University of Reading Employees' Pension Fund –Annual Engagement Policy Implementation Statement

Introduction

This statement sets out how, and the extent to which, the Engagement Policy in the Statement of Investment Principles ('SIP') produced by the Trustees, has been followed during the year to 31 July 2022. This statement has been produced in accordance with The Pension Protection Fund (Pensionable Service) and Occupational Pension Schemes (Investment and Disclosure) (Amendment and Modification) Regulations 2018 and the guidance published by the Pensions Regulator.

Members should be aware that this Statement is part of a wider set of information available on the Fund's governance and investment responsibilities undertaken by the Trustees:

- Members can view the SIP (mentioned above) on the University's website which discloses, in detail, the investment principles, policies, objectives, and strategy followed.

- Members can request a copy of the Annual Report and Financial Statements of the Fund, which contains certain information on the management of the Fund, its governance, investment risks management and level of Trustees' knowledge and understanding.

Investment Objectives of the Fund

The Trustees believe it is important to consider the policies in place in the context of the investment objectives they have set. The objectives of the Fund included in the SIP are to invest the Fund's assets in the best interest of the members and other stakeholders and, in the case of a potential conflict of interest, in the sole interest of the members. Within this framework, the Trustees' primary aim is to ensure all benefits are paid when they fall due.

Over the longer term, the Trustees would like to adopt a 'self-sufficiency' approach whereby the Fund's assets are less risky and there is a reduced probability of a funding deficit opening up in the future. It is proposed the portfolio will be invested in a range of credit based asset classes, broadly designed to generate income to meet pension outgo as it falls due. The Trustees are comfortable that the strength of the covenant offered by the University means that they can take a degree of risk in the portfolio over the longer term.

Assessment of how the policies in the SIP have been followed for the year to 31 July 2022

The information provided in the following section highlights the work undertaken by the Trustees during the year, and longer term where relevant, and sets out how this work followed the Trustees' policies in the SIP.

The strategic benchmark has been determined using appropriate economic and financial assumptions from which expected risk/return profiles for different asset classes have been derived. These assumptions apply at a broad market level and are considered to implicitly reflect all financially material factors.

Policies in relation to the Fund's investment strategy, day-to-day management of the assets, and associated risks

Please refer to Sections 5, 6, 7, 10 and 11 of the SIP for the Fund's policies around its investment strategy, the day to day management of the assets, and the associated risks.

The Trustees reviewed the Fund's investment strategy over the year, considering the Fund's liability profile and requirements of the Statutory Funding Objective, their own appetite for risk (including financially material risks such as Environmental, Social and Governance risks, including climate change), the views of the University on investment strategy, the University's appetite for risk, and the strength of the University's covenant. The Trustees also received written advice from their Investment Adviser.

The basis of the Trustees' strategy for the Fund is to divide the Fund's assets between growth assets which consist of diversified growth funds, a high lease-to-value property fund and two secured finance funds, and matching assets, comprising of buy and maintain credit and index-linked gilts holding. The Trustees regard the basic distribution of the assets to be appropriate for the Fund's objectives and liability profile, and the funds in which the Fund invests are expected to provide an investment return commensurate with the level of risk being taken.

The Fund's investment consultant supplies the Trustees with the following on a quarterly basis for each of the Fund's investments:

- Investment returns and performance commentary;
- Updates and developments, if applicable, for each manager and fund;
- A Manager Research rating;
- An ESG rating.

The Trustees use Trustee meetings and Investment Sub Committee meetings to ask questions of the investment consultant, and will also invite managers to present directly to the Trustees from time to time.

The Trustees recognise risk (both investment and operational) from a number of perspectives in relation to the investments held within the Fund. As detailed in Section 5 of the SIP, the Trustees consider both quantitative and qualitative measures for these risks when deciding investment policies, strategic asset allocation, and the choice of fund managers.

As the Fund invests in pooled investment vehicles, the Trustees accept that they have no ability to specify the risk profile and return targets of the manager, but believe that appropriate mandates can be selected to align with the overall investment strategy.

The Trustees recognise the need to hold investment managers and advisers to account. Whilst the day-to-day management of the Fund's assets are delegated to the Investment Managers, all other investment decisions including strategic asset allocation and selection and monitoring of Investment Managers is based on advice received from the Investment Consultant. Mercer Limited has been appointed for this purpose.

In December 2019, the Trustees put in place investment objectives for its Investment Consultancy Provider, Mercer, and its performance will be reviewed on a regular basis. The objectives may be revised at any time but will be reviewed at least every three years, and after any significant change to the Fund's investment strategy and objectives. These were subsequently reviewed in October 2022.

The intention of these objectives is to ensure the Trustees are receiving the support and advice it needs to meet its investment objectives. The Consultancy Provider objectives set cover both short and long term objectives across strategy, monitoring, compliance and regulation, client servicing and relationship management and member engagement and communications.

Policy on ESG, Stewardship and Climate Change

The following work was undertaken during the year relating to the Trustees' policy on ESG factors, stewardship and climate change, and sets out how the Trustees' engagement and voting policies were followed and implemented during the year.

The Fund's SIP includes the Trustees' policy on Environmental, Social and Governance ('ESG') factors, stewardship and climate change. This policy sets out the Trustees' beliefs on ESG and climate change and the processes followed by the Trustees in relation to voting rights and stewardship. This was last reviewed in May 2021.

In order to establish these beliefs and produce this policy, the Trustees undertook investment training in April 2019 provided by their investment consultant on responsible investment which covered ESG factors, stewardship, climate change and ethical investing. Prior to this training, the Trustees undertook a beliefs survey designed by their investment consultant to assist them with establishing their policies in this area. The results of this survey were presented at the Trustees' meeting on 11 April 2019, when the training took place, with the policy being incorporated into the SIP following this exercise.

Since then, the Trustees have also received an ESG benchmarking report from their investment consultant, which sets out how the Fund's investments compare from an ESG perspective versus the wider universe of managers/funds that Mercer research within the relevant asset classes. The results of this ESG peer group analysis showed that all of the Fund's investment managers score higher than average when compared against the wider universe of managers within each asset class, from an ESG perspective.

The Trustees keep their policies under regular review, with the SIP subject to review at least triennially.

The Trustees believe that environmental, social, and corporate governance (ESG) factors may have a material impact on investment risk and return outcomes, and that good stewardship can create and preserve value for companies and markets as a whole. The Trustees also recognise that long-term sustainability issues, particularly climate change, present risks and opportunities that increasingly may require explicit consideration.

The Trustees have given appointed investment managers full discretion in evaluating ESG factors, including climate change considerations, and exercising voting rights and stewardship obligations attached to the investments, in accordance with their own corporate governance policies and current best practice, including the UK Corporate Governance Code and UK Stewardship Code. The Trustees will review the investment managers' policies and engagement activities (where applicable) on an annual basis.

The Trustees consider how ESG, climate change and stewardship is integrated within investment processes in appointing new investment managers and monitoring existing investment managers. Monitoring is undertaken on a regular basis by receiving updates from investment managers and by Mercer providing the Trustees with ESG ratings for the strategies in which the Fund invests.

The Trustees requested that the investment managers confirm compliance with the principles of the UK Stewardship Code 2020. All managers confirmed that they are signatories of the UK Stewardship Code 2020 that took effect on 1 January 2020, and the FRC has now published the list of confirmed 2020 Signatories after assessing the reporting by each applicant.

Legal and General Investment Management ("LGIM") believe that they have fully applied each of the principles in its investment stewardship activity during 2021, and they have submitted the 2021 Active Ownership Report to the FRC as its response to the UK 2020 Stewardship Code.

As noted earlier, the investment performance report is reviewed by the Trustees on a quarterly basis – this includes ratings (both general and specific ESG) from the investment consultant. All of the managers remained generally highly rated during the year. When implementing a new manager the Trustees consider the ESG rating of the manager. The investment performance report includes how each investment manager is delivering against their specific mandates.

Voting and Engagement Activity

The Trustees have delegated their voting rights to the investment managers, who are expected to provide voting summary reporting on a regular basis, at least annually. The reports are reviewed as part of the production of this statement.

When the investment managers present to the Trustees, the Trustees will ask the investment managers to highlight key voting activity and the impact on the portfolio.

The Trustees do not use the direct services of a proxy voter.

The Trustees also received details of relevant engagement activity for the year from each of the Fund's investment managers.

The Fund's investment managers engaged with companies over the year on a wide range of different issues including Environmental, Social and Governance factors. This included engaging with companies on climate change to ensure that companies were making progress in this area and better aligning themselves with the wider objectives on climate change in the economy (i.e. those linked to the Paris agreement). The Fund's managers provided examples of instances where they had engaged with companies they were invested in/about to invest in which resulted in a positive outcome. These engagement initiatives are driven mainly through regular engagement meetings with the companies that the managers invest in or by voting on key climate-related resolutions at companies' Annual General Meetings. The resolutions are often co-filed by a number of investors who indicate or not their support for the resolution to the company's management.

LGIM

LGIM note that they have established a fully integrated framework for responsible investing to strengthen long-term returns. Their framework for responsible investing is based on stewardship with impact and active research across asset classes. These activities enable LGIM to deliver responsible investment solutions to their clients and conduct engagement with the aim of driving positive change.

LGIM's core investment beliefs are as follows:

1. *"Responsibility: We have a responsibility to many stakeholders. When we allocate capital, we conduct extensive research into potential environmental and societal outcomes.*

2. *Financial materiality: We believe ESG factors are financially material. Responsible investing is essential to mitigate risks, unearth opportunities and strengthen long-term returns.*

3. *Positive outcomes: We strive to effect positive change in the companies and assets in which we invest, and for society as a whole."*

There are a number of LGIM employees with roles dedicated to ESG activity, with further colleagues whose roles involve a very substantial contribution to their responsible investing capabilities and whose objectives reflect this, although their responsibilities are broader than solely ESG.

A key pillar of LGIM's approach to index strategies is active ownership: encouraging companies to consider sustainability risks develop resilient strategies and consider their stakeholders. They also seek to tackle sustainability risks in some strategies on a product level using tools such as ESG scoring, 'tilting' and exclusions, via index construction or design.

In the face of challenges like climate change, ageing populations or technological disruption, LGIM believe a different approach to managing capital is required – where ESG impact is considered alongside the traditional metrics of risk and return.

In recognition of climate change and its defining issues, LGIM supports efforts to limit carbon emissions to net zero by 2050. Within their Climate Impact Pledge, they commit to helping companies reach this objective. They are also targeting zero net amount of emissions across all assets under management by 2050.

In 2021, LGIM expanded the LGIM ESG Academy in partnership with the United Nation's (UN) Principles for Responsible Investment (PRI), with the aim of providing education to all employees on how their job relates to and interacts with LGIM's purpose and activities as a responsible investor.

A summary of the voting activity undertaken by LGIM on behalf of the Trustees over the last 12 months is set out below. This in relation to the Fund's holdings within the Dynamic Diversified Fund.

Key votes undertaken over the year	
	Company: *Rio Tinto Plc* **Resolutions proposed:** *Approve Climate Action Plan* **LGIM vote:** *Against* **Background:** *"We recognise the considerable progress the company has made in strengthening its operational emissions reduction targets by 2030, together with the commitment for substantial capital allocation linked to the company's decarbonisation efforts. However, while we acknowledge the challenges around the accountability of scope 3 emissions and respective target setting process for this sector, we remain concerned with the absence of quantifiable targets for such a material component of the company's overall emissions profile, as well as the lack of commitment to an annual vote which would allow shareholders to monitor progress in a timely manner."* **Further comment from LGIM:** *"LGIM considers this vote significant as it is an escalation of our climate-related engagement activity and our public call for high quality and credible transition plans to be subject to a shareholder vote."*
Dynamic Diversified Fund Over the year to 30 June 2022, LGIM voted on 99.8% of resolutions put forward at 9,483 meetings. LGIM voted against management for c. 22% of the total resolutions.	**Company:** *Prologis Inc* **Resolutions proposed:** *Elect Director Hamid R. Moghadam* **LGIM vote:** *Against* **Background:** *"A vote against is applied as LGIM expects companies to separate the roles of Chair and CEO due to risk management and oversight. Independence: A vote against is applied as LGIM expects a board to be regularly refreshed in order to maintain an appropriate mix of independence, relevant skills, experience, tenure, and background."* **Further comment from LGIM:** *"LGIM considers this vote to be significant as it is in application of an escalation of our vote policy on the topic of the combination of the board chair and CEO (escalation of engagement by vote). LGIM has a longstanding policy advocating for the separation of the roles of CEO and board chair. These two roles are substantially different, requiring distinct skills and experiences. Since 2015 we have supported shareholder proposals seeking the appointment of independent board chairs, and since 2020 we have voted against all combined board chair/CEO roles."*

Key votes undertaken over the year	
	Company: *Canon Inc* **Resolutions proposed:** *Elect Director Mitarai, Fujio* **LGIM vote:** *Against* **Background:** *"A vote against is applied due to the lack of meaningful diversity on the board. A vote against is applied due to the lack of independent directors on the board. Independent directors bring an external perspective to the board. Bringing relevant and suitably diverse mix of skills and perspectives is critical to the quality of the board and the strategic direction of the company. We would like to see all companies have a third of the board comprising truly independent outside directors."* **Further comment from LGIM:** *"LGIM views gender diversity as a financially material issue for our clients, with implications for the assets we manage on their behalf."*

For the Fund's property mandate, one of LGIM's key initiatives to promote ESG integration includes producing an asset sustainability fund for each property under management coordinated with maintenance and refurbishment funds, in order to reduce greenhouse gas emissions. This is linked with the inclusion of sustainability-related performance indicators in employees' appraisal targets and property supplier contracts.

<u>Invesco</u>

Invesco's fundamental belief is that ESG investing is an essential part of the solution to a sustainable future. They view it as an important agent of change in driving a holistic perspective on the investment industry's role in creating value.

Invesco's purpose is to deliver an investment experience that helps people get more out of life. Sustainable value creation and effective risk mitigation are fundamental to achieving that goal. As a result, their focus is on integrating ESG into the heart of their investment process, with their investment teams taking decisions every day on how to manage this integration and how to use their leverage in important areas such as client engagement and proxy voting.

They also flex this work around more specific client needs, using skills such as their self-indexing capabilities to provide the right ESG solutions. Invesco's dedicated global ESG Team act as a center of excellence to guide, support and inform all of their work in this area.

The following wording in regards to the Global Targeted Returns Fund, is taken from the 2020 ESG paper for Invesco's Multi-Asset offerings.

'The Global Targeted Returns strategy has two targets – risk and return. These are financial targets, and as such, the strategy does not have a sustainability target that we are mandated to deliver against. However, ESG considerations are a key element of our investment analysis because some have been crucial for a long time and other considerations are growing in importance and relevance for asset prices.

Within the Multi Asset team we have always analysed factors that sit within the broad church of ESG, and over recent years we have formalised that analysis so that it is defined and illustratable to clients. Though ESG, from a philosophical standpoint, does not form the sole basis of an investment decision, their consideration is a component of our investment analysis and their relevance and importance differ from idea to idea.

The Invesco Global Targeted Returns strategy has a very defined and repeatable three-step risk-based portfolio management process, and ESG considerations play a role within each step. Within the first step of our investment process we analyse the risk and return of our macro-themed ideas. Within that analysis, we consider many factors that are ESG in nature. These can include major political or regime change, environmental concerns, trade negotiations, demographics and inequality to name a few.

In the second step of our investment process, scenario testing is at the core of our risk analysis. We use scenarios to review the impact on the portfolio of adding, removing and changing ideas. Several scenarios that we test the fund against are ESG risk factors, and these include natural disasters, social unrest and a reversal of wealth inequalities.'

With regards to their approach within Multi-Asset strategies, ESG is integrated through Central Economic Thesis (CET) within Invesco's monthly reviews, where many ESG considerations are discussed, which recently (as of Q2 2021) has included reviews of US politics, inflation, reform in Chile & Russia, trade tensions and many other elements.

Invesco's 3-step process in integrating ESG within Multi-Asset strategies can be summarised at a high level as follows:

Step 1. Ideas – each research note has a dedicated ESG considerations section

Step 2. Fund management process – Scenario testing (including two-degree climate scenarios)

Step 3. Implementation – Active ownership via proxy voting within segregated sleeves.

The Multi Asset team have also provided tailored ESG solutions for clients, with two strategies that have specific exclusions and/or ESG factors.

Invesco have a global ESG team of 13 people & dedicated resources, and engaged with 3000+ companies on ESG topics in 2021.

In 2021 Invesco voted on over 116,000 resolutions at 12,093 shareholder meetings, voting against management at least once at 58% of meetings.

A summary of the voting activity undertaken by Invesco on behalf of the Trustees over the last 12 months is set out below. This in relation to the Fund's holdings in the Global Targeted Returns Fund.

Key engagement activity undertaken over the year	
Diversified Growth Fund Over the year to 31 July 2022, Invesco engaged with 19 companies.	**Company:** *Larsen & Loubro Ltd* **Issuer Industry:** *Infrastructure* **Background:** *Invesco asked Larsen about both their historic involvement in the Indian nuclear weapons programme and the nature of their ongoing involvement. Due to government secrecy agreements, Larsen was limited in what they were able to disclose. However, they were able to confirm that they had absolutely no involvement in the manufacture of nuclear weapons or their launch systems, and that their involvement was limited to the building of submarines.* **Engagement Result:** *Based on the information obtained, Invesco determined that Larsen was not in violation of the Article 8 framework. On that basis, Invesco was not required to sell out of this position.*
	Company: *BHP Group Ltd* **Issuer Industry:** *Materials* **Background:** *The climate transition action plan represents a step forward for BHP and sets targets for reducing part of its scope 3 emissions profile. However, the plan has drawn scrutiny for excluding downstream emissions associated with steelmaking from these targets. While these are a substantial portion on BHP's scope 3 emissions, there are significant challenges with setting firm targets in this area due to uncertainties regarding how to achieve decarbonisation of these activities. Challenges notwithstanding, the plan is strong relative to its major peers.* **Engagement Result:** *Invesco is broadly supportive of BHP's transition plan at this point in time. Support was not considered warranted for a shareholder proposal requesting extensive disclosure of lifetime production guidance for company assets among other items. Going forward, we will monitor progress against the transition plan's targets and the initiatives the company is taking to mitigate downstream emissions.*

Key engagement activity undertaken over the year	
	Company: *Samsung Electronics Co Ltd* **Issuer Industry:** *Technology* **Background:** *The IR team walked Invesco through their potential candidates for director positions with the upcoming AGM approaching. This took up a majority of the call, leaving little time for ESG questions. When asked about issues relating to environmental sustainability, Invesco was directed to their yet to be released environmental policy. They did not provide any details surrounding targets as it would be seen in the policy.* **Engagement Result:** *Invesco asked for a follow up meeting once the environmental policy has been released to evaluate the ambitiousness of the standards.*

Blackrock

As an investor in fixed income, it is important to note that there is more limited scope for engagement (relative to equity investors that can vote on resolutions etc.), however we have included wording from BlackRock below in regards to their engagement and reporting policies within this area.

Blackrock believes that effective disclosure can lead to real change in how companies are managed for the benefit of all stakeholders. Their Investment Stewardship team is a key partner for all investment teams at BlackRock. Their Investment Stewardship efforts, including their direct engagement and voting activities, encourage companies to deliver long-term, sustainable growth and returns for their clients.

Partnership across teams at BlackRock ensures they can leverage insights and knowledge, and bring the voice of all stakeholders, including corporate bond holders, to the table.

BlackRock's footprint in the fixed income markets also means that they have substantial opportunity to engage with sovereigns and debt management offices, issuers of securitized bonds, rating agencies, index providers as well as partnering with their public policy teams regarding ESG regulation, policy, and disclosure. BlackRock can also play a role in promoting awareness, disclosure, fostering debate, and highlighting risks, across various financial market participants.

Engagement is core to BlackRock's stewardship program as it helps them assess a company's approach to governance, including the management of relevant environmental and social factors. To that end, they conduct approximately 3,000 engagements a year on a range of ESG issues likely to impact their client's long-term economic interests.

For 2022, BlackRock are focusing on the following five engagement priorities:

- Board quality and effectiveness – Quality leadership is essential to performance. Board composition, effectiveness, diversity and accountability remain top priorities.

- Climate and natural capital – Climate action plans with targets to advance the transition to a low carbon economy. Managing natural capital dependencies and impacts through sustainable business practices.

- Strategy, purpose and financial resilience – A purpose driven long-term strategy, underpinned by sound capital management, supports financial resilience.

- Incentives aligned with value creation – Appropriate incentives reward executives for delivering sustainable long-term value creation.

- Company impacts on people / human capital – Sustainable business practices create enduring value for all key stakeholders

The priorities outlined above are aligned with the firm's commitment to make sustainability BlackRock's standard for investing and to support the goal of net zero greenhouse gas emissions by 2050 or sooner.

BlackRock has as an ESG Capital Markets working group, including investment professionals globally across fixed income asset and capital markets, specifically focused on driving innovation and diversifying issuance in ESG oriented fixed income securities, working directly with issuers and dealers to expand issuance across sectors and market new concepts.

<u>Mercer</u>

The sub-managers within the Mercer Secured Finance Funds engage with issuers via regular engagement meetings, related to various ESG issues. An example of an instance where Insight, one of the underlying sub-managers, have engaged with an underlying issuer is outlined below.

Key engagement activity undertaken over the year
Company: *Project Regents* Term securitisation of UK Bridging loans originated by a UK specialist lender with seven years of track record and £350 of total originations. Insight led discussions around ESG as the ESG score assigned was low and Insight had some concerns in originator governance. Insight discussed with Regents their concerns about the make-up of the board and how they prefer to see the majority of the board as independents. In response to Insight's comments, Regents responded that they were in the process of appointing a non-executive director (NED). This is expected to take nine months, This NED would be involved in bod approval of significant corporate decisions. Regents have emphasised that there are a number of risk mitigants in place on governance such as group level audits and facility level "agreed upon procedures" audits. Due to these discussions, Insight invested in the loan and are comfortable that Regents are putting in place the improvements in governance that were requested. Insight are close to the management and will monitor the progress.