From the Commonwealth Superannuation Corporation, August 2021

Sustainable investment opportunities that contribute to a better retirement and future

At the Commonwealth Superannuation Corporation, we focus on sustainable investment opportunities that contribute to a better future for the members of all of the superannuation schemes we manage, their retirement and the world.

Because one person's ethics may differ from another's, we take an **objective** approach to consider whether investment opportunities will grow savings in the long-term and whether there are any risks from environmental, social or governance (ESG) factors that can impact the long-term value of the investment.

A closer look at our investment approach from an ESG perspective

We believe that the most successful companies are those that consider all potential strategic influences on the long-term sustainability of their business, not just the short-term operational drivers of current profitability. We are focused on genuine sustainable impact, rather than simplistic divestment. There are many facets involved in managing ESG risks, because they are interdependent. We believe incremental, consistent changes are more effective in supporting robust and smooth transitions to a more sustainable future.

Our investment approach is aligned with the Paris Agreement which seeks to limit the increase in the global temperature to 'well below 2 degrees C' above pre-industrial levels. This is also consistent with the Australian Government's ratification of the agreement in 2016.

Some examples of our investments that are aligned with the United Nations' Sustainable Development Goals (SDGs) framework, include:

- **Aimmune Peanut Allergy Therapy**: Aimmune Therapeutics' research priority has been to help patients struggling with peanut allergies, and in February 2020, their groundbreaking work was approved by the Food and Drug Administration in the United States. This made it the first approved therapy for any form of food allergy. By seeking out responsible investments and championing businesses from the beginning, CSC has supported a life-changing discovery.
- **Supporting the COVID frontline:** We invest in private healthcare companies that are providing a range of critical healthcare services to support the pandemic frontline such as clinics, pathology, aged care and pharmaceuticals.
- **Modern Slavery:** We have been working with our investment managers and service providers in the last few years, to understand how they identify, manage and monitor risks of modern slavery in their supply chain. This has culminated in CSC's Modern Slavery Statement which has been published online.
- **GEMS Education:** Our investment in GEMS Education, the world's largest K-12 schools group, has generated positive social externalities globally, as well as created financial value for customers. GEMS educates more than 155,000 students across 80+ schools located in the UAE, Saudi Arabia and Europe.

How do we manage climate investment risk?

We actively assess ways to mitigate the risks, and identify opportunities in supporting companies to transition to a low carbon economy. We manage climate investment risk in three main ways:

- Proactively investing in renewable energy opportunities
- Supporting robust transitions away from coal, and;
- Improving our net portfolio carbon footprint over time.

Climate change is risk that we take seriously, in conjunction with all the risks 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 exposure to environmental, social and governance (ESG), technology, resourcing and financial risks. We recognise three investment risks associated with climate change:

- **Transition risks**, which arise 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,** which 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,** which stems from the potential for litigation if entities and governing bodies do not adequately consider or

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

How do we invest in renewables?

We have been, and will continue to, invest in renewable energy, primarily, but not exclusively, through our private asset portfolio. We have more than $1,097 million invested in high quality private and public assets, including wind farms, waste management infrastructure projects, and renewable energy. These investments reduce CSC's portfolio carbon emissions by over 427,000 tonnes of CO2 annum, compared to having this money invested passively to meet a similar level of energy demand (for the financial year to 30 June 2021).

In September 2015, we acquired a 50% ownership on Macarthur Wind Farm, the largest windfarm in the Southern Hemisphere. In 2020, our share of Macarthur's generation avoided the need to produce c.540,000 tonnes of CO2. For the period to 30 June 2021, this asset has returned 13.5% to our investors, with a low risk profile.

Supporting a robust transition away from coal

The reality is that Australia, and the rest of the world, still require coal to operate, but this need is reducing. To ensure this phasing out process is as 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.

We believe there is value in engaging with companies both directly, by dialogue, and indirectly, by voting all our stock. Our ability to do this derives from an investment governance process that began back in 2003; this resulted in our efforts being recognised by the United Nations in the form of an inaugural innovation award for impactful efforts on sustainability.

Over many decades, our 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 it can make through:

- **Divestments as a last resort.** We use divestments only when engagement with companies cannot reduce the risks to the long-term viability of the business (eg, undiversified companies like tobacco companies, or those that derive more than 70% of their income from thermal coal production or extraction) and/or because the activity is contrary to Australian government regulations, sanctions, treaties or conventions (eg, cluster munition manufacture).
- **Active engagement.** We engage both directly and indirectly with all its 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.** We are active participants in multiple asset owner forums, Room17 (SDG) project groups, etc.
- **Integration of all risks** into our formal investment processes and decision-making frameworks.

How does our governance support this?

The CSC Board of Directors has, and continues to have, detailed discussions about improving how climate change risk can be genuinely managed, not just in our investment portfolio, but also within our own organisation. To that end, it is developing a formalised organisation wide climate risk management policy, some of which has already been implemented for some time.

With respect to the investment portfolio, this risk management has been in place for a very long time and well before the most recent acceleration in awareness around long-term, common risks. 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. CSC is preparing its portfolios to manage the risks and opportunities to its customers' savings, should any of the many possible climate scenarios eventuate.
- Dedicating physical expenditure budgets within each of its directly-held property assets to minimise physical climate risks. CSC invests in global benchmarks to support and guide those budgets and their focus.
- Actively evaluating renewable energy and other sustainable opportunities and providing 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.

- Divesting from undiversified companies that derive 70% or more of their revenue from thermal coal extraction/production.

How do our efforts compare with global best practice?

CSC has received global recognition of our pioneering work in sustainability:

- We were a recipient of the United Nations' Principles of Responsible Investing Royal Award for excellence in sustainability in October 2003.
- A top 20% ranking globally in both the biennial 2017 and 2019 Bretton Woods II Most Responsible Asset Allocators Initiative (RAAI).
- We were awarded the 2018 AsianInvestor Institutional Excellence Awards in the category of Governance, in 2019, the category of Investment Innovation, and in 2020, the categories of ESG engagement and COVID response.

Furthermore, 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. We are also a signatory to the Montreal Carbon Pledge, which is supported by the Principles for Responsible Investment. Under the pledge, we commit to measuring and disclosing, on at least an annual basis, the carbon footprint of our public market equities portfolio.

For more information, please visit www.csc.gov.au