

INVESTMENTS AND TODAY'S CLIMATE CHALLENGES.

TCFD report - all you need to know!

What is the company managing your investments doing about today's climate challenge? What are their future plans to reduce their carbon emissions? In the UK, investment firms are required to publicly disclose actions taken and climate-related financial information consistent with the UK financial regulator's requirements.

The board of BNY Mellon Fund Managers Ltd (BNYMFM), which govern our UK-domiciled funds, is responsible for publishing this information. The regulatory report - called TCFD (Task Force for Climate-related Disclosures) – outlines:

- Governance around climate-related risks and opportunities.
- Actual and potential impact of climate change on the company's business and strategy.
- How such risks and opportunities are identified and quantified.

The report looks to show that financially material climate-related considerations are integrated across the business. This means from decision-making and business processes to the fund schemes it operates. It also examines the risks – and opportunities – that arise from climate issues on its fund offerings.

The report incorporates climate-related risks from BNYMFM's underlying investment firm partners – such as Newton – as well as its parent company, BNY Mellon. The latter publishes its analysis in an annual Sustainability report, which can be found here: www.bnymellon.com.

THE BASICS OF ANALYSIS

WHAT IS THE TCFD?

The aim of Task Force for Climate-related Disclosures is to encourage more informed investment decisions. The point is to provide specific information for people to understand the carbon-related risks of the assets in which they are investing.

It requires in depth data and analysis in specific areas:

Entity-level emissions: This covers both direct (Scope 1) and indirect (Scope 2) carbon emitters in a company. For example, Scope 1 covers things like the carbon emitted by office heating and lighting. Scope 2 covers the energy bought to heat and light the building.

Scope 3 emissions are more complex still. At an entity level companies need to report carbon emissions like business travel. Yet Scope 3 also covers investments. Each fund invests in a wide range of different companies or assets – some as few as 30 and others, as many as 100. What are the carbon emissions of these individual holdings? What is their exposure to climate-related risks?

THE DATA

Carbon metrics in the TCFD report include listed equities and corporate bonds. These account for the majority of assets in the 48 funds under BNYMFM's governance. Others are currently excluded from all calculations due to availability of data. It is the latter that is one of the weaknesses identified in the 2023 TCFD report for BNYMFM.

Emissions data is frequently based on estimates or proxy data. It can provide an imperfect view of portfolio exposures or risks. Data can also change materially from one year to the next, as coverage improves, or estimation methods change.

Today, BNYMFM is dependent on the quality of emissions data on public investments from an external provider, MSCI.

OUR BUSINESS

BNYMFM is at an early stage of understanding how climate-related issues affect the various aspects of its business. This means both its own strategy and planning as well as the funds it operates.

BNYMFM is looking to enhance integration of climate-related risks and opportunities into its broader business planning. Future TCFD reports should feature this progress. Through 2024, BNYMFM is undertaking a review of its operational emissions, working with its parent company BNY Mellon. It has also set up a new committee – the Responsible Investment Oversight Committee – which reports to the BNYMFM board.

In considering its approach to climate, it notes the most material areas for the business are areas like Scope 3 emissions. These are a result of activities in the UK marketing and distribution division that result in carbon emissions. However, material risks (as well as opportunities) identified relate to indirect “financed emissions.” These come from the companies held the underlying investments within each of the funds.

OUR FUNDS

How do we analyse the funds for climate impact? The investment managers (such as Newton, Insight and Walter Scott) running the funds within BNYMFM has their own TCFD reports. Each conducts their own analysis companies in which they invest within the funds.

Additionally, BNYMFM uses MSCI research to supplement this data. This research looks at possible financial loss under different scenarios related to climate. These risks fall into two main camps – physical and transition. The first looks at how a company – held within a fund – may be affected by damage or disruption resulting from a climate change event like a flood or wildfire.

Transition risks are harder to quantify as it is the impact associated with the move to a low carbon or net zero economy. Much of this is visible in how a company adapts to the policy, legal, regulatory and market pressure for change to a “greener” world. For example, some companies may lose business in the face of changing consumer demands; for others they may experience reputational damage from what they may – or may not – be doing.

However, this is not necessarily a negative measure either. Other companies may benefit from the transition to a greener economy. Climate opportunities range from renewable energy, green infrastructure, technological innovation, sustainable financing solutions and climate resilience solutions. These opportunities solve for climate mitigation and adaptation issues.

The 2023 report notes sectors such as materials, utilities and energy are the highest emitters across the MFM funds. This is no different to the highest emitting sectors in the MSCI All Countries World index.

Under a two-degree temperature rise scenario, transition risks will likely have the greater financial impact on the companies held in the funds. If global temperatures were to rise by three degrees, physical risk to the companies held in the BNYMFM funds is much higher (although still less than the average company in the MSCI AC World index).

One exception to this is the sustainable funds in the BNYMFM range, where the physical risks under a three-degree scenario are less.

FUTURE ACTIVITIES

Over the course of the coming year, BNYMFM intends to review funds where climate-related risks look high. They will explore steps they and the respective managers can take to improve their climate profiles.

Additionally, BNYMFM will look at broadening client exposure to its sustainable fund range.

From a business perspective the EMEA division of BNY Mellon Investment Management is to formally incorporate climate risk into its Risk and Controls framework. A review of the BNYMFM board’s executive committees will take place in 2024 to ensure climate-related risks are adequately covered across the business.

BNYMFM also intends to build on its relationships with its underlying investment partners, such as Insight Investments, as well as its parent company BNY Mellon, to ensure broader application of data.

Please click [here](#) to read BNYMFM's first published **Task Force on Climate-Related Disclosures** report.

IMPORTANT INFORMATION

Investment involves risk. The value of investments and the income from them can fall as well as rise and investors may not get back the original amount invested.

Forward looking statements

This report may contain forward-looking statements with respect to the financial condition, performance and position, strategy, results of operations and businesses. Such statements and forecasts involve risk and uncertainty and may not be a reliable indicator of future performance. Forward-looking statements are based on numerous assumptions, risks, and uncertainties, which may change over time and speak only as of the date they are made. Actual results could differ materially from those anticipated in forward-looking statements and future results could differ materially from historical performance. Nothing in this report should be construed as a forecast, estimate or projection of future financial performance and the Firm assumes no duty to and do not undertake to update forward-looking statements.

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Caution about climate-related metrics and data required for climate reporting

There are many significant uncertainties, assumptions and judgements underlying climate metrics that limit the extent to which climate metrics are reliable. Climate metrics and data (including data required to report climate-related risks and opportunities and their potential impacts), the models, scenarios used to create them and the measurement technologies, analytical methodologies and services that support them are at a relatively early stage and developing. Accordingly, there are limitations with respect to data and analysis techniques, which should be considered. Scenarios are not forecasts and are not predictions of future outcomes. Like any modelling, the further out the projection, the greater the uncertainties.

MSCI climate-related metrics provided in this report may not fully reflect future economic reality. This report contains certain non-financial metrics such as Climate Value-at-Risk metrics that are subject to measurement uncertainties resulting from limitations inherent in the nature of the metric and should not be construed to represent any belief regarding materiality or financial impact. Climate Value-at-Risk is being provided in this report for the purposes of complying with applicable reporting requirements.

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