written about. Snacks companies are heavy users of plastic packaging, which contributes to increasing volumes of waste which either cannot or is not recycled due to lack of infrastructure or to consumer behaviour. As one of the world's biggest snack manufacturers, Mondelez is intimately linked to this issue.

Action

We first engaged with the company in 2018 on implementation of its net-zero waste packaging vision, including targets of eliminating 65,000 metrics tonnes of packaging by 2020 and making all packaging recyclable by 2025. In 2019, it had already reached 93% recyclable packaging. We commended the progress and urged the company to further its work on facilitating recycling infrastructure to support consumers in the quest to close the loop on packaging. In 2020, our dialogue focused on the packaging strategy's three pillars: minimise use and include recycled materials, support development of recycling infrastructure, and collaborate with value chain partners. We were encouraged to see the company cement its commitments by joining the New Plastics Economy Global Commitment and Initiative and to set targets for reducing the use of virgin plastic by 5% by 2025. During engagements in 2021, Mondelez explained it is driving increased recycling rates in key sales markets, for example through its commitment to the Plastics Pacts Network.

Verdict

During our engagement, we have seen Mondelez make strong commitments and develop a robust approach to reducing plastic waste. Its active engagement in the value chain by participating in forums like the New Plastics Economy and the Consumer Goods Forum and the recently announced membership in AMERIPEN, a coalition of packaging value chain companies centred around a material neutral policy with a vision to driving a circular economy, drives home this point. We will maintain engagement to follow how the strategy plays out in terms closing the loop by capturing plastic and redirecting it back into the economy.

ESG Risk Rating: Rating of a company's ESG risk exposure and risk management compared to industry peers. Source: MSCI ESG Research Inc.

Top quartile:  GREEN Second quartile:  YELLOW Third quartile:  ORANGE Bottom quartile:  RED

Engagement case studies

Company: China Resources Gas Group Ltd

Country: Hong Kong

Sector: Utilities


Priority Company: -

ESG Risk Rating: 

Response to engagement: Poor

Theme: Climate Change

Issue: Emissions management

SDG:  13.2

Background

As the largest natural gas distributor in China, China Resources Gas (“CRG”) serves over 40 million industrial, commercial and residential customers across the country with a total connectable population of close to 300 million. Such scale makes CRG a key player in the government’s drive to decarbonise the coal-dominant energy sector. While there are questions around the role of natural gas as a transition or ‘bridge’ fuel, China’s policy framework will likely become more supportive for gas in power, as the government looks to meet its goal of peaking emissions by 2030 and achieving carbon neutrality by 2060, and the rising needs of power system flexibility driven by renewables integration. We have had concerns over the company’s limited approach to managing greenhouse gas (GHG) emissions, methane emissions in particular. Methane, a potent greenhouse gas, can escape to the atmosphere from cracks on gas pipelines and constitute a significant contributor to climate change.

Action

For the past two years we have tried to establish a dialogue on climate change management with the company. CRG has not responded to our repeated engagement efforts; however, this has not prevented us from consistently sharing views and recommendations on our expectations regarding effective greenhouse gas emissions management. We have encouraged the company to take more decisive action to improve its capacity to identify, measure and reduce methane emissions across its pipeline and storage network. We also called for greater transparency of methane leakage figures as well as detection and remedial efforts, and for collaboration with peers to address this issue at a wider industry level. Finally, we have asked CRG to set and disclose a GHG emissions reduction target that is aligned with China’s peak emissions and carbon neutrality pledges.

Verdict

While the company has not answered to our calls for engagement, we have seen in the past year notable changes in line with what we have been asking for the past two years. The launch of the China Oil and Gas Methane Alliance, to which CRG is a founding member, signals an appetite from management to incorporate methane emissions controls into GHG emissions reduction plans. Importantly, the company has committed to set a number of environmental KPIs, including an emissions reduction target. Going forward, we will continue to write to CRG with further recommendations for improvement, including setting a more robust climate governance framework, making sure GHG targets are based on science, and reporting in line with TCFD recommendations.

ESG Risk Rating: Rating of a company’s ESG risk exposure and risk management compared to industry peers. Source: MSCI ESG Research Inc.

Top quartile:  GREEN Second quartile:  YELLOW Third quartile:  ORANGE Bottom quartile:  RED

Appendix



SDG	Target	Target Summary
SDG1	1.1	Eradicate poverty and ensure a living wage for all
SDG2	2.1	End hunger and ensure access to safe and nutritious food
SDG3	3.1	Substantially reduce maternity mortality rates
SDG3	3.3	End AIDS, TB, malaria and other water-borne and communicable diseases
SDG3	3.8	Access to medicines and health-care
SDG3	3.9	Reduce deaths and illnesses from pollution and contamination
SDG5	5.1	End all forms of discrimination against women and girls
SDG5	5.2	Eliminate all forms of violence against women
SDG5	5.5	Ensure full equality of opportunity for women, including at leadership levels
SDG6	6.3	Improve water quality by reducing pollution
SDG7	7.2	Substantially increase the global share of renewable energy
SDG7	7.3	Double the global rate of improvement in energy efficiency
SDG8	8.2	Achieve greater productivity through innovation.
SDG8	8.5	Achieve full and productive employment for all
SDG8	8.6	Reduce the proportion of youth not in employment or education
SDG8	8.7	Eradicate forced labour, modern slavery & human trafficking
SDG8	8.8	Protect and promote safe working environments for all workers
SDG8	8.10	Increase access to finance
SDG9	9.4	Upgrade and retrofit industries to increase sustainability
SDG10	10.2	Empower and promote inclusivity for all
SDG10	10.4	Adopt policies to progressively achieve greater equality
SDG10	10.7	Facilitate safe migration through managed policies
SDG11	11.1	Ensure universal access to safe and affordable housing
SDG11	11.5	Reduce social and economic losses caused by disasters
SDG11	11.6	Reduce the negative environmental externalities of cities
SDG12	12.2	Sustainably manage and make efficient use of natural resources
SDG12	12.4	Manage chemical usage and waste throughout their life cycle
SDG12	12.5	Reduce waste through prevention, reduction, recycling and reuse
SDG12	12.6	Encourage companies to adopt sustainable practices and enhance ESG reporting
SDG12	12.c	Removal of market distortions such as fossil-fuel subsidies
SDG13	13.1	Strengthen adaptive capacity to climate-related events
SDG13	13.2	Integrate climate change plans into policies and strategies
SDG13	13.a	Address climate change mitigation for developing countries
SDG15	15.1	Ensure sustainable usage of terrestrial freshwater ecosystems

Appendix (continued)



SDG	Target	Target Summary
■ SDG15	15.2	Promote the implementation of sustainable management of forests
■ SDG15	15.5	Take urgent action to reduce degradation of natural habitats
■ SDG15	15.a	Increase financial resources to conserve ecosystems
■ SDG15	15.b	Mobilise resources to finance sustainable forest management
■ SDG16	16.5	Reduce corruption and bribery in all their forms
■ SDG16	16.b	Promote non-discrimination laws for sustainable development