

# New Zealand Superannuation Fund

## Q3 2019

The purpose of the **reo**<sup>®</sup> (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**<sup>®</sup> 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

Alongside the effects of the U.S.-China trade war, tensions in the Persian Gulf, the Hong Kong protests and a generally tumultuous political landscape across the world, climate change-related news also had a strong showing in world news this quarter as millions of young people took to the streets worldwide in the biggest climate strike in history ahead of the UN Climate Action Summit in New York. At the same time, the private sector announced several actions that suggest companies have become aware of the need to work collaboratively: 87 major global companies pledged to reduce emissions and align their businesses with a 1.5°C future.

#### Climate Action 100+ inaugural progress report

*Engagement*

2019 marks the second year of the Climate Action 100+ Initiative (CA100+).

BMO GAM is leading and actively supporting 23 company engagements in this initiative. Two of the BMO-led companies were featured in the progress report – Volkswagen and General Motors (GM). The results of our collaborative engagements included the “carbon neutral” commitment by Volkswagen in early 2019, and the shareholder resolution at GM asking for lobbying disclosure in May 2019.

The past quarter saw 27 engagements by us with these CA100+ companies, covering Australia, Europe, US, China and Thailand. Significantly, we got to meet China Shenhua and Thailand’s national oil company PTT. In terms of outcomes of our engagement, we can highlight the “net zero emissions” 2050 commitment announced by Duke Energy, a US utilities BMO is actively involved in within CA100+, and BHP’s commitment to set a medium-term “Science-Based Target” to align to the goals of the Paris Agreement.

#### Minerals Council of Australia – shifting gears?

*Public policy*

We joined a group of investors to meet the CEO of the Minerals Council of Australia (MCA). We discussed growing concerns about the Council’s lobbying position with regards to climate change in Australian energy policy.

MCA briefed us on its new climate change position, which now features explicit support for the Paris Agreement. MCA is also drafting a climate change strategy, which will include the promotion of specific abatement technologies relevant to the sector and its downstream value chain, for example Carbon Capture and Storage.

We will continue our engagement with MCA to better understand whether its upcoming climate change strategy would meaningfully decarbonise the sector in Australia.

#### Deforestation and the Amazon fires

*Engagement*

We asked some of Europe’s largest banks to update and strengthen their lending and underwriting policies and guidelines for palm oil, soy, timber, and cattle, and to have overall anti-deforestation commitments. As part of our sustainable banking in ASEAN engagement project, we asked banks to enhance their sustainability criteria when lending to the palm oil sector and have no-deforestation commitments in place. We also directly engaged palm oil producers on their no-deforestation commitments, as well as companies sourcing commodities such as soy, sugar, palm oil and rubber on their approach to ensuring transparent and traceable agricultural supply chains.

We signed the PRI investor expectation statement on deforestation and forest fires in the Amazon, asking companies to commit to eliminating deforestation within their operations and supply chains.

We signed the Cerrado Manifesto - Statement of support to encourage producers to halt deforestation in Brazil’s Cerrado biome, a biodiversity hotspot covering approximately 20% of Brazil.

Finally, we joined the SPOTT (Sustainability Policy Transparency Toolkit) supporter network, asking for more transparency in commodity supply chains with the aim to avoid further deforestation.

#### US Governance

*Shareholder primacy and proxy advisers under attack in the US*

We attended the fall conference of the US Council of Institutional Investors (CII) where we contributed to the priorities setting.

Two announcements dominated discussions. Firstly, the Business Roundtable, whose membership comprises CEOs of the largest US companies, declared that their mantra that companies’ main purpose was to maximise shareholder value would be replaced with a commitment to all stakeholders.

In addition, the SEC released a troubling update in which it provided guidance on proxy advisers to re-classify their research as a form of solicitation, significantly increasing the regulatory burden and compliance risk to produce their research. Given the critical role that proxy advisers play in enabling investors to implement their stewardship responsibilities, making their work harder and riskier was generally not welcomed.

*US investors look to strengthen governance standards despite market headwinds*

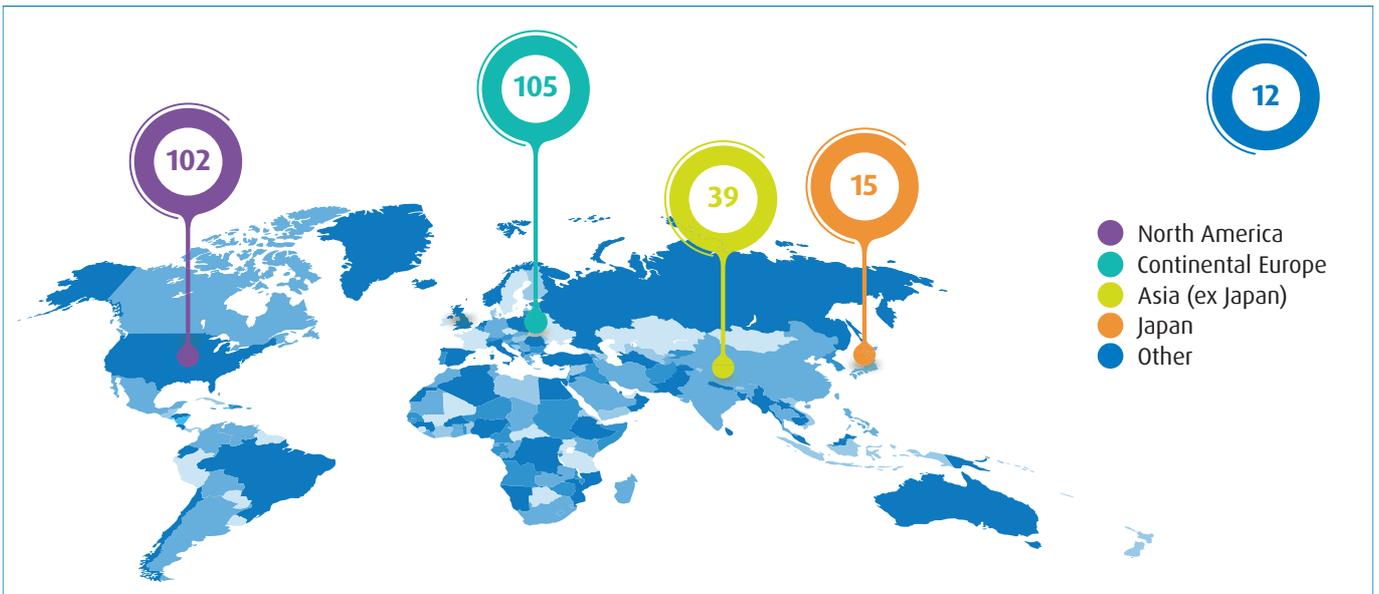
We attended the inaugural conference of the Investor Stewardship Group (ISG), comprised of over 60 US and international institutional investors with more than \$31 trillion in assets. The aim of the group is to establish and promote a framework of basic standards of investment stewardship and corporate governance for investors and companies, respectively.

We have been encouraged to see this initiative grow in both size, purpose and relevance over the last year, particularly in the current U.S. environment where other market stakeholders are working to suppress investors pushing for governance reform.

Companies engaged this quarter

Companies Engaged	Milestones achieved	Countries covered
273	72	30

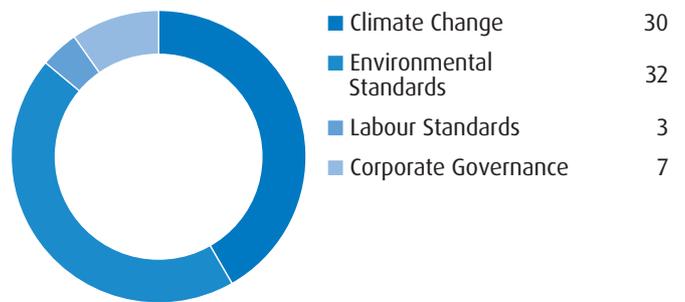
Companies engaged by region



Companies engaged by issue \*\*



Milestones achieved by issue



\* *reo*® is currently applied to £128bn (\$163billion / €143billion) of assets as at 30th June 2019.

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

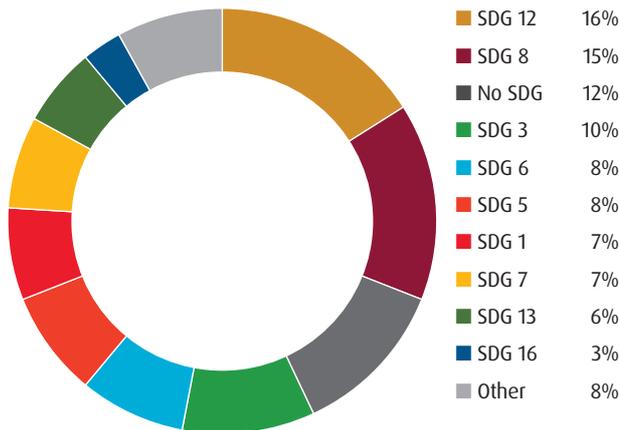
\*\*\* This report has been compiled using data supplied by a third-party electronic voting platform provider. The statistics exclude ballots with zero shares and re-registration meetings. Meetings/ballots/proposals are not considered voted if: ballots have been rejected by voting intermediaries (e.g. 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. This document is for professional advisors only and should not be circulated to other investors. 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)

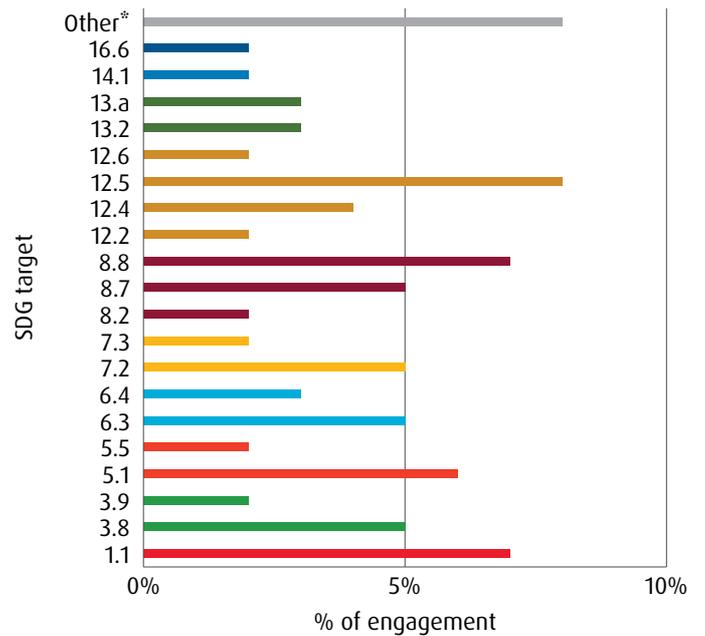
The 17 Sustainable Development Goals (SDGs) were developed by the UN and cross-industry stakeholders with a view to providing a roadmap towards a more sustainable world.

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.

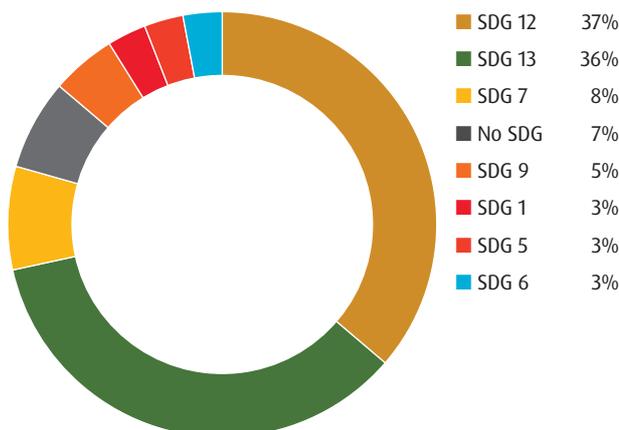
Engagement: SDG level



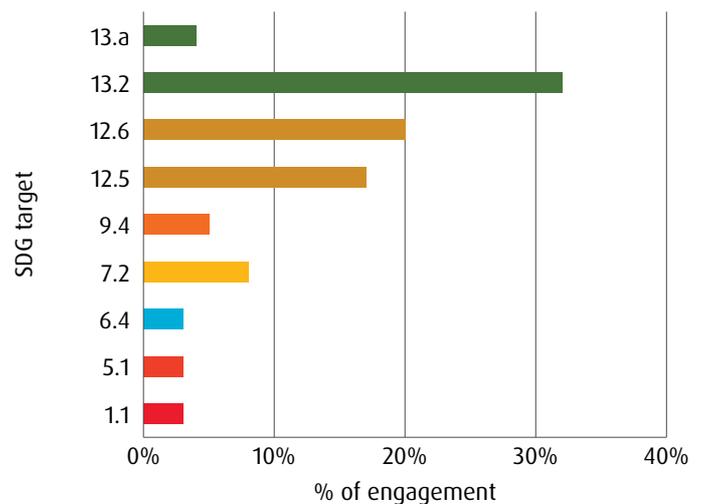
Engagement: SDG target level



Milestone: SDG level



Milestone: SDG target level



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

## Engagement case studies

Company: Duke Energy Corp

Country: United States

Sector: Utilities

Priority Company: 4

ESG Risk Rating: 

Response to engagement: Good

Theme: Environmental Standards

Issue: Climate Action 100+ engagement meeting

SDG:



13.2



7.2

### Background

Duke Energy is one of the largest electric utilities in the US, with over 53MW of installed capacity, just under one-third of which is currently coal. Its total CO2 emissions from electricity generation were over 100 million tons, although these emissions have reduced significantly over recent years resulting from a series of coal plant retirements. BMO has engaged both one-on-one and through the Climate Action 100+ initiative - following investor pressure, the company was the first US utility to publish a climate scenario analysis. Following this, engagement has focused on urging it to set a future decarbonisation trajectory.

### Action

In September we had a collaborative Climate Action 100+ call, which on the Duke Energy side included both senior executives and operational specialists. This took place just a few days after the company announced its 2050 net zero carbon target, alongside a 50% by 2030 emissions reduction target. The investor group warmly welcomed the company's ambition. One key question discussed was the trajectory between now and 2050, with some investor views that the new 2030 goal was not sufficiently ambitious. Additionally, the company told us that there would be no changes to existing capex plans over the next 5 years resulting from the announcement - although it was keen to emphasise that its capex already incorporates significant renewables investments. We asked about future coal retirements, with Duke indicating it might consider giving more clarity through its reporting; and were encouraged that the company gave a detailed response on how it is considering the social and community aspects of power plant closures. We also asked whether success against the new targets would be linked to executive remuneration. The company told us they are open to this in principle but have struggled to find appropriate metrics. Finally, we spoke about lobbying expectations and the recent letter sent to US companies by an investor collaboration that includes BMO. Duke promised a response to the letter by November.

### Verdict

In contrast with the previous call at the end of 2018, the tone of this call was far less formal and defensive, and the company seemed open to discussing some of the more challenging issues. The net zero carbon target is undoubtedly ambitious, and currently only matched in the US market by Xcel Energy, which has also set a net zero 2050 goal. Whilst absolutely welcoming the announcement, we recognise that implementation is critical with all such commitments. We will continue to speak to Duke Energy about their definition of net zero and the planned scale of offsets, as well as the trajectory of action, discouraging backloading too much to the later part of the time period. We will also continue to press for coal phase-out by 2030, whilst recognising the need to take account of the social consequences.

**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
SDG1	1.4	Ensure equal rights to resources and basic services
SDG2	2.1	End hunger and ensure access to safe and nutritious food
SDG2	2.3	Double agricultural productivity of small-scale food producers
SDG2	2.4	Implement climate-resilient and sustainable food production
SDG3	3.3	End AIDS, TB, malaria and other water-borne and communicable diseases
SDG3	3.4	Reduce mortality from non-communicable diseases and promote mental health
SDG3	3.6	Halve deaths and injuries from road traffic accidents
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	5.5	Ensure full equality of opportunity for women, including at leadership levels
SDG6	6.1	Achieve universal access to safe & affordable drinking water
SDG6	6.3	Improve water quality by reducing pollution
SDG6	6.4	Increase water-use efficiency to address water scarcity
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	8.3	Promote development-oriented policies
SDG8	8.4	Improve resource efficiency and prevent environmental degradation
SDG8	8.5	Achieve full and productive employment for all
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	9.1	Develop resilient and sustainable infrastructure
SDG9	9.4	Upgrade and retrofit industries to increase sustainability
SDG10	10.2	Empower and promote inclusivity for all
SDG10	10.5	Improve the regulation and monitoring of financial markets
SDG11	11.2	Provide access to safe and affordable transport systems
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	12.3	Halve global food waste at the production and consumer level.
SDG12	12.4	Manage chemical usage and waste throughout their life cycle

## Appendix (continued)



SDG	Target	Target Summary
■ SDG12	12.5	Reduce waste through prevention, reduction, recycling and reuse
■ SDG12	12.6	Encourage companies to adopt sustainable practices and enhance ESG reporting
■ SDG13	13.2	Integrate climate change plans into policies and strategies
■ SDG13	13.a	Address climate change mitigation for developing countries
■ SDG14	14.1	Prevent and reduce marine pollution of all kinds
■ SDG15	15.1	Ensure sustainable usage of terrestrial freshwater ecosystems
■ 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
■ SDG16	16.5	Reduce corruption and bribery in all their forms
■ SDG16	16.6	Develop effective, accountable and transparent institutions
■ SDG16	16.10.	Ensure public access to information and protect fundamental freedoms