A4S
ASSET OWNERS
NETWORK

PUTTING IN PLACE TCFD METRICS

Practical example: HSBC Bank (UK) Pension Scheme

THE PRINCE OF WALES'S
CHARITABLE FUND

INTRODUCTION

HSBC Bank (UK) Pension Scheme manages two schemes: a defined benefit scheme with 97,000 members and assets under management of £30.7 billion, and a defined contribution scheme with 90,000 members and assets under management of £4.9 billion.

In order to understand better how exposed our portfolios are to carbon-intensive companies, we started using the weighted average carbon intensity (WACI) metric for our invested defined benefit (DB) and defined contribution (DC) assets. We have disclosed this metric and subsequent data in our TCFD statements since the 2017 financial year. As data has become more available over time, we have covered more assets in this calculation.

WACI is a backward-looking metric, so we wanted to balance it with a metric that is forward-looking. So in 2020, we commissioned a second metric: **The Transition Pathway Initiatives' management quality score** (TPI MQ). TPI MQ gives us insight into how well our investee companies are planning to manage both their greenhouse gas emissions and the risks and opportunities arising from transitioning to a low-carbon economy. We can then benchmark companies' carbon emissions against international targets and national pledges made as part of the Paris Agreement. We will include the TPI MQ metric in our TCFD statement for the 2021 financial year.

Together, WACI and TPI MQ give us valuable insight into the climate risk of our investments.

HOW

Developing and calculating the metrics:

Having researched the options, we then worked closely with external advisers to develop our metrics. We use regular investment consultant advisers for both our DB and DC assets, giving us a broad range of expert input. To give us confidence that we are using good-quality, unbiased data, an independent data provider calculates the metrics.

Getting the metrics approved:

Our metrics are part of an overarching climate risk management framework and we needed to get use of both metrics approved. We have a two-step process: our Assets and Liability Committee (ALCO) review and approve metrics, and endorse the overall framework which is sent to the full trustee board for final approval. To equip decision makers with the right information, we facilitated training for ALCO, and then later for the wider board, on our proposed metrics and why we had chosen these over the alternatives. Our investment consultant provided the training through videos, supplemented by written materials, to make the content accessible.

Using the metrics:

We use our metrics as a risk management tool and a way to understand how asset managers are managing our portfolios. Metrics are currently imperfect and the data used to produce them are partial in coverage and constantly evolving, so we prefer to treat metrics as sources of information about risk – rather than as a standard that all assets must meet. This becomes a starting point for fruitful conversations with asset managers about climate-related risk management and climate risk policies. Through this engagement, we can push for changes that can better support the shift to a low-carbon economy and ensure our beneficiaries' investments remain resilient to this transition.

Example: using metrics to engage with asset managers

If we were to calculate the WACI metric for a fixed income portfolio that, hypothetically, includes oil company bonds that mature in 2030, the result would tend to be higher than if it did not include these bonds. That's useful information, and we would want to ask the asset manager why they had invested in those assets so we could understand the thinking behind it. Analysing the portfolio using WACI would give us greater and more granular insight into the carbon implications and our risk, and so our conversation with the asset manager would become more precise. The Trustees prefer an active engagement - rather than exclusion - approach. Consequently, any assets that possess a high WACI score does not automatically warrant the need to sell such an asset.

DISCLOSURE

Excerpt from our 2020 Taskforce on Climate-related Financial Disclosures (TCFD) Statement, showing the calculations made using the WACI metric for the main equity exposures of both the DB and DC assets of the scheme as at 31 December 2019.

DB	31/12/2019				31/12/2018				31/12/2017			
	FUM £m	Carbon Emissions Intensity (Weighted Average Carbon Intensity – Scope 1 & 2) – tonnes CO_2e/mUSD revenue			FUM £M	Carbon Emissions Intensity (Weighted Average Carbon Intensity – Scope 1 & 2) – tonnes CO_2e/mUSD revenue			FUM £M	Carbon Emissions Intensity (Weighted Average Carbon Intensity – Scope 1 & 2) – tonnes CO_2e/mUSD revenue		
		Fund	Bmk	Diff		Fund	Bmk	Diff		Fund	Bmk	Diff
Global Equities	**Fund no longer in portfolio**				1,969	209	297	-30%	2,245	185	296	-38%
Sterling Corporate Bonds - active	**1,477**	**291**	-	-								
BlackRock Investment Management (UK) Limited	841	287	-	-								
M&G Investments	636	297	-	-								
Global Bonds - active	**5,973**	**228**										
AXA Investment Managers	2,714	212	-	-								
BlackRock Investment Management (UK) Limited	1,399	199	180	11%	Not previously analysed				Not previously analysed			
Legal & General Investment Management	618	63	-	-								
Loomis, Sayles & Company	1,242	376	-	-								
Liquid Matching Assets (dollar)* - active	**1,182**	**543**										
Insight Investments	1,182	543	-	-								
Illiquid Matching Assets - active	**552**	**1,428**										

Source: 2020 Taskforce on Climate-related Financial Disclosures Statement, HSBC

DC	31/12/2019				31/12/2018				31/12/2017			
	FUM £m	Carbon Emissions Intensity (Weighted Average Carbon Intensity – Scope 1 & 2) – tonnes CO_2e/mUSD revenue			FUM £M	Carbon Emissions Intensity (Weighted Average Carbon Intensity – Scope 1 & 2) – tonnes CO_2e/mUSD revenue			FUM £M	Carbon Emissions Intensity (Weighted Average Carbon Intensity – Scope 1 & 2) – tonnes CO_2e/mUSD revenue		
		Fund	Bmk	Diff		Fund	Bmk	Diff		Fund	Bmk	Diff
Global Equities - Passive	3,079	183	274	-33%	2,373	209	297	-30%	2,400	185	296	-38%
Global Equities - Active	401	112	172	-35%	383	154	214	-28%	433	301	489	-38%
Emerging Market Equities - Active	154	165	300	-45%	74	150	392	-62%	77	207	437	-53%
UK Equities - Active	89	68	123	-45%	72	175	138	+26%	83	194	152	+28%
Sustainable & Responsible Equities - Active	33	73	169	-57%	24	292	189	55%	27	233	544	-57%
Shariah Law Equities - Passive	43	72	222	-68%	24	72	72	0%	20	84	84	0%
UK Equities - Passive	24	121	123	-1%	17	138	138	0%	18	152	152	0%
North American Equities - Passive	22	175	175	0%	11	180	180	0%	Not previously analysed			
Asia (ex Japan) Equities - Passive	6	243	243	0%	3	238	238	0%				
Europe (ex UK) Equity - Passive	5	177	181	-2%	3	171	171	0%				
Japan Equities - Passive	3	104	104	0%	2	141	141	0%				

Source: 2020 Taskforce on Climate-related Financial Disclosures Statement, HSBC

This analysis is our starting point, and we gain greater insight into the carbon implications and risks as we analyse our funds further. For example, the Sustainability & Responsible Equities – Active Fund has shown a significant degree of variability in the calculated WACI figures year on year. There are many possible reasons behind the variability in figures which may include, but are not limited to, changes in underlying fund managers; changes in underlying investment positions; improvements in data coverage and accuracy; and/or allocations to transition leaders, in which the current WACI numbers may initially be high but the expected future improvement pathway is better eg construction companies with the most ambitious carbon reduction plans.

NEXT STEPS

Over the next few years, we will keep up with research findings and industry practice on existing and emerging metrics by being active members of platforms such as the Cambridge Institute for Sustainability Leadership, the UN's Principles for Responsible Investment (PRI) and Climate Action 100+. It's inevitable that we will start to see new metrics being developed. Where these are more useful than our current metrics, or work well alongside them, we will change our practice and adapt our disclosures.

Ultimately, we aim to have a dashboard of metrics. No single number can give us a full picture of our climate risks, but a carefully selected combination of metrics can offer a much more rounded view.

At the moment, because we have only two metrics and companies are only beginning to analyse scope 3 emissions, we haven't set specific targets. As industry practice and data quality evolves, though, we hope to develop targets that we can integrate into decision making – with the goal of building portfolios aligned with the Paris Agreement.

TOP TIPS

TRAIN DECISION MAKERS

Training trustees helps them to be informed decision makers. Our training described the proposed metrics and their methodology. We also presented alternative metrics, so trustees could see the advantages and disadvantages of different options.

UNDERSTAND YOUR METRICS

Learn how your metrics can be used, what they can tell you and the data you need to calculate them. Be aware of their limitations, too. This will help you clarify how best to include the metrics in your work – and where you should be cautious.

PLAN YOUR DISCLOSURES

Start planning your disclosures early based on the data you need, incorporating enough time to ask and receive data from different stakeholders so you can build them into your TCFD reports.

KEEP METRICS UNDER REVIEW

This area is changing rapidly, with research organizations developing new metrics and companies generating better data. Build in regular reviews to make sure that you stay up to date.

USE EXTERNAL ADVISERS

Talk to a range of people – including advisers and fund managers – so you can get new ideas and different perspectives. The more diverse your advisory team, the better your outcomes.

GET IN TOUCH OR FIND OUT MORE

@PrincesA4S

The Prince's Accounting for Sustainability Project (A4S)

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A4S ASSET OWNERS NETWORK

The A4S Asset Owners Network is a grouping of pension fund chairs and trustees to discuss integrating sustainability into investment decision making. Click here to find out more.