Australian Government
Commonwealth Superannuation Corporation

09/20

Your super and climate change

Climate change is a significant global risk. We take it seriously, as we do with all of the risks that we must consider in order to build robust investment portfolios that can deliver all of our customers a sustainable retirement income. We take an active but integrated approach, considering our entire portfolio net exposures to Environmental, Social, and Governance (ESG), Technology, Resourcing, and Financial risks.

Any single risk cannot be viewed in isolation because risk is fluid and interactive, it changes with regulatory, technological and behavioural trends.

What are the investment risks associated with climate change?

- **Transition risk** arises from the transition to a low-carbon economy. Transition risks include changes in regulatory policy, technological innovation, renewable power and energy advancements, and social adaptation.
- **Physical risk** causes direct damage to assets or property as a result of rising global temperatures. Physical risks, including extreme weather events, have the potential to cause supply chain disruption, resulting in lower productivity as well as potentially lower asset values.
- **Liability risk** stems from the potential for litigation if entities and governing bodies do not adequately consider or respond to the impacts of climate change, and may include the potential breaching of directors' duties.

CSC Commonwealth Superannuation Corporation

The information provided in this factsheet is general advice only and has been prepared without taking account of your personal objectives, financial situation or needs. Before acting on any such general advice, you should consider the appropriateness of the advice, having regard to your own objectives, financial situation and needs. You may wish to consult a licensed financial advisor. You should obtain a copy of the relevant **Product Disclosure Statement (PDS)** and consider its contents before making any decision regarding your super.

Defence Force Retirement and Death Benefits Scheme
ABN: 39 798 362 763

Australian Defence Force Superannuation
ABN: 90 302 247 344
RSE: R1077063

Commonwealth Superannuation Scheme
ABN: 19 415 776 361
RSE: R1004649

Public Sector Superannuation accumulation plan
ABN: 65 127 917 725
RSE: R1004601

Military Superannuation and Benefits Scheme
ABN: 50 925 523 120
RSE: R1000306

Australian Defence Force Cover
ABN: 64 250 674 722

Public Sector Superannuation Scheme
ABN: 74 172 177 893
RSE: R1004595

1922 Scheme
DFRB Scheme
PNG Scheme
DFSPB
CSC retirement income

What is CSC's role?

Robust risk management is the most critical aspect of converting savings into wealth capable of generating sustainable income. It is the heartbeat of our investment team. We were one of the first Australian superannuation funds to implement full risk transparency at the security level in our portfolio more than a decade ago.*

In order to fulfil the financial retirement objectives of all our customers, we work to build portfolios that:

(i) take the right types of risks, in sufficient quantities, to achieve our return targets sustainably; and

(ii) mitigate the types of risks that could impair capital permanently in a material way.

It's critical to our purpose that the financial returns generated from our portfolio of investments meet our compensation hurdles for the risks we take in exposing our customers' savings to them.

* CSC's bottom-up risk system integrating financial, natural & social-resource risks across the entire portfolio has been fully operational since July 2009 and covers both public and private market assets. We have been continuously evolving this to incorporate factor analysis, portfolio attribution and other analytic tools to supplement the primary risk system, recognising the need for specialised complementary or contrarian insights to facilitate better informed decision making.

We manage climate investment risk in three ways

1. Renewable investments

We invest in renewable-energy assets and strategies because renewable energy is the most likely future of our global energy system.

We believe that our strategy will genuinely support a smooth transition to a lower-emission world.

2. Robust transitions from coal

We support robust transitions away from coal by focusing our exposures in the relatively cleaner producers in Australia who are also self-investing in renewables and operate with high human and community safety standards. As long-term investors, we can support a transition that respects: the practical demands for energy in our country and around the world simply to continue to operate; the labour force impacts; and understands that divesting to shorter-horizon shareholders is unlikely to reduce the climate risk at all.

3. Impact on climate footprint over time

We don't have a specific temperature target (e.g. 1.5 degrees) because climate action can be implemented in many ways, not all of which actually result in reduced climate risk. Our approach considers the current state of a company's carbon footprint and the market's appreciation of that (as reflected in its share price), as well as its capability to improve that footprint over time. And to measure that at a net portfolio level, because the risks and opportunities from different climate actions in our domestic and international assets are interdependent.

We believe that our strategy will genuinely support a smooth transition to a lower-emission world.

Portfolio facts that evidence our strategy

1. Investing in renewables

The UN Sustainable Development Goals (SDGs) are global aspirations for a better world. In the case of climate change, the relevant goals are *SDG 7: Affordable and Clean Energy* and *SDG 13: Climate Action*.

We have been and will continue to invest in renewable energy, primarily (but not exclusively) through our private asset portfolio. We recognise that renewable energy is the future of our global energy system. At present we have:

- Over A$771 million invested in high-quality private and public assets—including wind farms, waste management infrastructure projects, and renewable energy initiatives that add to the net new supply of facilities (as at 30 June 2020) .
- These investments reduce our portfolio carbon emissions by over 200,000 tonnes of CO2 per annum, compared to having this money invested passively to meet a similar level of energy demand (for calendar year 2019).
- Our Macarthur Wind Farm is the largest windfarm in the Southern Hemisphere and provides energy for 181,000 households, saving 1.5 million tonnes of greenhouse gases every year. This asset has returned 12.4 % pa to our investors, with a low risk profile, since inception to 31 December 2019.

2. Supporting robust transition away from coal

Australia (and the rest of the world) still require coal to operate, but this is reducing. To ensure this process is smooth and as fast as it can be, we support robust transitions away from coal, constrained today not by any lack of renewable energy, but by an inability to store and distribute it reliably.

To do this, we recognise that:

- Divesting a coal company will not reduce its impact on climate because this has very limited impact on global emissions. It simply changes the ownership of the asset, but it continues to operate. We believe that long-term investors have a responsibility to support these existing companies to make the necessary trade-offs in short-term profits to ensure longer-term viability via investment in cleaner activities.
- Australian producers are amongst the cleanest in the world and operate with high human and community safety standards.
- There is value in engaging with companies both directly (via dialogue) and indirectly (via voting all our stock). Our ability to do this derives from an investment governance process that began for us back in 2003. Our efforts were recognised then by the United Nations in the form of an inaugural innovation award for impactful efforts on sustainability*.

Over many decades, the CSC Board has evaluated and experienced the advantages and disadvantages of different approaches to encourage sustainability in the long term value and quality of our customers' savings. We have compared the impact we can make through:

- Divestment (we do not invest in tobacco or cluster munitions, for example);
- Active engagement (we engage both directly and indirectly with all our most material public companies);
- Proxy voting (we vote all of our stock domestically and internationally consistently and according to our principles);
- Collaboration with global leaders (see Appendix for details); and
- Integration of analysis of all risks into our formal investment processes and decision-making frameworks.

We're preparing our portfolios to manage the risks and opportunities to our customers' savings should any of the many possible climate scenarios eventuate.

*An inaugural citation developed by the UN Environment Program Finance Initiatives (UNEP FI) and the Royal Awards for Sustainability, recognising CSC's innovative and impactful consideration of ESG factors. We identified the criticality of long-term thematic risks and poor operational practices.

3. The journey is just as important as the destination

We do not have any specific climate scenario or temperature target. This is because climate action can be implemented in many ways, but not all of them actually reduce climate risk. We seek genuine, authentic steps that can achieve impact consistently and incrementally, rather than grandiose gestures.

There are many facets involved in managing the risks of climate change effectively in the best interests of our customers. We're preparing our portfolios to manage the risks and opportunities to our customers' savings should any particular climate scenario (of the many possible scenarios) eventuate—e.g. uncertainty about the timing and quantity of government intervention such as carbon tax and at what price, actions from all producers or consumers of old and new energy.

The CSC Board of Directors has and continues to have detailed discussions about how climate change risk can be genuinely managed not just in our investment portfolio, but also within our own organisation. To that end, we are developing a formalised organisation wide climate-risk management policy, some of which has already been implemented for some time.
The CSC investment team assesses and manages climate-related issues through the portfolio by:

- Understanding and measuring the climate-related exposures through the portfolio by seeking partnerships with external research and data providers, incorporating exposures to physical, transition and liability risks related to climate;
- Conducting stress and scenarios analysis, such as forward looking scenarios of different transition pathways to a lower carbon economy, carbon price implications, stranded assets analysis and physical climate scenarios;
- Incorporating CSC's active owner and climate-risk policies within external manager mandates. In an

environment of developing policy responses, active management is likely to be very important;

- Engaging actively and constructively with investee companies on climate change issues;
- Dedicating capital expenditure budgets within each of its directly-held property assets to minimise physical climate risks. We invest in global benchmarks to support and guide those budgets and their focus.
- Actively evaluating renewable energy and other sustainable opportunities and provide private capital to those which have high potential of generating sufficiently high risk-adjusted return, particularly in regions requiring significant infrastructure investment to capitalise on climate change;
- Disclosing climate change exposures to stakeholders.

Examples of climate change risks to investment sectors considered

We are methodically and comprehensively considering which companies, industries and countries will benefit from transition to a lower carbon world compared to the ones that will lose value.

While fossil fuels are the main companies the media and investors typically focus on, our full investment team (across all asset classes and markets) have extended our assessment to a broader assessment of potential impacts, for example:

- **Energy:** transitioning from coal and oil to renewables + energy storage & responsive demand management.
- **Autos:** transitioning from combustion engines to electric motors.
- **Construction**: the impact on real estate assets of increases in energy efficiency standards will require refits for homes and offices and increasingly higher construction standards for bushfire prone areas.
- **Agriculture:** Productivity increases required to offset deforestation, especially in emerging markets, use of agricultural chemicals particularly in developed countries, transitioning away from reliance on animal proteins.
- **Consumer sectors:** increasing restrictions on plastic will impact many consumer staples companies.
- **Waste:** Transition to a circular economy will see new infrastructure and utilities systems benefit from a more sustainable approach to limited resource usage.
- **Water:** water shortages and droughts driving water efficiency and increasing competition between users.
- **Infrastructure:** transition towards decentralised networks in favour of lower emitting (but slower) transportation methods.

We have been pioneers in considering non-financial ESG issues for many years and continue to engage with industry participants, specialist managers and service providers in increasing disclosure, transparency and availability of quality data to price and quantify these emerging risks. For example, UN Innovation award in 2003, AsianInvestor for Excellence in Governance (2018) and Innovation (2019) awards, Bretton Woods II top 20% of the world’s most Responsible Asset Allocators in 2017 and 2019.

We will continue to assess all risks and opportunities arising from climate change, as we do with all of the risks that we must consider in order to build robust investment portfolios that can deliver all of our customers a sustainable retirement income.

Appendix: Collaboration with global leaders

Since 2001 CSC has been instrumental in collective efforts to address climate change (and other ESG) risks, via membership of the Investor Group on Climate Change (IGCC). CSC has been a signatory to the Carbon Disclosure Project (CDP) since 2002 and in recent years the associated Water and Forests program. This program uses an online system to seek disclosure from companies of their exposure to the risk of carbon, water and deforestation in their operations and supply chains. This enables wider investor scrutiny on climate change risk.

CSC views participation in such collective efforts as the most effective way to minimise overall (“non-diversifiable”) climate change risk to customer portfolios, as (aside from considerations mentioned above) we do not regard CSC’s investment decisions as capable, in isolation, of affecting the economics of large-scale industrial activities such as fossil fuel-based energy production.

CSC is currently also committed to the Montreal Carbon Pledge, Principles of Responsible Investment (PRI), and the Global Institutional Governance Network (GIGN). We publicly support the global best practice Taskforce for Climate-related Financial Disclosures (TCFD), committing to increased transparency and disclosure of climate related financial risks and encouraging our investment managers and service providers to do the same. The ultimate aim of increased transparency is to make markets more efficient, and economies more stable and resilient.

We have also recently signed the Carbon Disclosure Project's (CDP) non-disclosure campaign. This collaborative effort seeks to increase response rates from previously non-disclosing companies to provide investors with greater transparency and comparability of high-impact companies across global markets, with respect to environmental issues.

We are also a signatory to the Partnership for Sustainable Capital Markets. The Partnership involves some of the world's largest asset owners and represents a firm commitment to long-term investing and the consideration of environmental, social and governance factors. It also poses a warning to companies seeking capital, stating "companies that seek to maximise corporate revenue without considering their impacts on other stakeholders — including the environment, workers and communities — put their long-term growth at risk and are not attractive investment targets for us." The letter also provides a similar message to financial partners.

Where can I get more information?

CSS — **Commonwealth Superannuation Scheme**

EMAIL members@css.gov.au
PHONE 1300 000 277
FAX (02) 6275 7010
MAIL CSS
GPO Box 2252
Canberra ACT 2601
WEB csc.gov.au

PSS — **Public Sector Superannuation Scheme**

EMAIL members@pss.gov.au
PHONE 1300 000 377
FAX (02) 6275 7010
MAIL PSS
GPO Box 2252
Canberra ACT 2601
WEB csc.gov.au

PSSap — **Public Sector Superannuation accumulation plan**

EMAIL members@pssap.com.au
PHONE 1300 725 171
FAX 1300 364 144
MAIL PSSap
Locked Bag 9300
Wollongong NSW 2500
WEB csc.gov.au

ADF Super — **Australian Defence Force Superannuation**

EMAIL members@adfsuper.gov.au
PHONE 1300 203 439
FAX 1300 204 314
MAIL ADF Super
Locked Bag 9400
Wollongong DC
NSW 2500
WEB csc.gov.au

Military Super — **Military Superannuation & Benefits Scheme**

EMAIL members@enq.militarysuper.gov.au
PHONE 1300 006 727
FAX (02) 6275 7010
MAIL MilitarySuper
GPO Box 2252
Canberra ACT 2601
WEB csc.gov.au