Intended for retail clients and consumers.
All investing involves risk.

Climate Impact Pledge

An overview

LGIM

Why is a Climate Impact Pledge important?

Everything is connected. The environment and the economy are so closely linked.

Climate change and its ripple effect on areas like farming and agriculture, food supply, transport infrastructure, buildings and livelihoods has become more apparent. This has the potential to have a significant financial impact on global markets and in turn an individual's pension and investments.

Climate change is not just an environmental issue, it's a socio-economic issue too.

Taking action to avert the climate emergency by transitioning to a low-carbon economy (an economy based on sustainable actions that result in less environmental impact) is more critical than ever.

A vital way to address climate change is to reach net zero carbon emissions by 2050 globally. Carbon emissions is one of the key greenhouse gases (GHGs) that, when emitted into the atmosphere, are responsible for the greenhouse effect on the planet.

What this means is that globally we need to emit no more carbon emissions into the atmosphere than the earth can absorb. Therefore, to reach net zero, the things that emit carbon (industry, agriculture, energy extraction and use) need to match the things that absorb carbon in our natural world (trees, soil, oceans) and via new technologies, for example for carbon capture.

This is all part of the mission to prevent global warming going above a dangerous temperature.

An international climate change treaty, called the Paris Agreement, aims to stop the world's average temperature rise to well-below 2°C, or ideally 1.5°C. Today, we are at approximately 1.1°C and already witnessing the devastating effects of global warming.

To help address this critical threat, in 2016, Legal & General Investment Management (LGIM) launched our targeted climate engagement programme. LGIM's Climate Impact Pledge assesses approximately 5,000 companies worldwide – across 20 climate-critical sectors – on their climate governance, strategies, policies, metrics and targets.

From oil and gas, clothing and airlines to technology, food manufacturing and utilities, we have selected the companies that are responsible for more than half of greenhouse gas emissions from the world's largest listed companies.

In addition to a data-driven assessment of climate commitments and efforts of these companies to limit carbon emissions to net zero by 2050, we engage with a subset of these to influence and support them to reach this objective.

We act as shareholders on behalf of our members and clients. As a result, if companies fall short of minimum expectations and fail to address their climate responsibilities over time, we act by using our granted investor voting rights – such as voting against the re-election of a company director/chair in annual general meetings. Ultimately, we may exclude them (dependent on guidelines of the relevant investment agreement) from those fund and pension ranges that adopt the Climate Impact Pledge[1].

In this kind of environment, companies need to show they can change and adapt. Through the Climate Impact Pledge, the aim is to influence the direction of companies to evolve into better versions of themselves, to avoid exacerbating global warming.

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1. Companies are divested from selected funds with £158 billion in assets under management (as at 31 December 2022), including funds in the Future World fund range, LGIM's ESG fund ranges and all auto-enrolment default funds in L&G Workplace Pensions and the L&G Mastertrust. Companies are divested up to a pre-specified tracking-error limit. If the tracking error limit is reached, holdings are reduced rather than fully divested. LGIM's total AUM was £1.2 trillion as at 31 December 2022. The AUM disclosed aggregates the assets managed by LGIM in the UK, LGIMA in the US and LGIM Asia in Hong Kong. The AUM includes the value of securities and derivatives positions.

How we measure

Our assessment draws upon around 70 data points, including our own climate modelling tool (called Destination@Risk), which involves robust measurement of the climate risk embedded in investments and their climate alignment as well as several reputable third-party data providers.

Companies are scored out of a 100 across five key areas:

1.
Governance

How is the oversight of climate issues managed at the board level and communicated to investors?

2.
Strategy

What policies do companies have in place, and what policies are they lobbying governments for?

3.
Risks and opportunities

How much of companies' current earnings comes from 'green' activities and how much of potential future earnings is at risk in the low-carbon transition (shift from an economy that depends heavily on fossil fuels to a sustainable, low carbon economy)?

4.
Scenario analysis

What level of global warming are companies' plans aligned to?

5.
Metrics and targets

How ambitious are companies' emission targets, and how do they compare to past performance?

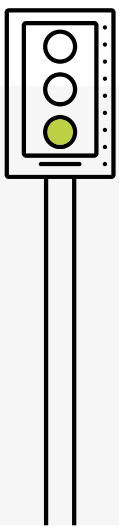
Compliance with individual indicators within these five areas is assessed through a traffic light system.

To be transparent and to help raise best practice standards across global markets, we make these climate ratings publicly available.

Red – Companies falling below our global minimum standards in this area.

Yellow – Companies that have met our global minimum standards but room for improvement remains.

Green – Companies that have exceeded our global minimum standards in this area.



There are several minimum standards or minimum expectations we look for when assessing companies. These include sector-specific questions such as:

Does the company…

- Have board member(s) with responsibility for climate-related issues?
- Have comprehensive climate disclosures?
- Have an environmental policy?
- Have a GHG (greenhouse gases) reduction programme?
- Have a (no) deforestation programme?
- Have a responsible investment programme?
- Consider environmental impact in product design?
- Disclose life-cycle assessment of emissions?
- Demonstrate a year-on-year reduction in emissions intensity?

Through data sources, we measure companies globally against these minimum standards. We vote against companies that do not meet at least one – or, for companies in North America, Europe and Australasia, three – of the minimum standards.

In 2023, we identified 299 companies out of the broader set of roughly 5,000 companies that did not meet our minimum expectations on climate change.

In-depth priority engagements and exclusion

We select approximately 100 companies (from the broader list of approximately 5,000 companies) for priority 'in-depth engagement'.

Sector experts from across LGIM's stewardship and investment teams work more closely with these companies to actively progress climate-related strategies and processes.

These companies are chosen because they are influential in their sectors, but in our view are not yet 'leaders' on climate change.

Further measurement is in place for those that are selected, under a sector-specific 'red line' method.

Examples of red lines:

- No operational emissions target
- No disclosure of Scope 3 emissions (indirect emissions that occur in a company's value chain)
- No restrictions around coal investing
- Plans to increase thermal coal capacity
- No plans for coal phase-out
- Lack of a comprehensive deforestation (clearing of forested land) policy
- Lack of comprehensive regenerative agriculture policy

Where companies do not perform well against our assessment or are unresponsive to engagement recommendations, we can ultimately make the decision to exclude investment in them in certain funds*. See the examples below.

If a company fails to meet our minimum expectations and red lines, a decision will be taken whether to exclude the company. The decision is considered and finalised through a robust internal governance process. Resulting actions are then implemented by the relevant investment manager as part of the annual update of the Pledge.

We continue to monitor companies after they have taken the decision to exclude them from relevant funds. Companies can be reinstated back into funds (that adopt the Climate Impact Pledge) if we believe that they have made satisfactory improvements.

Examples of where we have decided to exclude a company

Company in the cement sector

Reason: Breach of red lines including no operational emissions reduction target in place. Unsatisfactory responses to engagement and no improvements made since voting against the company Chair, due to the same concerns.

Company in the food sector

Reason: Progress on lower-impact products but no deforestation policy published and no targets or disclosure for Scope 3 emissions (includes all indirect emissions that occur in the value chain of a company) from agricultural products.

Company in the real estate sector

Reason: Breach of red lines including no disclosure of emissions from property portfolio or emissions target covering property portfolio's operational emissions. No improvements made following engagement and an earlier vote against the company Chair for the same reason.

Company in the utilities sector

Reason: Increased ambition for emissions reduction targets. However, pathway to action is seemingly misaligned as company plans to have coal running until 2050.

*Companies are divested up to a pre-specified tracking-error limit. If the tracking error limit is reached, holdings are reduced rather than fully divested.

Review process for the Climate Impact Pledge

The Climate Impact Pledge engagement programme is reviewed on an annual basis by the LGIM Investment Stewardship team.

The list of companies we engage with, vote against and exclude investments in, is updated on an annual basis and published in June each year.

Voting takes place at company meetings which can be held at any time during the year.

We continue to collaborate and challenge to help create positive change. Inaction is not an option.

Contact us

For further information about LGIM, please visit lgim.com or contact your usual LGIM representative

Key Risks

The value of an investment and any income taken from it is not guaranteed and can go down as well as up, you may not get back the amount you originally invested.

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