Rathbones Group Plc

Our approach to investment in fossil fuels, including thermal coal

June 2023

Our approach to investment in fossil fuels, including thermal coal

The Intergovernmental Panel on Climate Change (IPCC) has warned that to limit global warming to 1.5°C above pre-industrial levels, the world's carbon emissions need to halve by 2030 and reach net zero by 2050. Rathbones Group Plc (Rathbones) aims to contribute to the move to a net zero economy while delivering on our clients' investment objectives. As stewards and allocators of capital, we recognise that we have a responsibility to understand and take action to minimise the potential implications of climate change on the assets we manage on behalf of clients. We support the aims of the Paris Agreement and have made a Group-wide commitment to achieving a transition to net zero by 2050 or sooner. To support this, we have set near-term targets, validated by the Science Based Targets Initiative (SBTi), to reduce emissions including those embedded in portfolio holdings.

With fossil fuels envisaged to play a role in many plausible net zero scenarios and transition pathways, we see carefully considered investment in certain fossil fuel companies as compatible with our aim of achieving net zero emissions.[1] Our investment in fossil fuel companies is guided by our four responsible investment pillars:

1. Engagement with consequences

With high carbon emitting companies, we prioritise engagement, both directly and through investor organisations. We monitor fossil fuel companies' energy transition commitments and track progress using appropriate metrics.[2] Through shareholder engagement, we encourage the development of robust and credible net zero decarbonisation strategies in line with the 1.5°C goal, and push companies to enhance corporate disclosure and board accountability. Over time, the targets, metrics and milestones to which we hold fossil fuel companies accountable will evolve and become more exacting. We recognise the importance of engagement in influencing the energy transition, and we may reduce or exit our holdings in investments that present material and inadequately managed climate risk, particularly those that have failed to adequately respond over time to our engagement efforts.

2. Voting with purpose

We actively vote on our holdings in line with our responsible investment commitments. This may involve voting against management in some instances. Our bespoke voting policy includes specific climate-related elements, including promoting net zero carbon strategies, voting against climate transition plans which are not aligned with the science in sectors with high levels of carbon emissions, supporting the election of directors with climate-related experience and, where relevant, voting against directors and boards not managing climate risk adequately. We also support ESG shareholder resolutions calling for improved reporting on net zero transition plans or climate action.

3. Integration of environmental, social and governance (ESG) factors

We consider material ESG and climate factors in the evaluation of investments to help identify opportunities and risks. For example, during a market transition away from fossil fuels, an oil and gas company might carry the risk that its resources lose their value and cannot be recouped or exploited due to regulatory rulings or policy changes on climate change. Through our research process, which includes ESG monitoring across sectors and asset classes, we aim to identify sound investments in companies that provide clean energy and the requisite new infrastructure, enabling us to support the clean energy transition away from fossil fuels.

4. Transparency

We actively report on our progress towards our net zero targets, including through annual reports to the Net Zero Asset Management initiative on the percentage of our assets-under-management that are aligned with net zero. We also provide disclosures on our Scope 1 and 2 and material Scope 3 emissions through an **annual Taskforce on Climate-Related Financial Disclosures (TCFD) report**.[3]

Phasing out financial support to thermal coal

Thermal coal used in coal fired power plants produces a significant proportion of global electricity, making coal a leading contributor to climate change. Relative to other fossil fuels, the combustion of coal adds significantly more carbon dioxide into the atmosphere per unit of heat energy generated.[4] For thermal coal specifically, cleaner energy substitutes for power generation are available today (renewables, gas and nuclear), which means that thermal coal does not present a long-term viable fuel source in a world that needs to reduce carbon emissions significantly.

We have therefore established a policy setting out a phased approach to reducing investment in companies involved in the thermal coal sector (including companies engaged in mining, power generation or providing support to the thermal coal industry). Our goal is to phase out financial support to thermal coal companies by 2030 by limiting or ceasing investment in public listed equities, corporate bonds and direct private equity when issued by companies that breach specific thermal coal thresholds and criteria (see next paragraph).[5] Where we hold investments in these companies, we will heighten our engagement and voting activities, in line with our four responsible investment pillars, explained above.

Our thermal coal thresholds are set against parameters such as the company's revenue exposure to thermal coal, its annual thermal coal production or power production from thermal coal, and whether the company is expanding its coal mining or coal power capabilities. In addition, we will consider whether the company has published a robust and credible net zero plan and evaluate the quality of that commitment and progress against it using the metrics referenced in footnote 2. Within each phase of our phase-out plan, different thresholds will be set for each parameter. Subject to data availability, we will screen companies within our investable universe against these thresholds and take appropriate action to meet our commitment to phase out financial support to thermal coal companies.

Phase 1

In this initial stage, we will focus on companies that mine thermal coal and generate power from thermal coal. Using internal and external research, we will initially screen our investable universe to identify mining and power generation companies which derive over 10% of their revenue from thermal coal. These companies will then be scored against the Phase 1 thresholds using insights from third-party data providers, our engagement activities and internal research. Companies which breach our thresholds will be designated as excluded investments and we will prevent new investment in them. Where we have existing holdings in excluded thermal coal companies, we will continue to encourage those companies to establish science-based targets and transition plans and, where the ESG risk is unlikely to be resolved, may initiate a divestment process.

Phase 2

The thresholds on our thermal coal scorecard in respect of coal mining and power generation companies tighten over time. We will set these thresholds to align with the IPCC's 1.5°C scenario.

Over the longer term, in addition to limiting our investment in thermal coal companies, we intend to escalate our engagement with companies that provide material and/or financial support to such companies to ensure that they too are taking steps towards achieving net zero emissions.

Rathbones has discretionary authority over most but not all clients' assets invested with us. We may vary the requirement to adhere to specific milestones in our phase-out plan if, in our judgement, this approach is inconsistent with regulation, a specific mandate or strategy (including the investment objectives and investment guidelines of the client or fund).

Our thermal coal phase-out policy applies to Rathbones as a whole and includes all existing business segments. We will review the suitability of our approach on an ongoing basis.

For more information regarding our approach to responsible investment, please visit our website.

[1] Rathbones primarily has exposure to fossil fuels through direct investment in the equities and fixed income securities of oil and gas companies, companies that operate in the energy sector, and providers of services, technology and equipment to the oil industry or the coal mining sector. Fossil fuel exposure may occur via companies which use it as a raw material (e.g. the chemicals sector) or as a key fuel source which is difficult to substitute (e.g. the steel and cement industries). Rathbones also has indirect exposure through investing in banks, which may lend to fossil fuel projects, and insurance and asset management businesses, which may have investments in fossil fuel companies and projects. We may also have exposure to fossil fuels indirectly through collective investments or index-based investments such as exchange traded funds or structured products.

[2] Metrics are qualitative and quantitative, spanning governance, strategy, risk management / capital allocation and targets.

[3] Scope 1, 2 and 3 emissions refer to the categorisation of the different kinds of carbon emissions a company creates in its own operations, and in its wider value chain. Scope 1 covers direct greenhouse gas emissions made, for example, while running vehicles; Scope 2 emissions are those created indirectly, such as through the electricity or energy which is being produced on its behalf and which it buys for heating and cooling its buildings. Scope 3 emissions include all the emissions that the organisation is indirectly responsible for up and down its value chain.

[4] Thermal coal emits almost twice as much CO2 per unit of energy vs natural gas and around a third more than diesel and gasoline according to the International Energy Agency. As a result, accelerating efforts to phase down unabated coal power in the energy system now forms part of global agreements on climate change. See: United Nations Framework Convention on Climate Change, Addendum to the Report of the Conference of the Parties serving as the meeting of the Parties to the Paris Agreement on its second session, held in Glasgow from 31 October to 12 November 2021, (published on 2 March 2022).

[5] Where we hold collective investments, index trackers and ETFs we cannot directly influence the constituent holdings. However, we conduct detailed due diligence and can engage with the asset managers responsible for managing these portfolios to understand their policies and processes for managing and mitigating climate risk.

Important information

This document is published by Rathbones Group Plc and does not constitute a solicitation, nor a personal recommendation for the purchase or sale of any investment. No consideration has been given to the particular investment objectives, financial situations or particular needs of any recipient and you should take appropriate professional advice before acting.

Rathbones Investment Management will not, by virtue of distribution of this document, be responsible to any other person for providing the protections afforded to customers or for advising on any investment.

Rathbones Group Plc, and its associated companies, directors, representatives, employees and clients may have positions in, be materially interested in or have provided advice or investment services in relation to the investments mentioned or related investments and may from time to time purchase or dispose of any such securities. Neither Rathbones Group Plc nor any associated company, director, representative or employee accepts any liability for any direct or consequential loss arising from the use of information contained in this document, provided that nothing in this document shall exclude or restrict any duty or liability which Rathbones Group Plc may have to its customers under the UK regulatory system.

We are covered by the Financial Services Compensation Scheme. The FSCS can pay compensation to investors if a bank is unable to meet its financial obligations. For further information (including the amounts covered and the eligibility to claim) please refer to the FSCS website www.fscs.org.uk or call 020 7892 7300 or 0800 678 1100.

Unless otherwise stated, the information in this document was valid as at 28 February 2023. Rathbones Group Plc is independently owned, is the sole shareholder in each of its subsidiary businesses and is listed on the London Stock Exchange.

Rathbones is a trading name of Rathbones Group Plc. Rathbones Investment Management Limited is authorised by the Prudential Regulation Authority and regulated by the Financial Conduct Authority and the Prudential Regulation Authority. Registered office: Port of Liverpool Building, Pier Head, Liverpool L3 1NW. Registered in England No. 01448919. Head office: 8 Finsbury Circus, London EC2M 7AZ.

Rathbone Greenbank Investments is a trading name of Rathbones Investment Management Limited.

Rathbone Unit Trust Management Limited is authorised and regulated by the Financial Conduct Authority. Registered office: 8 Finsbury Circus, London EC2M 7AZ. Registered in England No. 02376568.

Rathbones Investment Management and Rathbone Unit Trust Management are wholly owned subsidiaries of Rathbones Group Plc.

Rathbones Investment Management International is the Registered Business Name of Rathbones Investment Management International Limited which is regulated by the Jersey Financial Services Commission. Registered office: 26 Esplanade, St. Helier, Jersey JE1 2RB. Company Registration No. 50503. Rathbones Investment Management International Limited is not authorised or regulated by the Prudential Regulation Authority or the Financial Conduct Authority in the UK. Rathbones Investment Management International Limited is not subject to the provisions of the UK Financial Services and Markets Act 2000 and the Financial Services Act 2012; and, investors entering into investment agreements with Rathbones Investment Management International Limited will not have the protections afforded by those Acts or the rules and regulations made under them, including the UK Financial Services Compensation Scheme. This document is not intended as an offer or solicitation for the purchase or sale of any financial instrument by Rathbones Investment Management International Limited.

The information and opinions expressed herein are considered valid at publication, but are subject to change without notice and their accuracy and completeness cannot be guaranteed. No part of this document may be reproduced in any manner without prior permission.

Rathbones

rathbones.com
@RathbonesGroup
Rathbones Group Plc
@Rathbonesplc