SPRING 2025

ENGAGE

WWW.LPF.ORG.UK

LOTHIAN PENSION FUND

CONTENTS

WELCOME TO ISSUE 9 OF ENGAGE

2024 was another exceptionally busy year at Lothian Pension Fund (LPF). Thanks to the strong funding position of 157% at March 2023, we were able to reduce contributions for the majority of our employers for the period commencing April 2024. This enabled our local authority employers to redeploy their budget into other council services to the benefit of the community. We also increased the size of our investment team improving resilience, capacity and accountability.

This issue includes updates on our responses to industry consultations (the UK Government Pensions Investment Review and the Financial Reporting Council's review of the UK Stewardship Code) as well as our support of investor initiatives focused on addressing systemic risks posed by climate change and biodiversity, and an example of our approach to voting.

I'm also pleased to announce that we've been shortlisted for the Pensions Age Defined Benefit Pension Scheme of the Year award. The Pensions Age Awards celebrate excellence within the UK Pensions industry in these increasingly challenging economic times. We have a clear purpose at LPF – to administer the LGPS for Edinburgh and the Lothians – and a vision to be the leading LGPS in Scotland, if not the UK, and it's great to see our hard work being recognised externally and by our peers.

For more information on our Responsible Investment activities, you can view our 2024 Stewardship Report, on our website.

David Vallery
Chief Executive Officer
Lothian Pension Fund

RESPONSIBLE INVESTMENT UPDATE

2024 was an historic year with voters in more than 60 countries, representing around half the world's population, going to the polls. It turned out to be a difficult year for incumbents, resulting in significant political changes.

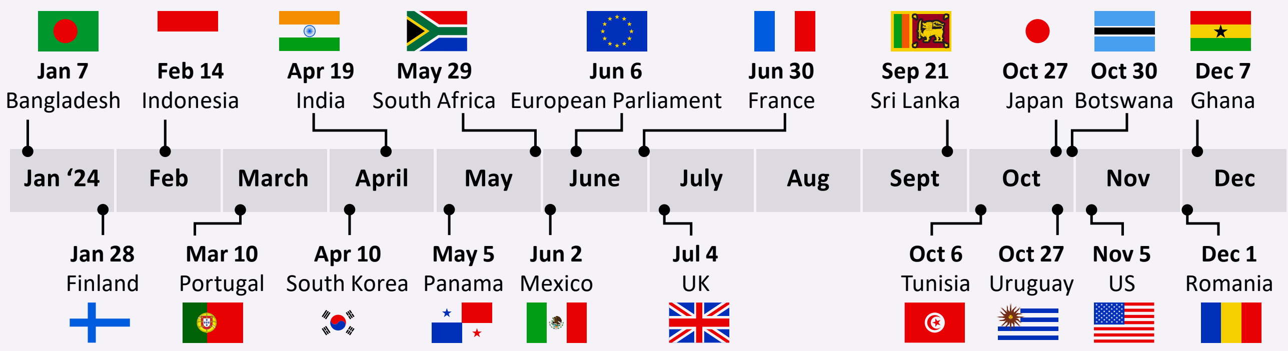
President Trump

The inauguration of Donald Trump as the 47th President of the US on 20 January 2025 was of global interest, with key features of his campaign including a withdrawal of the US from the Paris Agreement* and proposals to implement huge new tariffs* on imports to the US.

THE PARIS AGREEMENT

*The Paris Agreement is an international treaty, which was adopted at the United Nations Climate Change Conference in Paris in 2015. It brings the international community together to undertake ambitious efforts to combat climate change and adapt to its effects, with the ambition to limit the global average temperature rise in this century to well below 2 degrees Celsius, while pursuing efforts to limit the temperature rise to 1.5 degrees.

Voters in nations around the world went to the polls in 2024



* Date indicates start of elections of first election of the year.
Source: The International Foundation for Electoral Systems.

PEW RESEARCH CENTER

TARIFFS

*Tariffs act as a tax on imports: by increasing the price paid by US consumers for imported goods, they reduce demand for foreign made goods and potentially support investment in domestic production capacity, while the government can use the extra tax income to reduce government debt and increase spending on domestic policies.

Within his first days in office, President Trump signed an order to remove the US from the Paris Agreement, repealed a bar on drilling for oil in the Arctic, cut-off climate-related funding that was approved under the Inflation Reduction Act, froze the leasing of federal lands and waters for renewable projects and revoked an executive order from President Biden for 50% of new vehicle sales to be electric vehicles by 2030.

While President Trump has yet to fully implement new import tariffs, the biggest impact from a climate perspective is expected to come from tariffs on lithium-ion battery imports from China. As the US imports large quantities of these batteries from China, the proposed 60% tariff could increase the cost of energy storage systems in the US by 16%. Furthermore, President Trump's proposed 25% tariff on imports from Mexico, which accounts for about one-third of total US electric vehicle imports, is expected to reduce demand for these foreign-made electric vehicles.

While uncertainty surrounds the scale and timing of tariff implementation at the time of writing, targeted countries (for example China, Canada and Mexico) are expected to retaliate with their own tariffs on US-made goods. This means that tariffs are likely to reduce international trade, reduce economic growth and increase inflation. Markets have already responded to this outlook with government bond yields rising, acting as a brake on global economic growth.

The loss of federal policy support will act as a drag on the green transition in the US, in particular reducing support for increased adoption of electric vehicles and the development of offshore wind farms in US federal waters. However, the withdrawal from the Paris Agreement will take 12 months to be implemented and is mainly symbolic given that the US has not been leading global efforts to tackle climate change. Furthermore, the economics of renewable energy remain favourable in the US and state-level policies will continue to support development of onshore wind and solar farms, maintaining some momentum in the energy transition.

International ramifications

Over recent months we've seen an exodus of the largest US banks from the Net Zero Banking Alliance (NZBA) and a steady stream of departures of investment firms from the Net Zero Asset Managers Initiative (NZAMI). Threats of US legal action related to accusations of collusion or anti-competitive practices have also created a more risk-averse approach to participation by these investment firms in collaborative engagement activities.

While many of these financial institutions retain commitments to supporting the global transition to net zero, we've observed a broad retrenchment from commitments to decarbonise their investment or lending portfolios, reflecting heightened scrutiny over the ability to meet these targets given the real-world transition is not progressing as quickly as was previously anticipated. The underperformance of some green or transition focused investment strategies in recent years (with high inflation and interest rates impacting the economics for capital intensive investments such as offshore wind) has highlighted the risk of performance volatility in focused investment strategies that lack diversification.

In light of the above, the Glasgow Financial Alliance for Net Zero (GFANZ)* announced a major strategic pivot in January 2025. GFANZ will no longer require the financial sector organisations it works with to have made net-zero commitments and is now transitioning to a stand-alone body supporting broader climate financing efforts, particularly on the mobilisation of transition finance to emerging economies.

GFANZ

* GFANZ was formed during the global climate conference in Glasgow in 2021 as an umbrella organisation for leading financial institutions that were committed to accelerating the net-zero transition and had adopted net-zero targets.

There is increasing understanding that the transition to a lower carbon economy will take many decades and is unlikely to proceed smoothly or uniformly across all markets or geographies. Merely investing in the small proportion of companies that already operate in green industries today will be insufficient to bring about the necessary industrial-economic transformation across the globe. Instead, companies across all industries, in particular those that create the most emissions, need policy support and investment to plan and implement appropriate transition plans.

LPF's approach to climate change already acknowledges the uncertainties of a multi-decade transition. We continue to engage with investee companies, both directly and through collaborative initiatives and service providers. We also engage with policy makers and regulators, for example by participating in industry consultations and as a signatory to the [Global Investor Statement to Governments on the Climate Crisis](), where we called on governments to enact five essential policy actions to accelerate the private capital flows needed for a just transition to a climate-resilient, nature-positive economy. Later in this issue, our Responsible Investment Analyst, Natalie Drysdale, provides more information on our participation in a collaborative engagement initiative, aiming to address nature and biodiversity loss around the world.

UK

In July 2024 a new Government was elected in the UK with a manifesto that included a number of commitments relevant to Local Government Pension Schemes:

- Pensions Review: aiming to boost investment, increase savers' returns and tackle waste in the pensions system
    - Our Chief Financial Officer, Alan Sievewright, provides more information on our engagement with the UK Government on these proposals below on page 8
- Transition Plans: aiming to make the UK the green finance capital of the world, UK-regulated financial institutions (including pension funds) and the largest 100 companies listed in the UK will be required to develop and implement credible climate transition plans that align with the goals of the Paris Agreement
    - In September 2024 LPF joined a group of investors, to write to the chairs of large UK-listed companies setting out our expectations for companies to produce credible transition plans and provide investors the opportunity to vote to approve these plans. Further detail is provided on page 10
    - Transition plans are expected to build on existing expectations for pension funds to undertake climate-related risk management. We expect a consultation on transition plan reporting for UK-regulated financial institutions to be launched in 2025.

In mid-2024, the Financial Reporting Council (FRC) announced revisions to the UK Stewardship Code (the Code) reporting requirements ahead of a fuller consultation on more significant changes, which was launched in November. The Code promotes improved transparency, disclosure and accountability in the stewardship eco-system. Signatory reporting is assessed by the FRC to maintain standards. The Code has a strong reputation both domestically and internationally for supporting high-quality stewardship.

- As a signatory to the Code, LPF welcomes the aim to reduce the reporting burden while still supporting high quality and accountability. We've responded to the consultation, noting that the updated Code is expected to be published later in 2025 for first implementation in 2026, while our 2025 report will follow the revised requirements announced in 2024.

Also in 2024, the Financial Conduct Authority (FCA) announced an overhaul of UK listing rules as part of their efforts to boost growth and innovation in UK stock markets. Notable changes will have an impact in terms of stewardship approaches:

- The removal of mandatory shareholder votes on significant party transactions
- The removal of mandatory shareholder votes on related party transaction
- A more permissive approach to listing with dual class share structures.

The FCA acknowledged that this new approach slightly increases risk for investors but takes the view that this approach better reflects the risk appetite that the UK economy needs to achieve growth. We'll be managing the implications of the changes by adjusting our minimum expectations for UK companies on these corporate governance topics while continuing to advocate for better practice application of shareholder rights.

In this issue of ENGAGE, we include an example of engagement and voting on corporate governance matters by one of our in-house equity portfolio managers, Stewart Piotrowicz.

Gillian de Candole,
Head of Responsible Investment

UK GOVERNMENT PENSIONS REVIEW

The UK Government announced their Pension Review in July 2024, aiming to boost investment, increase savers' returns and tackle waste in the pensions system. The review is focused on defined contribution workplace schemes and the Local Government Pension Scheme (LGPS) in England and Wales.

The review is being led by the Pensions Minister, working closely with the Minister of State at the Ministry of Housing Communities and Local Government (MHCLG) to look at how tackling fragmentation and inefficiency can unlock investment potential of the £360m LGPS in England and Wales.

The first phase of the review focused on developing policy in four areas related to pension investment:

- Driving scale and consolidation of defined contribution workplace schemes
- Tackling fragmentation and inefficiency in the LGPS through consolidation and improved governance
- The structure of the pensions ecosystem and achieving a greater focus on value to deliver better outcomes for future pensioners
- Encouraging further pension investment into UK assets to boost growth across the country

LPF participated in the Call for Evidence in September 2024, which was part of the first phase of the Pensions Review. While the

Scottish LGPS is out with the remit of the review, LPF is a successful fund within both the Scottish LGPS and in the wider UK context, so our contribution is meaningful to this review. LPF's internal investment capability is a significant cost advantage, and our collaborative efforts with like-minded funds generate additional benefits to each fund. This includes supporting collaborative partner funds on responsible investment matters.

Interim findings from phase 1 of the Pension Review were published in November 2024, accompanied by two consultations:

1. Unlocking the UK pensions market for growth
2. Local Government Pension Scheme in England and Wales: Fit for the future

LPF has responded to the second of these, supporting proposals to strengthen the management of LGPS investments as our business model already utilises key aspects of the proposals:

'LPF's internal investment capability is a significant cost advantage, and our collaborative efforts with like-minded funds generate additional benefits to each fund.'

- Our in-house investment management saves LPF c.£30m/year on investment costs, based on independent benchmarking, whilst also achieving better than peer group investment return with lower investment risk. Our FCA regulated firm, LPFI, provides investment management services to partner LPGS in Scotland and Northern Ireland, generating savings for these funds and aligning with the Government's aim to generate more efficiencies within the system
- LPF's investments include local and UK infrastructure, property, equities and bonds. Therefore, whilst our strategy is focussed on earning an appropriate risk adjusted return to benefit members and employers, it also supports the UK government's agenda for pension schemes to invest in the UK and its infrastructure. We suggest that the Administering Authorities of LGPS funds set a UK level "target" for local investing, supplementing this with reporting of where in the UK these assets are located.

Alan Sievewright,
Chief Finance Officer

COLLABORATIVE ENGAGEMENT FOR CLIMATE STRATEGY VOTES

Engagement Objectives

Support companies to adequately plan for the decarbonisation of their business models to reduce transition risk.

Background

Investors expect companies to set out credible transition plans, that include Paris-aligned targets and detailed strategies for achieving those goals. To enable shareholders to make informed investment and stewardship decisions, companies should outline their climate strategies within these transition plans and include material climate-related impacts in their financial statements.

Around a fifth of FTSE 100 companies (excluding investment trusts) have provided their investors with the opportunity to vote to approve their climate strategy and/or transition plan and this is now being viewed as good practice.

Providing a resolution on the climate transition plan at the company's Annual General Meeting (AGM) enables shareholders to signal support for the plan and associated capital expenditure requirements. Conversely, it also allows investors scope to express concern through a dedicated vote. Under the UK Corporate Governance Code where there's significant shareholder dissent (20% or more), such companies should engage with shareholders about their concerns.

Action

In September 2024, LPF joined a group of investors, led by the Local Authority Pension Fund Forum (LAPFF) and CCLA, to write to the chairs of 76 FTSE 100 companies that haven't held a vote on their climate transition plans in the past three years. The letter detailed our expectations for companies to set out credible transition plans and provide investors the opportunity to vote to approve these plans, ahead of the 2025 AGM season.

The letter noted that the Transition Plan Taskforce recommends that companies should update their transition plans every three years, and shareholders should be provided with a vote on this at least as frequently.

Outcome

64% of the targeted FTSE 100 companies responded:

- One company committed to an AGM vote in 2025, and another responded that it expects to include a vote on its transition plan in 2026
- The majority of companies stated that a transition plan vote is something they'll keep under review, indicating an increasing focus on accountability to shareholders.

Reflection

LPF's ability to influence investee companies through voting and engagement is limited as a relatively small minority investor. However, by collaborating with like-minded investors on engagement initiatives such as this letter, we amplify our voice to have a more significant influence to encourage companies to develop, publish and execute their plans to transition their business models. By encouraging an acceleration of decarbonisation of the global economy, we aim to drive the long-term value of our investment portfolio and contribute to the long-term health of the financial system. The letter was co-signed by 41 investors representing aggregate assets under management of £1.6 trillion.

This illustrates the collective scale of support for companies to demonstrate that they're adequately planning for the decarbonisation of their business models and to give shareholders a vote on their transition plan.

ROBUST MEASURES

Where we assess a company's climate strategy to be insufficient to meet the goals of the Paris Agreement and no opportunity is provided for a shareholder vote on the company's climate strategy and/or transition plan, we may:

- Vote against the reappointment of relevant directors
- Vote against the company accounts for failing to include material climate impacts within the financial statements
- Vote against remuneration policies that appear misaligned to incentivising transition
- File/co-file or vote for shareholder resolutions that call for robust target-setting, and a clear and credible strategy in place to achieve the stated targets.

The letter was co-signed by 41 investors representing aggregate assets under management of

£1.6 trillion

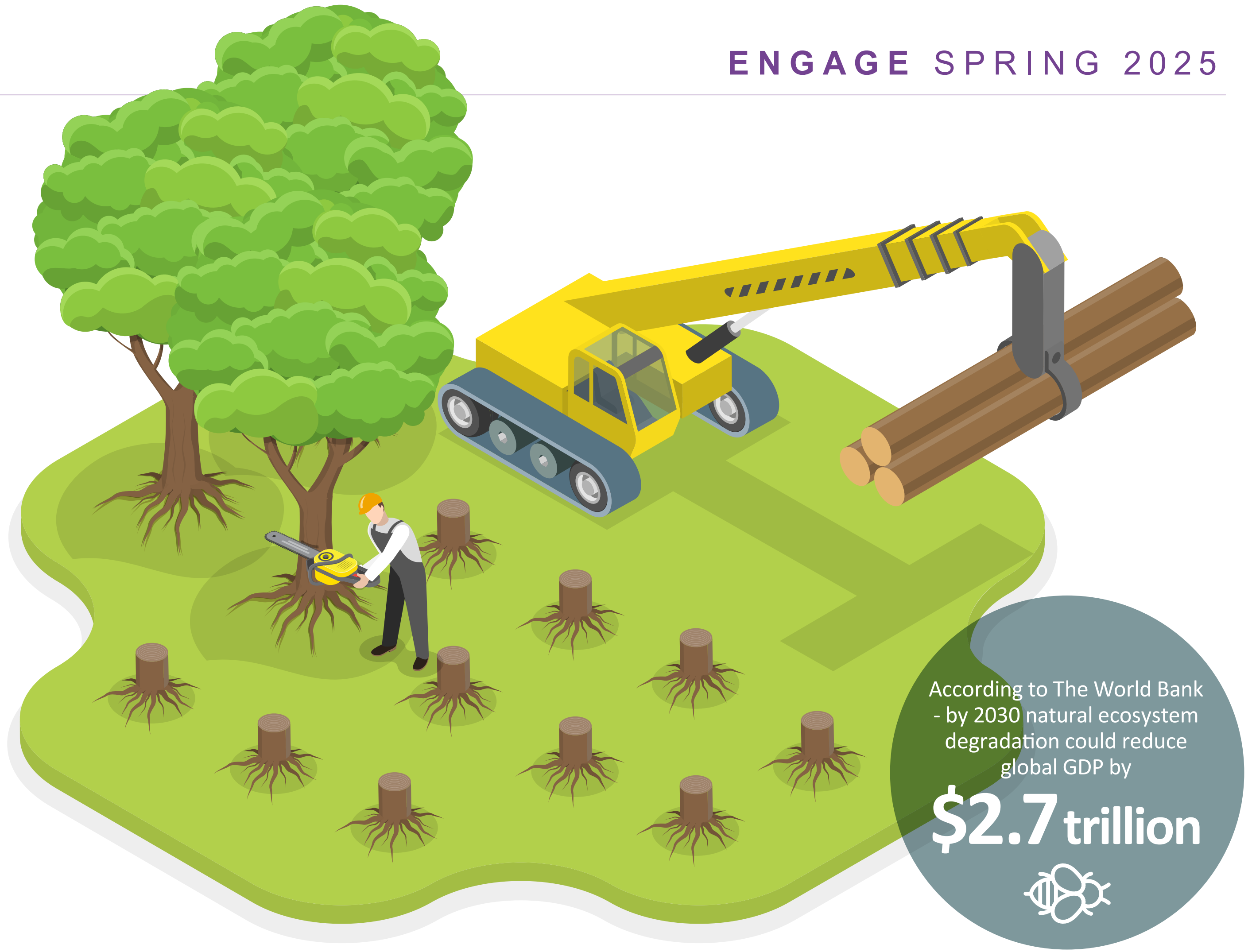
LPF is committed to transparency on voting. When exercising our equity voting rights, we consider both global best practice and regional governance requirements. Our voting and engagement service provider applies a rigorous case-by-case approach to assessment of transition plans, only recommending support of plans that demonstrate robust targets and a clear and credible strategy to achieve the stated targets.

Gillian de Candole,
Head of Responsible Investment

‘WE DEEM IT IMPORTANT TO SIGNAL OUR SUPPORT OF EFFORTS TO REDUCE THE IMPACT THAT OUR INVESTMENTS HAVE ON NATURE AND BIODIVERSITY.’

Natalie Drysdale, Responsible Investment Analyst

SPRING AND BIODIVERSITY



Climate change is resulting in nature and biodiversity loss around the world. This not only has an impact on people's livelihoods and natural ecosystems, but it also has material financial impacts for the global economy as a vast number of sectors rely on nature to deliver its business activities. The World Bank has estimated that natural ecosystem degradation could potentially reduce global GDP by US$2.7 trillion by 2030[1], with agriculture, foresting and mining industries and emerging markets being impacted to a greater degree. As nature and biodiversity loss has become more extreme over time, the importance of engagement to minimise the financial risks is growing, especially as long-term investors.

LPF has engaged on nature for many years through our voting and engagement partner, Federated Hermes EOS (EOS). We also recognise that stewardship efforts to influence companies to take actions to account for climate risks and reduce their adverse impact on nature can be more effective through collective engagement as an investment community. In October 2024, LPF became an endorser of the SPRING initiative. SPRING is a stewardship initiative for nature, addressing the systemic risks of biodiversity loss to protect the long-term interests of investors[2]. It was launched in June 2024 by the Principles for Responsible Investment (PRI).

As an endorser, we publicly signal support for the initiative's objectives and strategy. The initiative is focusing on engaging with companies identified as having high exposure to geographical areas suffering deforestation and land degradation through their direct operations or industry supply chains as deforestation and land degradation are significant contributors to global diversity loss. Encouraging further development and alignment of policies to support and protect biodiversity are also key elements of the SPRING engagement framework.

The SPRING initiative is initially focusing on engagement with 60 target companies. SPRING has a list of expectations that engagement may involve around which focus on three areas: business operations, strategy and risk management; supply chain management; and political engagement.

Nature Action 100 is another investor-led engagement initiative that aims to reverse nature and biodiversity loss. In addition to supporting engagement, Nature Action 100 has designed a benchmark that measures the progress of the initiative's 100 target companies against its expectations related to ambition, assessment, targets, implementation and governance of nature risks. The benchmark analysis has found strong progress is being made regarding disclosure of ambition, targets and implementation plans. However, improvements in disclosure on implementation progress is needed to allow for investors to better assess and measure if the company is on track to meet targets. There's also limited disclosure among the companies around the progress towards recognising and protecting the rights of Indigenous Peoples and local communities.

TARGETED APPROACH

The sectors that the target companies operate in significantly rely on nature and biodiversity including:

- Agriculture and Food
- Consumer Goods
- Mining
- Automotives
- Oil And Gas
- Finance
- Chemicals/Pesticides

LPF indirectly supports the initiative through EOS being a Nature Action 100 investor participant.

We own a small number of the SPRING and Nature Action 100 target companies, but due to the systemic issue of financial risks from nature and biodiversity loss, we believe it's important to support engagement to encourage best practice, regardless of whether we hold the company. This is the case particularly for engagement around companies' roles in encouraging public policy development. We endorsed SPRING as we recognise the potential that collaborative engagement can have in strengthening nature related corporate practices and mitigating some of the financial risks to our investments. Equally we deem it important to signal our support of efforts to reduce the impact that our investments have on nature and biodiversity.

Natalie Drysdale,
Responsible Investment Analyst

1: World Bank Document. 2: https://www.unpri.org/investment-tools/stewardship/spring/about-spring

THOUGHTFUL VOTING: ASHTEAD GROUP

Background

Ashtead is a UK-listed international equipment rental company with national networks in the US, the UK and Canada. It rents a range of construction and industrial equipment across a wide variety of applications to a diverse customer base. LPF have been shareholders of Ashtead since early 2012.

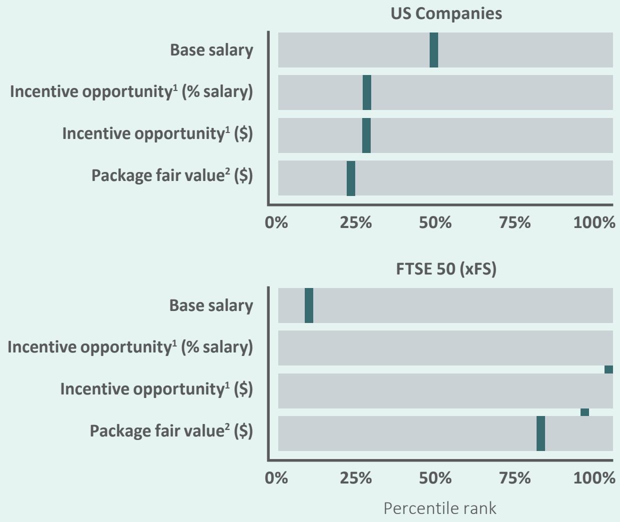
At LPF we believe that Responsible Investment includes exercising our rights and responsibilities as shareholders, so we aim to vote on all resolutions tabled at the General Meetings of our investee companies. We subscribe to a specialist third party service, EOS at Federated Hermes (EOS), to provide engagement and voting recommendations to us on our internally managed listed equity investments.

EOS has developed region-specific principles that set out the fundamental expectations of companies, including on business strategy, financial structure, governance and the management of social and environmental risks. These inform EOS's voting recommendations. Generally, we follow EOS's voting recommendations, however, we reserve the right to override them based on our internal team's investment research and direct engagement with companies.

Voting Considerations

In August 2024, we became aware that potentially controversial changes to Ashtead's remuneration policy and its long-term incentive plan (LTIP) were being proposed, for voting on by

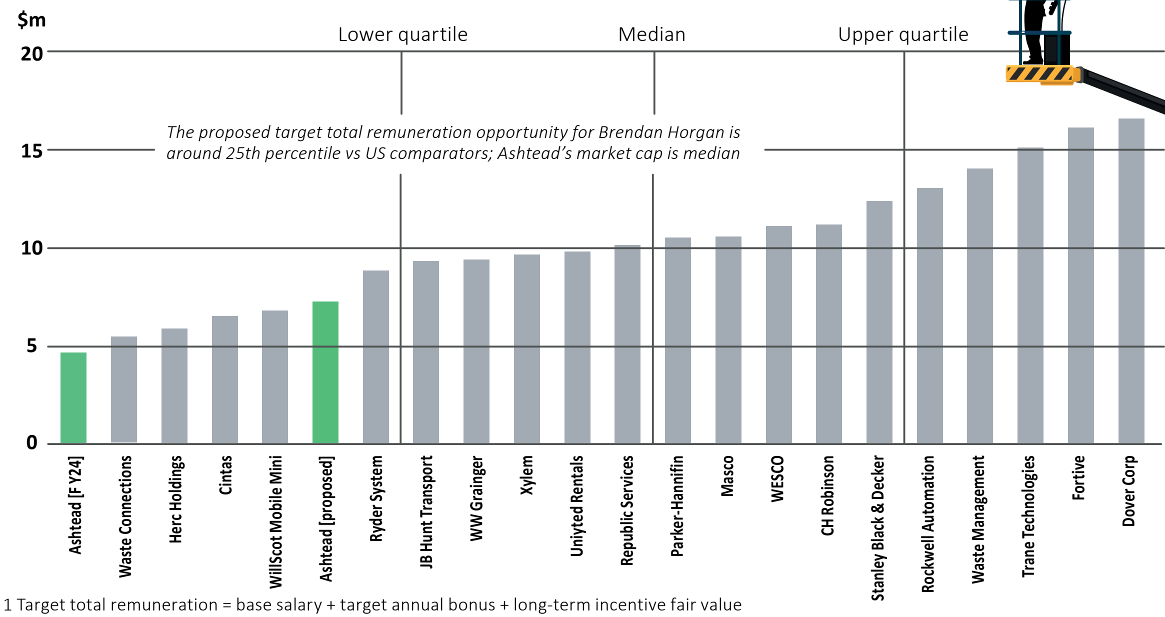
Comparative assessment of proposals vs market norms

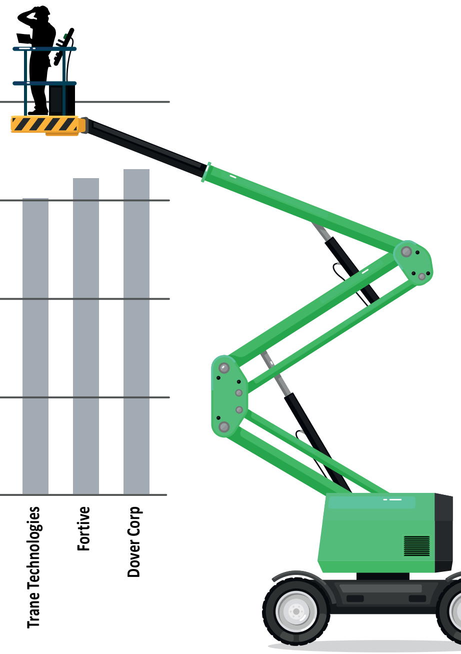


1 Maximum bonus + maximum long-term incentive opportunity [valued on the basis of PSU equivalents]. 2 Base salary + target bonus + fair value of long-term incentives.

Chief executive target total remuneration[1]: Ashtead vs US comparators

[market data as available at 31 May 2024]





1 Target total remuneration = base salary + target annual bonus + long-term incentive fair value

shareholders at the company's Annual General Meeting (AGM) in September 2024.

We reached out to EOS to discuss their vote recommendation intentions and they responded that they'd be recommending a vote against the company's proposed remuneration policy and amendments to the LTIP, due to concerns about the scale of the proposed variable pay opportunity which significantly exceeded UK peer comparisons. In addition, EOS recommended a vote against the chair of the appointments committee due to concerns about a lack of diversity below the board level.

We joined a call with the CEO of Ashtead ahead of the AGM to discuss these issues. We didn't receive any indication that the company intended to take specific action to address its gender diversity issues. Ashtead's rationale for the proposed remuneration policy and LTIP amendments however, centred on its aim to bring remuneration more into line with relevant competitive market norms in the markets in which the group competes for talent and to reflect the CEO's experience and strong track record over the last five years.

While Ashtead is listed in the UK, we noted that Ashtead is somewhat unusual in that the vast majority of its operations and workforce are located in the US. Given this and the fact the CEO is also US-based, we considered US peers to provide a more appropriate comparison.

Top-left we can see that, from a UK perspective, Ashtead pays a relatively low salary but large overall package. Using the US market norms as the comparator suggests the salary is close to median, while the overall package is lower quartile.

To give further context, the chart above shows the unchanged Ashtead target total remuneration (furthest left green bar) as well as the newly proposed one (the second green bar from the left). With the new proposal, target total remuneration is "only" approaching lower quartile versus Ashtead's median market capitalisation. This compares to the most obvious direct peer (United Rentals) who are close to median.

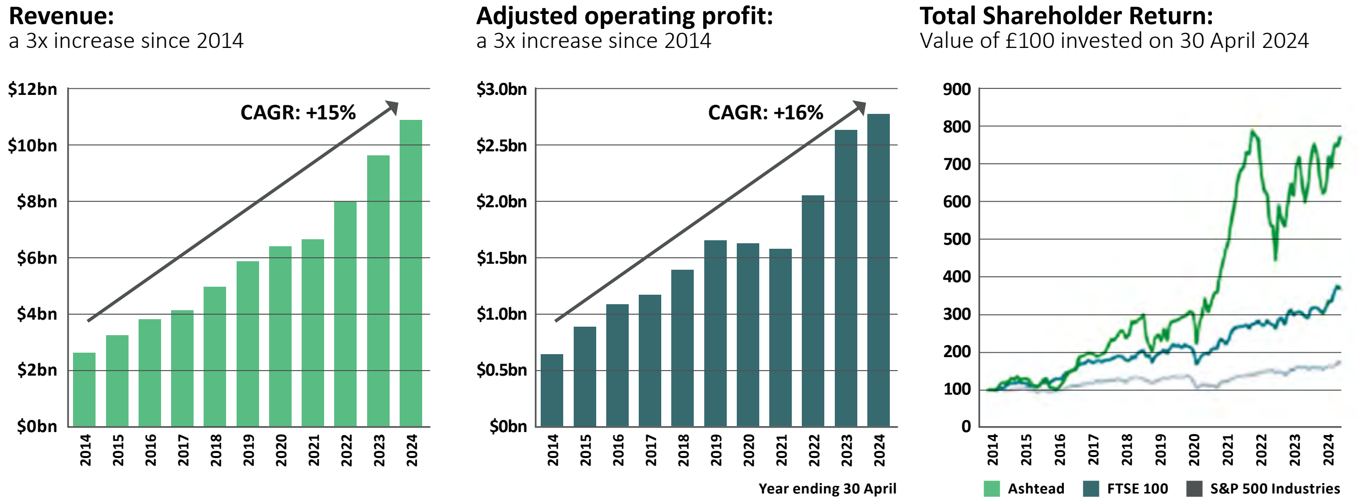
We also noted that this package only pays in full if targets are met and delivering on these targets means management are aligned with the interests of shareholders.

Voting Action and Outcome

We elected to vote in favour of the remuneration policy, but against the re-election of the chair of the appointment's committee.

At the AGM on 4 September 2024, all the resolutions put to shareholders were passed. However, in accordance with the UK Corporate Governance Code, the level of shareholder dissent (>20%) required the company to make an explanatory statement in its AGM results announcement. Ashtead committed to engage with shareholders in respect of the implementation of its remuneration policy and publish an update within six months.

A strong and sustained performance track record



On 10 December, Ashtead announced plans to move its primary listing to New York in the next 12-18 months, while retaining a secondary UK listing in the International Companies segment. The board said it will discuss the proposal with shareholders before putting forward a formal resolution for approval.

Reflection

In alignment with LPF voting policy, we conducted our own research into potentially controversial proposals and voted accordingly. The reason we "disagreed" with EOS's recommendation on Ashtead's remuneration policy and LTIP was on the scale of excess after adjusting for regional market norms.

We consider executive compensation structures as a critical governance tool for aligning the activities of management with a company's purpose, strategy and incentivising long-term value creation, including wider social and environmental outcomes. Where we consider there to be a disconnect between pay and the broader stakeholder experience, we're prepared to vote against remuneration policies and/or the director of the remuneration committee: 25% of our votes against management in 2023 were on remuneration concerns.

We think very highly of Ashtead's current CEO, Brendan Horgan. We strongly believe that longevity of senior management is important to the success of most businesses. Brendan is only the company's second CEO since we invested in early 2012, and he was an internal appointment. A snippet of their recent track record is shown above.

We'll continue to engage with the company, particularly on the proposed listing change.

Stewart Piotrowicz
Portfolio Manager

LOTHIAN
PENSION FUND

If you'd like more information on our ESG activities, please visit our website www.lpf.org.uk.

PO Box 24158, Edinburgh, EH3 1GY

Phone: 0131 529 4638
Email: pensions@lpf.org.uk
Web: www.lpf.org.uk