EVENLODE

INVESTMENTS FOR LIFE

Evenlode Investment
Net Zero Roadmap 2024

evenlodeinvestment.com

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INTRODUCTION

Evenlode Investment's fiduciary duty is to preserve and enhance the value of our clients' assets through robust analysis, long-term engagement and risk management. We believe the primary role of risk management is to safeguard clients' capital over the long term.

We recognise that the effects of climate change and the transition to a net-zero economy can create significant financial risks for companies, investors, and the financial system. Evenlode may be affected by climate risks either directly or indirectly through our relationships with customers and the macro-impacts on the economies we serve, potentially resulting in both financial and non-financial consequences.

We consider climate change and the transition to a low carbon economy to be one of the biggest systemic risks and challenges facing society, the global economy and our investee companies today. Rapid global decarbonisation in line with 1.5°C is needed to avoid the worst effect of climate change. To manage climate-related risk in our portfolios and contribute to this global imperative, Evenlode joined the Net Zero Asset Managers (NZAM) initiative[1] in June 2021 and committed to reaching net zero across our investment portfolios by 2050 or sooner, across 100% of our investments. Additionally, Evenlode as a business has committed to be net zero across all geenhouse gases, excluding financed emissions, by the end of 2030. This is an ambitious target; however we feel it is a realistic one. In saying that, our actions will inevitably involve the use of offsets, as certain categories of transport, notably air travel, will certainly not be decarbonised by that time. However, we are committed to ensuring that offsets do not exceed 5-10% of our overall emissions, focusing instead on direct emission reduction strategies.

Following the Paris Aligned Investment Initiative's (PAII) Net Zero Investment Framework (NZIF)[2] - one of the three methodologies endorsed by NZAM - we are setting net zero-aligned engagement, portfolio alignment and decarbonisation targets. To achieve these targets, we will need all the tools available to us as asset managers. This includes using direct and collective engagement with investee companies, regulators and policy makers, and using our voting rights to vote on resolutions at company meetings to encourage more action on climate change. We will need to structure our voting, engagement and escalation in the most effective way in support of our net zero stewardship and engagement strategy.

We would like to emphasise our commitment to allocating 100% of our assets under management towards our net zero ambition. At Evenlode, we have always believed in long-termism, alignment, and sustainability. Our first Net Zero Roadmap is a significant milestone in our journey to achieve sustainable returns for our clients whilst also running a sustainable business, over the long term.

In the following sections, we will present our Net Zero Roadmap, with a particular emphasis on our financed emissions as they make up a large proportion of our negative externalities as a business. Our goal is to align our entire business model with the latest and most ambitious climate science recommendations. We believe that through active engagement and a thoughtful investment decision-making process, which considers climate-related risks alongside fundamental business risks, we can have the greatest impact on the financial services sector and society.

Achieving net zero emissions will require changes across every sector and geography of the economy. The radical and systemic transformations needed cannot be achieved by a single organisation or industry alone. However, we believe in the power of dialogue and active ownership. As a long-term investor with a strong focus on stewardship and effective engagement, we feel that we can influence our investee companies towards more effective transition plans and more sustainable practices. We are conscious of the uncertainties the global economy can bring, so we have avoided long-term forecasts. However, through this report, we aim to provide clarity to our internal and external stakeholders on the actions we will take to decarbonise our portfolios up to 2030, with the Stewardship team and fund managers regularly reviewing these targets on an annual basis.

1 NZAM is an international group of asset managers committed to supporting the goal of net zero greenhouse gas emissions (GHG) by 2050 or sooner, in line with global efforts to limit warming to 1.5°C. This important initiative was launched in December 2020 with an initial group of 30 signatories. See more here: https://www.netzeroassetmanagers.org/

2 Net Zero Investment Framework Implementation Guide, March 2021. https://www.parisalignedinvestment.org/media/2021/03/PAII-Net-Zero-Investment-Framework_Implementation-Guide.pdf

NET ZERO TARGETS

Whilst the Evenlode Funds do not have a sustainability objective, we have committed to reach net zero greenhouse gas (GHG) emissions across 100% of our investments in Material Investee Companies by 2050, or sooner, to support providing long-term risk-adjusted returns.

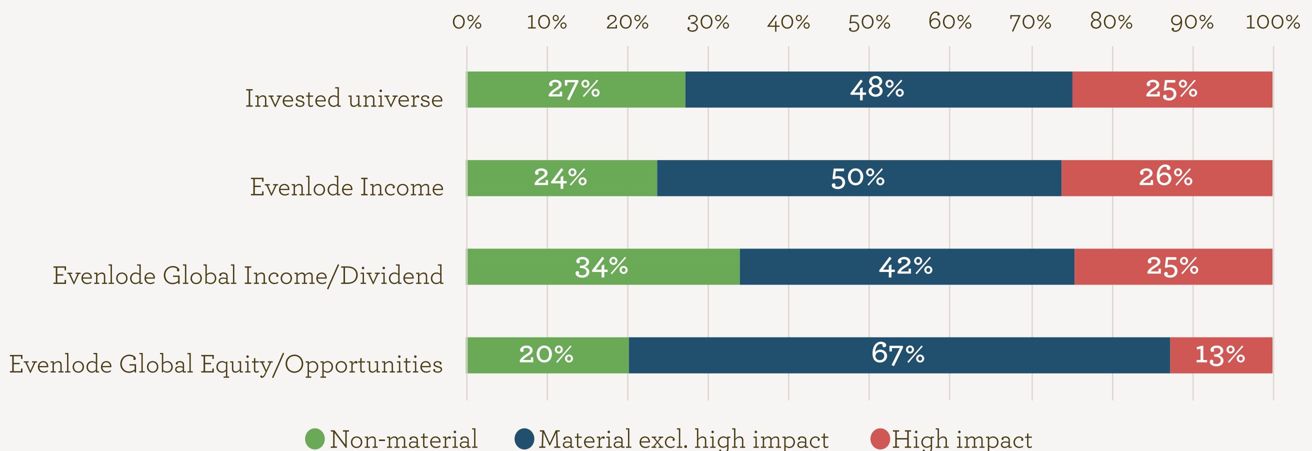
Material Investee Companies are defined as companies operating in NACE (a European standard classification system) categories A-H and J-L. This approach is consistent with the NZIF.

The interim targets pursued by the Investment Manager to achieve the net zero greenhouse gas emissions target include:

- 100% of financed emissions in material sectors to be aligned, achieving net zero or under direct or collective engagement by the end of 2022. This target was met in September 2022.
- 50% of our assets under management (AUM) in material sectors to be aligning, aligned or achieving net zero by 2025, and 100% by 2030.
- 100% of AUM in material sectors to be net zero or aligned by 2040.
- 51.6% reduction in emissions per £10k invested across scopes 1, 2 and 3 by 2030 (using the baseline of end 2020).

As a reminder, 'financed emissions' refer to the total GHG emissions financed by the portfolio, expressed in metric tonnes of carbon dioxide equivalent (tCO_2e). It provides a broader view of the portfolio's impact by considering the total associated emissions, rather than normalising to a specific investment size. We use the definition provided in the NZIF for *companies in material sectors and high impact companies*, which are a subgroup of companies in material sectors.

At the end of 2023, 64 companies or 73% of our portfolio companies across all funds were considered material and/or high impact, and 17 companies or 25% of portfolio companies were considered high impact. Definitions of *aligning, aligned or achieving net zero* as well as the alignment criteria underlying these classifications are provided in the Appendix (page 19). Definitions of Scope 1, Scope 2 and Scope 3 can be found on page 15.



PROGRESS

2022 ENGAGEMENT TARGET

In August 2022, we released our first Net Zero Engagement and Voting Policy, reaffirming our view that climate change and the shift to a low-carbon economy represent critical systemic risks and challenges for society, the global economy, and our investee companies. Our commitment to the imperative of rapid global decarbonisation in line with the 1.5°C target remains unchanged and forms a key part of our stewardship strategy over the coming months and years.

Since setting our baseline targets, we made significant progress. Firstly, we achieved our short-term goal by engaging with 63 companies or 100% of our financed emissions in material sectors, by the end of 2022. We categorised companies based on their status in the net-zero journey, classifying them as not aligned, committed, aligning, aligned, or achieving net zero under the NZIF. We provided clear explanations for these classifications and offered personalised feedback to each company, outlining the steps needed to advance to a higher net-zero category. Our engagement target for the year was successfully met. However, this did not mean we stopped engaging. Last year, we focused on companies that were lagging on their transition plans. Specifically, we engaged with companies that were either 'not aligned,' 'committed to align,' or 'material/high impact' and not progressing at a reasonable rate. As a result, we engaged with 43 companies on their net zero transition plans last year (2023).

EXAMPLE – HEINEKEN

In 2022, we contacted Heineken to address our concerns regarding the company's climate commitments. Our baseline assessment indicated that it was only "Committed to Aligning." We requested that the company set a 2025 emission reduction target, including at least 67% of scope 3 emissions, within the next 12 months. We also sought clarification on the proportion of the net zero target to be achieved through emission reductions.

Heineken operates in a sector with significant climate-related risks and has a substantial impact on the climate. In 2023, we reached out again to emphasise the importance of a clear and robust Net Zero strategy. We recommended that Heineken publish a detailed action plan, including information on renewable energy procurement, the use of offsets, carbon pricing, and future capital allocation plans aligned with climate goals. We received a positive acknowledgement, with the IR team thanking us for the feedback. Although it's difficult to attribute our engagement efforts to the change, the letter yielded positive results: Heineken improved its transition plan, providing more detailed information. After two years of discussions, Heineken attained the "Aligning" classification under the NZIF, reflecting significant progress in their climate strategy.

Engagement Pyramid

ENGAGEMENT OBJECTIVES

Tier	Objective
TIER 4	**Achieving Net Zero target** and sustaining it.
TIER 3	**Becoming aligned:** emission performance in line with targets, audit of emissions.
	For high impact companies also: full decarbonisation strategy, capital alignment, green revenue disclosure, details of offsets if applicable.
TIER 2	**Becoming aligning:** setting science-based short and medium-term targets in line with 1.5°C covering at least 67% of scope 3 and disclosure of at least 90% of relevant emissions.
	For high impact companies also: action plan for how to achieve these targets.
TIER 1	**Becoming committed:** setting a long-term net zero by 2050 commitments covering at least 95% of scope 1 and 2 and 90% of scope 3.

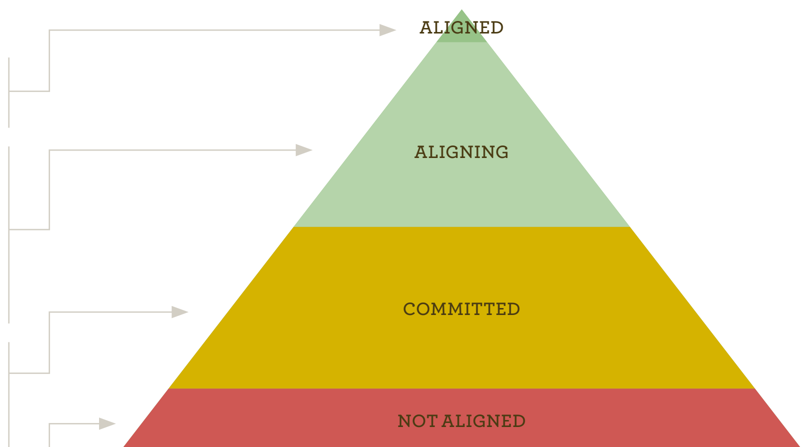


Figure 1. Engagement pyramid.

Net zero alignment of companies in material sectors as of 31 December 2023 (% of AUM)

- Achieving net zero (0%)
- Aligned (7.4%)
- Aligning (41.7%)
- Committed to aligning (36.5%)
- *Not aligned (14.4%)

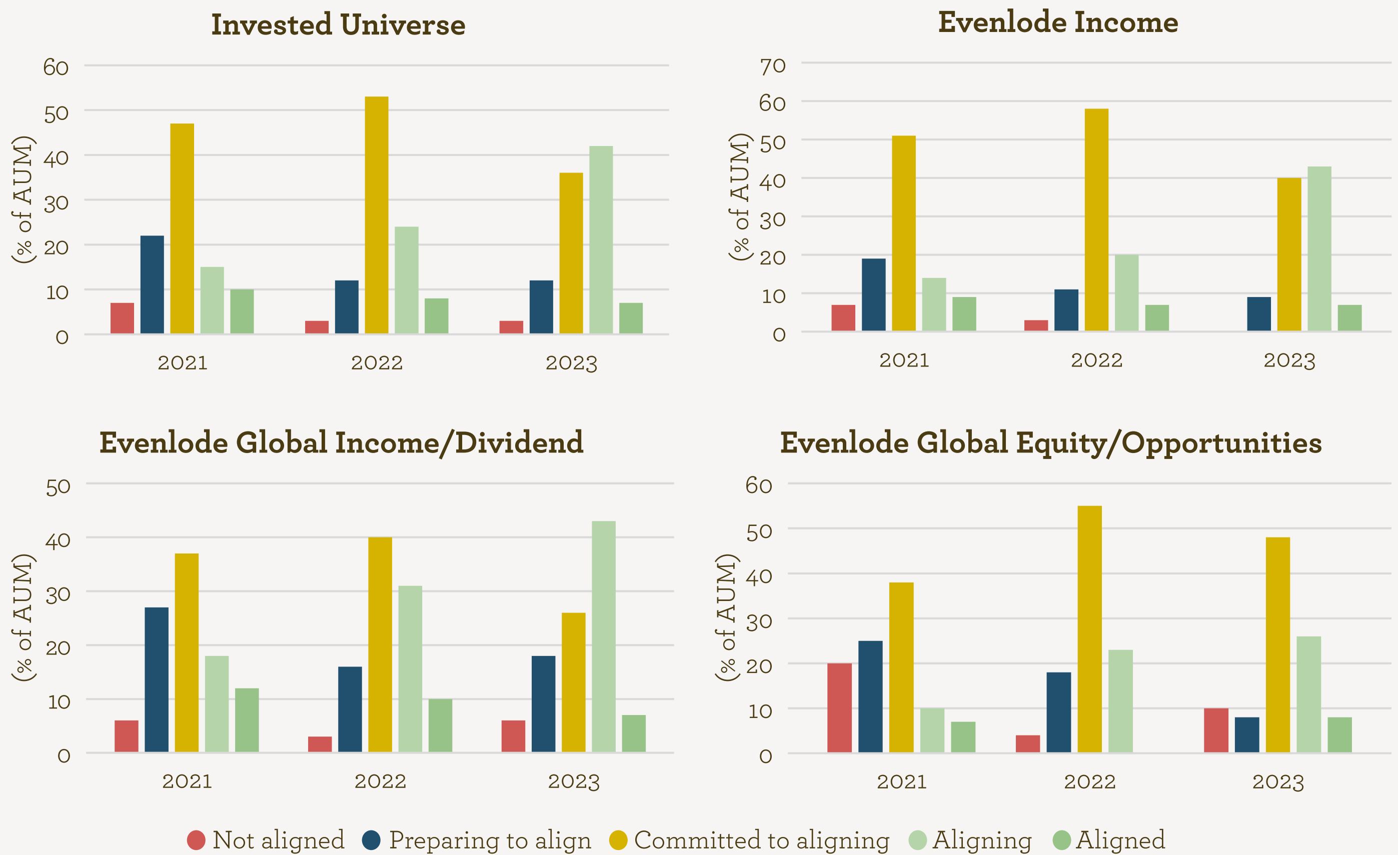
*This number includes the 'Preparing to Align' category created by Evenlode Investment.

2025 SHORT-TERM AUM ALIGNMENT TARGET

The second priority for us is to ensure that 50% of our AUM in material sectors is 'aligning', 'aligned', or 'achieving net zero' by 2025. Again, we want to align with best practice and therefore set an ambitious target.

For companies to pass this target threshold:

- They have to set a short or medium-term target.
- They should disclose scope 1, 2 and material scope 3 emissions data.
- Their targets should cover all greenhouse gases (not just CO2) and at least 95% of scope 1 and 2, and at least 90% of scope 3 emissions.
- Their trajectory should be consistent with what is needed to meet emissions targets.



PROGRESS

At the end of 2021, the first year of assessment, 24% of our invested AUM was either 'aligning', 'aligned' or 'achieving net zero'. Nearly 7% were 'not aligned' to net zero – this meant that there was no ambition of a long-term 2050 goal which was consistent with global net zero emissions. Communication Services, Financial Services and Information Technology were some of the sectors that were lagging.

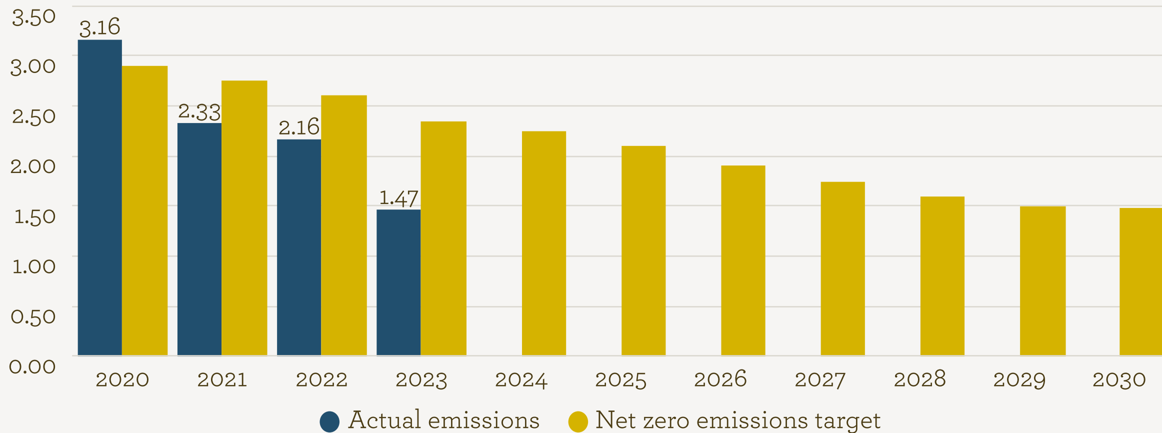
At the end of 2022, we were positioned at 32% 'aligning', 'aligned' or 'achieving net zero' and only 3.5% of invested AUM was 'not aligned' and therefore had not set a target. There was a large shift from the 'preparing to align' category to 'committed to align'. This meant that a larger number of companies, like Visa, Aon and LVMH had now set targets and were committed to aligning with a net zero world.

At the time of writing, our third round of assessments for 2023 is now complete and we are pleased to say that we have seen considerable progress in our alignment target year-on-year. For our material sectors only, 49% of our invested AUM is now either 'aligning', 'aligned' or 'achieving net zero' with only 2.6% 'not aligned'.

Important note: When interpreting and developing our initial net zero assessment framework, we wanted to set a high standard by encouraging companies to establish short-term emissions-related targets approved by the SBTi[1]. While the NZIF does not mandate short-term emissions reductions, it emphasises climate-related targets, which may involve engagements with suppliers, for instance. After conversations with several companies last year regarding their short-term targets or lack thereof, we recognised the challenges they faced in getting these targets approved - by the SBTi - in time for the 2023/24 reporting cycle. In certain cases, this process can take up to two years. Consequently, last year we chose not to adopt an overly stringent stance towards companies that are either in the process of engaging with the SBTi for short-term emissions reduction targets or have set 2025 targets involving supplier engagements. We have been impressed with companies progressing on their net zero alignment targets over the last 12 months, however, a portion of the improvement that we have identified would be due to the re-classification of our 2025 target methodology. The more challenging target for the funds and subsequently our investee companies is regarding their emission intensity for 2030.

1 https://sciencebasedtargets.org/about-us#who-we-are

EMISSIONS INTENSITY TARGET



When we started reporting our emissions intensity in 2019, the emissions associated with investing £10k in one of our funds was 3.52 tCO_2e. The following year, 3.16 tCO_2e. This was approximately a 10% reduction, year-on-year. At the end of 2021, the emissions associated with investing £10k in one of our funds was between 0.6 and 2.3 tonnes of CO_2 equivalents, or between 25 and 56 kilogrammes for scope 1 and 2 alone. For context, average per-capita emissions for UK residents in 2021 was 4.8 tonnes per year.

In 2022, we achieved an overall reduction of 7.2% in our emissions per £10k invested across our investment portfolios – a decrease from 2.33 to 2.16 tCO_2e from 2021. This reduction was solely driven by a 25.2% decrease in emissions per £10k invested for Evenlode Income (EI), our largest fund. This can be explained by a significant emissions reduction reported by the fund's top three emitters from 2021, namely Smiths Group, Procter & Gamble, and Reckitt Benckiser. Other Evenlode funds experienced an increase in emissions per £10k invested. Evenlode Global Equity (EGE) experienced a sizeable increase in emissions per £10k invested due to the fund's higher exposure to the Consumer Staples sector, which expanded from 15.1% to 25.1% during the year. Similarly, the increase in emissions per £10k invested for Evenlode Global Income (EGI) can be partly explained by the fund's higher exposure to the Industrials and Consumer Staples sectors compared to last year as well as a higher emissions footprint per investment for the fund's top three emitters, namely Henkel, C.H. Robinson, and Quest Diagnostics.

In 2023, we achieved an overall reduction of 32.2% in our emissions per £10k invested across our investment portfolios – a decrease from 2.16 to 1.47 tCO_2e. This significant reduction in our funds' financed emissions has been driven by several different factors. Firstly, the quality of reported data has improved as measuring methodologies improve and quality engagement with suppliers increases. Companies are best placed to report their emissions as they are most familiar with the nuances of the business model. Secondly, we have noticed strong engagement programmes from investee companies with their suppliers. For example, GlaxoSmithKline, a pharmaceuticals company held by EI and EGI, managed to reduce their overall CO_2e emissions intensity by 24%, or almost 5m tonnes through engaging with suppliers and reporting up to date figures for their scope 3 emissions.

EGI's emission intensity reduced significantly due to the fund rotating out one of the most emission intensive holdings, Henkel. EGE AUM has increased five-fold since last year's analysis was undertaken, and while the total emissions have increased, the fund's emissions intensity has come down by almost half. This is a result of large emissions reductions made by RELX, Verisk, Experian and Broadridge, in conjunction with the sale of C. H. Robinson, EGE's top contributor in 2022. Experian, a company held in all our funds, changed their calculation methodology for their 'Purchased Goods and Services' category last year to include more data from their suppliers. This resulted in a 68% decrease in their emissions for this category.

We have chosen an emission intensity target rather than an absolute target for our financed emissions as we are expecting AUM to increase in the coming years. To balance this with the potential for absolute emission increases, we have chosen a more stringent reduction target of 7% per annum in line with the SBTi Net Zero standard as opposed to a minimum 4.2% reduction per annum for scope 1 and 2, and 2.5% for scope 3 in the near-term for absolute emission reduction targets. This leads to a 51.6% reduction overall from 2020 to 2030. This is in line with the Standard's requirement to halve emissions before 2030 and to achieve a 90% reduction by 2050.

We believe that a science-based climate strategy is necessary to drive sustained emission reductions. We therefore intend to focus on engagement with portfolio companies over the next few years so that they have the necessary strategy in place to decarbonise. We expect this engagement push to contribute to rapid alignment of portfolio companies with 1.5°C. We recognise that there will be a time lag between target setting and seeing the effects of our climate strategy on company emissions and therefore portfolio emissions. Hence, we expect the targeted emission reductions to be realised most strongly in the second half of this decade. For this reason and due to the uncertainty around the enabling environment for decarbonisation (such as decarbonisation of the electricity grid, government action on climate and/or consumer behaviour), we have focused our efforts on asking companies to engage with their value chain to start the decarbonisation journey first, and then set emissions reductions targets by 2030. We will continuously review this and strengthen our targets or re-baseline our targets if we deem it necessary.

AMBITION

STRATEGY

The future is extremely uncertain making it unfair and inaccurate for us to predict events beyond 2030. In the following sections, we outline our strategy for further reducing GHG emissions both in our business and across our investments (financed emissions).

OPERATIONS

Let's start with our operational emissions. As discussed within our entity-level Taskforce on Climate-Related Financial Disclosures (TCFD) report, Evenlode Investments' operations are not the most emission-intensive aspect of our business. It is important to note that over 95% of our emissions as a firm originate from our investments, sometimes categorised by the market as 'financed emissions'. Nevertheless, we believe it is our fiduciary duty to our employees and the local community to operate the business as sustainably as possible. This commitment is not only to benefit the environment but also to raise awareness and educate our stakeholders about the significance of operational efficiency and sustainability.

Targets

Operationally, our target is to be net zero across GHGs, excluding financed emissions, by the end of 2030. Some of our actions will include:

- Reducing our business travel emissions. This will include choosing trains and electric cars as sustainable alternatives to flying.
- Constructing a new office which prioritises sustainability.
- Engaging with our most significant suppliers to understand and reduce their own emissions reductions.
- Increasing employee awareness.

These actions will inevitably involve the use of offsets, as certain categories of transport, notably air travel, will certainly not be decarbonised by that time. However, we are committed to ensuring that offsets do not exceed 5-10% of our overall emissions, focusing instead on direct emission reduction strategies. Additionally, we are actively exploring long-term opportunities to address these challenging areas. For instance, we are currently developing a new long-term home for Evenlode near Moreton-in-Marsh in Oxfordshire. This new site, which is under construction, will prioritise sustainability. The architects and designers have been instructed to utilise existing steel, recyclable materials, and the current framework to minimise the impact on the existing ecosystem. The project is expected to be completed by the summer of 2025.

For more information on our operations, please refer to our TCFD entity-level report on our website. We will be monitoring our progress on this target and will provide you with an updated figure next year.

FINANCED EMISSIONS

STEP 1: EDDIE ENHANCEMENTS

Evenlode has developed a proprietary research system, called EDDIE. This system houses all the research undertaken by the team, including initiation notes, quarterly updates, meeting notes, expert calls, and environmental, social, and governance (ESG) assessments. The system also includes a range of tools used to help manage the portfolio, including trade modelling, income management and reporting tools.

A recent addition has been the integration of the following emissions intensity metrics into the fund modelling tool:

- **Emissions per £10k invested:** The amount of GHG emissions for each investee company, which are then normalised to a £10k investment. In simple terms, each company's emissions are first calculated using CDP[1] and company reported data. The emissions are then divided by the total value of the portfolio and multiplied by £10k.
- **CO_2e/£m revenue:** Measures the total GHG emissions of a company expressed in terms of CO_2 equivalent per £1m of the company's revenue. It quantifies the emissions intensity in relation to the company's output.

Source: Evenlode's proprietary research system: EDDIE

The integration has made it easier for fund managers and investment analysts to track the emission intensity of each fund on a weekly basis. Each weekly investment decision, driven by valuation and recent market research, includes a check on the portfolio's emission intensity to see if it is increasing or decreasing. Although we do not invest in a company solely based on its emission intensity - as there are many other variables we consider like valuation, and recent news flow/ trading statements - the metrics serve as a guide to understand the direction of travel. It is important to note however, that there are many contradictions that don't fully capture the complete picture. For example, theoretically, we could sell an expensive stock to buy a cheaper one. The cheaper stock might have a lower emissions-to-sales ratio, but if its price-to-sales ratio (or P/E ratio) is low, it could result in a higher emissions-to-investment ratio. This scenario is acceptable and even beneficial for emissions reduction, despite potentially increasing the metric by which we assess the funds.

In the context of our net zero targets, the primary objective is to reduce the total carbon emissions of our portfolios over time. This might involve reallocating funds from expensive stocks that are not managing their emissions well to cheaper, more efficient ones. Our goal is not only to lower emissions per investment, but to cut total emissions. Even if emissions per investment rise initially, our long-term aim is to achieve overall emissions reduction. Over time, we hope that investing in and enhancing our existing workflow within EDDIE will gradually guide us towards our net zero targets and improve the emissions-to-investment metric.

1 The Carbon Disclosure Project (CDP) is a global non-profit organisation that runs a disclosure system for companies, cities, states, and regions to manage their environmental impacts. It provides a platform for measuring, understanding, and communicating environmental data, particularly related to climate change, water security, and deforestation. https://www.cdp.net/en/info/about-us

STEP 2: TARGETED ENGAGEMENTS
The following pieces of analysis help us target our engagements towards companies that are most impacted by climate-related risks and opportunities:

1. **AGM analysis:** We prioritise engagements with companies where we have voted against management on a particular resolution, especially if the resolution is a 'Say on Climate' vote. We are an advocate of a 'Say on Climate' vote especially when it is being displayed through the framework of the TFCD, allowing stakeholders to understand how companies are considering climate in their long-term strategy and how it is being measured over time. The momentum created for shareholders to express their support and/or discontent towards climate transition planning has been encouraging. Furthermore, adoption of such a vote enhances awareness of the organisation's climate strategy to the market and allows engagement plans to be initiated by investors.

   Spending time analysing climate transition plans is crucial for companies in certain sectors. As climate strategies become more intertwined with the overall long-term business strategy, shareholders may end up being asked to approve on certain elements of the company's strategy which is technically being re-packaged as the 'climate transition plan'. In situations where a company has submitted its own climate transition plan and we identify that the plan does not meet our minimum standards, we may vote against the plan and initiate an engagement strategy.

2. **Emissions analysis:** We have been publicly disclosing our financed emissions since 2019, for 100% of our investments. It is our view that by assessing the financed emissions of our funds annually and reporting our findings publicly, we stand a better chance of understanding the climate impacts of our companies as well as the transition risks, they are likely to face. The analysis enables us to engage with the most emission-intensive businesses in a targeted manner, consequently making progress towards our net-zero emission intensity targets. As is the nature of measuring financed emissions and the complications around data quality, the analysis is as perfect as some of the estimations provided to us by our investee companies.

   Nevertheless, this process provides valuable insights to steer our investment discussions and stewardship efforts towards our net zero targets. On an individual level, companies are continuing to increase or maintain their disclosure and the quality of the data being reported continues to improve year-on-year. Our analysis and subsequent engagements with our portfolio companies are becoming more impactful and as a result we can provide a clearer representation of our financed emissions to our clients. Evenlode will continue to engage with our portfolio companies to improve reporting and drive action to cut emissions.

3. **Carbon pricing:** In 2021, we started to look at the importance of carbon pricing and the effect that mechanisms already in use have on the companies we invest in. It is generally accepted that carbon prices need to grow over the long-term to drive investments at the necessary scale and pace. To keep global warming below 2°C the consensus suggests that prices must reach $50/tCO2 to $100/tCO2 by 2030[2]. As a result of this initial scoping activity, we decided to focus on the ten highest emitters in terms of carbon intensity (CO_2e/£m revenue) across the Evenlode portfolios. This led to a more targeted engagement strategy towards the most intensive holdings in the portfolio. These are also the investee companies that were classified as 'High Impact' under the NZAM initiative.

4. **Net zero assessments:** We use active engagement and voting to move portfolio companies along their net zero journey. This is where we can have the biggest impact and can contribute to real decarbonisation in the economy. Should a company's lack of net zero alignment present a severe, unmanaged risk, we would escalate our engagement. This could include a collaborative engagement, voting to effect change at board level, making a change to the maximum position size (risk budgeting process) or in some cases complete exclusion from our portfolios. It is important to us that engagements involve active dialogue with the company, that it is clear what the intention of an engagement is at the outset, and what the outcomes were once it is complete. We monitor all engagements within our proprietary research management system (EDDIE), alongside all other analysis carried out on a company. This means that engagements can be actively managed from start to finish and that they are also visible to the entire investment team, so that duplication of engagement effort by different members of the team can be avoided.

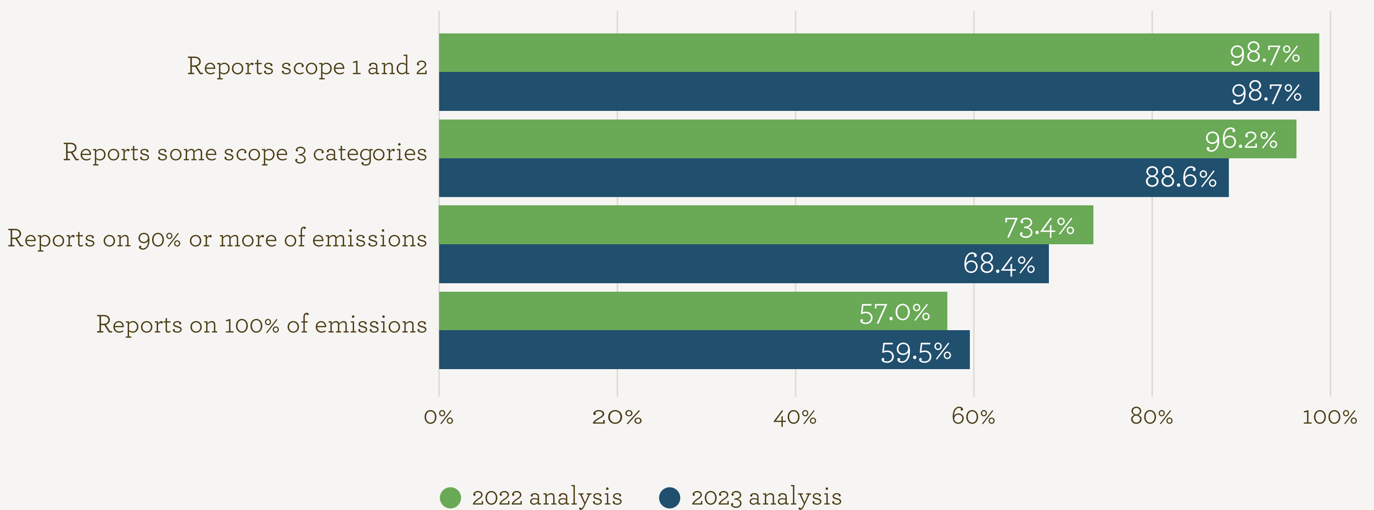
2 https://openknowledge.worldbank.org/entities/publication/58f2a409-9bb7-4ee6-899d-be47835c838f

Engage to enhance transparency

We believe that measuring the carbon footprint of our investee companies is a good indicator of their readiness for the transition. Since we began analysing the emission intensity of our portfolios in 2019, we have observed a positive trend; companies have been improving their emissions disclosures, especially scope 3. As data quality has improved, the reported emission intensity of both individual companies and our overall portfolios has decreased materially. A significant factor behind this reduction is the increased accuracy of data reported directly by companies, as opposed to reliance on third-party data providers.

Since we began conducting this analysis, we have witnessed a gradual increase in total emissions disclosure at the portfolio level. This year however we note a slight decline in the percentage of companies reporting on scope 3 emissions. There has been a rotation away from companies such as Clorox, Estée Lauder, Money Supermarket, AstraZeneca and eBay, into the likes of Clarkson, Spirax Sarco and Snap-on, principally as a result of our valuation discipline. However, where the former set of businesses were reporting 100% of their total emissions, the latter cohort calculate and disclose just 5% or less. The Stewardship team view this shift as an opportunity to engage in a meaningful way with companies who have not yet developed their emissions reduction strategies sufficiently.

Holding companies' emissions reporting by scope



Percentage of companies in Evenlode portfolios reporting across the different scopes. Source: CDP and Evenlode. 2022 analysis based on Evenlode portfolios as at 30 December 2022, using data from the CDP 2022 Full GHG Emissions Dataset. 2023 analysis based on Evenlode portfolios as at 29 December 2023, using data from the CDP 2023 Full GHG Emissions Dataset.

Our priority towards our net zero transition plan is to enhance our engagement with emission-intensive companies, especially those not yet reporting their own emissions. Encouraging these companies to begin direct emissions reporting is crucial for several reasons. Firstly, it allows investors to gain a clearer and more accurate understanding of the emission intensity within their portfolios. Accurate data is essential for making informed investment decisions and for assessing progress toward climate targets.

Early and consistent emissions reporting benefits companies as well. By providing their own data, companies can avoid being marked down based on potentially less accurate third-party estimates. This transparency can lead to a more favourable perception by investors and stakeholders, ultimately supporting the company's market position and long-term sustainability efforts.

Moreover, early reporting aligns companies with increasing regulatory requirements and market expectations. As global climate policies tighten and investor demand for ESG information grows, companies that proactively disclose their emissions will be better positioned to meet future compliance standards and attract investment.

Improvements in disclosure

In 2021, there was significant progress in scope 3 emissions reporting, with an additional nine companies reporting 90% or more of their total emissions, representing a 33% increase compared to the previous year. By 2022, the trend continued positively, with an additional five companies reporting some scope 3 emissions, a 12.5% increase from the previous year. Moreover, 20 more companies reported 90% or more of their total emissions, marking a 60.4% increase. Notably, 25 companies began reporting all their emissions, a remarkable 136.4% increase. This led to 91.6% of Evenlode's financed emissions being reported by portfolio companies, up from 83.0% in 2021.

In 2023, while we witnessed a slight decline in the percentage of companies reporting on scope 3 emissions due to changes within the funds, the overall trend of improved disclosure remained. The number of companies reporting more than 90% of their scope 1, 2, and 3 emissions dropped slightly from 58 to 54 out of 79 holdings, primarily due to portfolio rebalancing. Despite this slight setback, these changes have presented new engagement opportunities with companies reporting less than 5% of their emissions. We plan to focus on these companies in 2024 to encourage greater transparency and reporting accuracy. Our continuous engagement efforts underscore our commitment to robust and comprehensive emissions data, which is crucial for accurate analysis and informed investment decisions.

Engage with policymakers

For the global economy to decarbonise in line with the Paris alignment targets, a multi-stakeholder approach is required. Engaging only with like-minded investors and companies is not enough. Policymakers and industry standard setters must play an active role alongside public and private companies.

We are active participants of groups such as the Investor Forum, Climate and NatureAction 100+, International Corporate Governance Network (ICGN), Financial Reporting Lab's (FRC) Climate Change and Steering Committees and the United Nations Principles for Responsible Investment (UNPRI). Through collaboration we inform our own net zero strategy, share best practice and develop innovative thinking that will help us to reduce ESG-related risks and therefore financial risks to our clients over the long-term. We have found this industry participation vital in helping us to formulate the next steps in our strategy. Our overall approach around direct vs collaborative engagements is simple. We believe collaboration is important to strengthen our collective influence in addressing ESG issues and learn from like-minded investors. Collaboration can also increase the chances of a positive outcome. However, as long-term investors we have developed long-term relationships with our investee companies through direct engagements and we believe that is a key ingredient in effecting change that will benefit both our companies and clients.

Additionally, we recently hosted our first Net Zero Roundtable, gathering a diverse group of stakeholders, including representatives from public and private companies, charities, academic institutions, and industry standard setters, each providing their unique perspectives and expertise. The objective was to assess the significant challenges that businesses will face on their journey toward achieving net zero emissions. Through presentations, breakout sessions, and a panel discussion, the day aimed to address the following crucial questions and ideas:

1. Are current strategies and initiatives adequate?
2. What systemic changes are necessary within the market?
3. Who are the key stakeholders in your organisation for sustainability collaborations?
4. How can we focus on climate winners and improve the narrative?

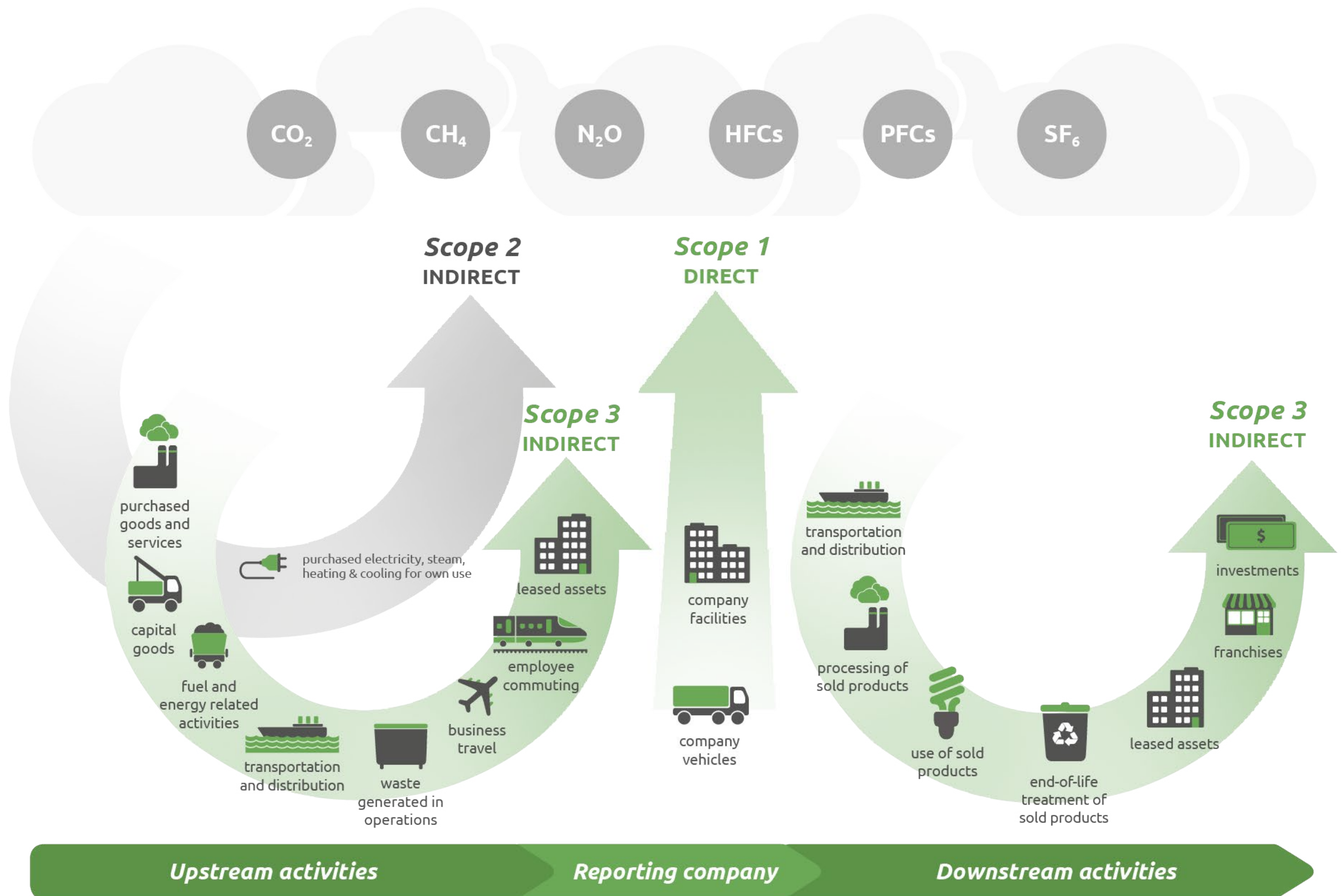
Our learnings from the day were that the global transition requires a coordinated, long-term strategy throughout the value chain that incorporates cultural differences and financial challenges. In the context of a just and fair transition, fair treatment for the emerging economies needs to be considered and monitored, with cultural context in mind. Supply chain dynamics present both challenges and opportunities in emissions reduction, with a focus on incentivisation, education, and the need for consistent policies and regulation across industries. One thing is quite clear, engagement with portfolio companies and the supply chain is crucial for tangible decarbonisation impact. Imperfect data and therefore goals are inadequate excuses when you have robust data management tools and sector-specific strategies.

STEP 3: UNDERSTAND EFFICIENCIES

Operational

Over the past three to five years, we have observed notable trends in the business operations and energy purchasing decisions of our investee companies. Specifically, scope 1 and 2 emissions have been decreasing at an encouraging rate. To clarify, company emissions are categorised into three scopes:

1. **Scope 1**: Emissions derived from direct business operations.
2. **Scope 2**: Emissions from purchased energy.
3. **Scope 3**: Emissions associated with the supply chain.



Source: World Resources Institute (WRI) and World Business Council for Sustainable Development (WBCSD)

Although scope 1 and 2 emissions make up less than 5% of our investee companies' total emissions, they can significantly impact reducing emissions throughout the value chain. Efficient processes in these areas can serve as sustainability signals, influencing the entire organisation with the improvements often resulting in cost savings and reduced capital costs.

For example, the London Stock Exchange, a holding in our UK Income and Global Equity funds, has significantly reduced its scope 1 and 2 emissions. Scope 1 emissions decreased by 26%, scope 2 by 16% compared to the previous year, and scope 3 by 90%, relative to their 2019 baseline. The reduction in scope 1 emissions was primarily due to a 28% reduction in floor area, resulting in fewer offices in use and consequently lower fuel consumption for heating. Additionally, in 2023, natural gas consumption decreased by 24% compared to 2022, driven by the disposal of several data centres. They feel that the decision of moving more of their physical data centre locations to the cloud will not only reduce their acute physical risk but also significantly reduce their scope 1 and 2 emissions.

Supply chain
Historically, there have been a few reasons why we have seen scope 3 emissions reductions within the portfolios:

1. **Improvement in company data**: More accurate reporting, as estimates from third parties tend to overestimate emissions.
2. **Changes in reporting methodology:** Companies in the trial-and-error phase, trying to understand the GHG protocol methodologies that work best for their business.
3. **Reduced employee commuting:** Due to hybrid working environments in a post pandemic world.
4. **Supplier engagement on decarbonisation:** Thorough due diligence on the sustainability characteristics of the value chain.

Companies that engage with their suppliers on their decarbonisation strategy are best positioned to reduce their emissions over the long term. They recognise the importance of addressing emissions across the entire value chain, not just within their own operations. Supply chain disruptions due to climate impacts can have significant financial implications. By working with suppliers to reduce emissions, companies can lower the risk of such disruptions. Additionally, regulations are increasingly requiring companies to report on and reduce their carbon footprint, including scope 3 emissions. Companies that engage with suppliers on decarbonisation are better positioned to comply with these regulations and avoid potential penalties.

For these reasons, at the start of 2024, we decided to integrate a question on 'supplier engagement' into our ESG risk score matrix. This allows us to evaluate the company's relationship with its stakeholders, ensuring the company is not just focusing on short-term financial performance but also on its long-term resiliency as a business.

STEP 4: INVESTMENT DECISIONS
As a reminder, the Evenlode Funds do not have a sustainability objective. Our primary objective is to seek real, durable returns for our clients over the long-term, investing in a sustainable way that contributes to a positive future. We believe that this objective can be best achieved by integrating ESG factors into our risk management framework. This ensures that all long-term risks, of which climate is one, are continuously monitored and managed on an ongoing basis. We believe active risk management is crucial to ensuring long-term investment returns.

With that in mind, we believe some investee companies are managing climate and nature-related risks better than others. Consequently, these companies receive higher scores on our ESG risk scoring matrix and are allocated a larger maximum position size in our portfolios. This position size represents the largest investment a fund is willing to make in a company, regardless of valuation metrics, including dividend yield.

Beyond 2027, we anticipate that decarbonisation risk within our framework will become more significant in our investment decisions. This shift will primarily impact emission-intensive holdings lagging on their net-zero targets; for example, if a company is considered material and/or high impact under the European classification of economic activities or NACE (Nomenclature of Economic Activities) classification, or is on the ClimateAction 100+ list and has not:

- Set a science-based target approved by the SBTi.
- Ensured the target covers 90% or more of all scopes and GHGs.
- Focused clearly on reductions over offsets.
- Committed near-term opex or long-term capex to its GHG reduction targets.
- Used an internal carbon price for capital allocation decisions.

Historically, we have observed that companies scoring poorly on ESG-related risks negatively affect other risk factors, particularly management culture and quality, long-term industry outlook, and, in some cases, the economic moat of a business. We foresee these knock-on effects becoming even more prevalent over time. As decarbonisation risks become more material, we will have to further lower the maximum position sizes of key holdings and potentially exit those not managing climate-related risks appropriately.

LOOKING AHEAD

We foresee several reasons why scope 3 emissions will reduce at an exponential rate over the next five to ten years:

1. **Improvements in supply chain efficiencies**: Companies are increasingly influencing their suppliers to adopt sustainable alternatives. This positive outcome is a direct result of the effective engagements we are currently witnessing. Over the next few years, we expect a substantial number of suppliers to have implemented these sustainable practices, driven by both pressure from leading companies and the competitive advantage sustainability offers. This shift will significantly reduce emissions as more suppliers improve their operational efficiencies and minimise waste throughout the supply chain.
2. **Product design and innovation**: Requiring less energy-intensive materials or more efficient production methods is another key factor. Companies are investing heavily in research and development to create products that are not only better for the environment but also more cost-effective. We anticipate that innovations in product design will have matured, leading to widespread adoption of these advanced materials and methods. This transition will reduce the carbon footprint of products from their creation to their disposal, making a notable impact on scope 3 emissions.
3. **Consumer behaviour**: Consumers are increasingly adopting more sustainable practices which influences their buying patterns. This trend is expected to continue and accelerate, driven by greater awareness of environmental issues and the availability of greener alternatives. We predict a substantial shift in consumer demand towards sustainable products. Companies responding to this demand will not only enhance their market positions but also contribute to a significant reduction in emissions as products with lower environmental impact become the norm.
4. **Regulatory compliance and standards**: Adhering to stricter environmental regulations will play a crucial role in reducing emissions across the supply chain. Governments globally are enacting more stringent policies to combat and reduce the worst effects of climate change. We expect these regulations to be firmly in place, compelling companies to align their operations with higher sustainability standards. This regulatory push will ensure that companies systematically reduce their carbon footprints, thereby achieving lower scope 3 emissions.

While these initiatives will drive considerable reductions in emissions over the next few years, the most significant changes in systems and infrastructure are likely to occur from 2030 onwards. These long-term transformations - including widespread adoption of cutting-edge technologies, substantial investments in renewable energy, and complete overhauls of supply chain logistics - will have a massive multiplier effect on reducing emissions. Post-2030, we anticipate that these systemic changes will enable companies to set some more realistic goals and for some, achieve their sustainability goals, drastically lowering emissions across all scopes. This approach highlights the importance of setting robust interim targets and continuously innovating and investing in disruptive climate-related technologies to ensure that the groundwork laid today will yield exponential benefits in the decades to come.

Baseline amendment

As discussed above, a significant proportion of the emissions reductions in our invested portfolios was largely attributed to companies improving the quality of their reported data compared to the previous year. Emissions data is typically most accurate when reported directly by the company. However, transparency alone is not sufficient. In 2023, the number of companies reporting more than 90% of their scope 1, 2, and 3 emissions slightly decreased from 58 to 54 out of 79 holdings. Despite this, there was a minor increase in the number of companies reporting 100% of their emissions, rising from 45 to 47. We anticipate that over the next three to five years more than 90% of the companies in our portfolios will be reporting over 90% of their scope 1, 2, and 3 emissions. At this stage, we would expect to see a natural decline in the rate at which our funds experience a reduction in their emission intensity, purely due to enhanced transparency.

As a result of improvements and/or inconsistencies of the data being gathered from investee companies, we have decided to re-baseline our targets from 2025 onwards. There has been a notable decrease in our emission intensity, however we are conscious that the large reason behind this has been improvements in data. This is why the Stewardship team is currently undertaking a large attribution analysis, to understand what proportion of the reductions the funds have experienced has been due to improvements in data, the companies operational/supply chain efficiencies or tilting the portfolio towards with attractive sustainable traits. Our initial thought is that because the weekly nudges in our portfolios are mainly driven due to valuation, it would be difficult to apportion a percentage towards the latter reason. Nevertheless, we think it would be useful to understand the differences between disclosure and efficiencies.

CONCLUSION

Evenlode has a defined risk management framework focused on factors that affect a company's ability to withstand uncertainty. These risk factors include ESG risks, which are independently managed by our Stewardship team. If we determine that companies are not appropriately managing their climate-related risks, our internal risk controls will prompt us to shift away from certain companies and/or sectors.

As our strategy outlines, we will spend the next three years improving our internal processes via EDDIE, engaging with key companies on transparency, working with policymakers, and conducting thematic analyses to understand and reduce inefficiencies. Following on from that and with valuation and materiality of risk in mind, we will reallocate our capital away from companies that are not effectively managing their sustainability risks towards those better prepared for the transition.

We hope this transition plan has given you an insight into our strategy on decarbonisation in the near-term. By proactively managing ESG risks, we aim to safeguard your investments against future uncertainties and align your portfolio with companies that are managing climate-related risks. However, this transition plan is not just about mitigating risks; it is also about seizing opportunities in companies that are leading the market with a robust net zero strategy. We believe that companies leading the way in these key areas will be the ones to thrive in the future, and we are committed to supporting these leaders through our investment choices.

APPENDIX

We define alignment levels following the NZIF:

Alignment classification	Meeting criteria	Description
Not aligned	-	No target set
Preparing to align*	-	Have set a target that is not in line with 1.5°C.
Committed to aligning	1	Have set a net zero target for 2050 or earlier that covers at least 95% of scope 1 and 2 and at least 90% of scope 3 in line with 1.5°C.
Aligning	1, 2, 4 and partial 5	Additionally: have set a short- (up to 2025) and medium-term target (up to 2035, covering at least 67% of scope 3), disclose at least 90% of scope 1, 2 and scope 3 emissions, and for high impact companies, have a plan relating to how the company will achieve these targets.
Aligned	1-4 (and 5-6 for high impact companies)	Additionally: have adequate emission performance over time in line with the targets set, and for high impact companies, have a decarbonisation strategy that sets out how they will achieve their targets and allocate capital in alignment with their long-term climate target. Also have emissions audited, disclose % of green revenues and details of offsets used.
Achieving net zero		Additionally: have reached or are close to net zero and have an investment plan or business model expected to continue to achieve that goal over time.

*Alignment classification created by Evenlode Investment to differentiate between companies who haven't set a climate -related to those who have, even if not in line with 1.5°C.

Alignment criteria	Description
1 Ambition	A long-term 2050 goal consistent with global net zero.
2 Targets	Short- and medium-term emissions reduction targets (scope 1, 2, and material scope 3).
3 Emission performance	Current emissions intensity performance (scope 1, 2, and material scope 3) relative to targets.
4 Disclosure	Disclosure of scope 1, 2 and material scope 3 emissions.
5 Decarbonisation strategy	A quantified plan setting out the measures that will be deployed to deliver GHG targets, proportions of revenues that are green and where relevant increases in green revenues.
6 Capital allocation alignment	A clear demonstration that the capital expenditures of the company are consistent with achieving net zero emissions by 2050.

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Get in touch:

Tel +44(0)1608 695200
Email evenlode@evenlodeinvestment.com
Visit evenlodeinvestment.com

Important Information

We believe that delivering real, durable returns over the long term can be best achieved by integrating environmental, social and governance (ESG) factors into our risk management framework as this ensures that all long-term risks are monitored and managed on an ongoing basis. In addition to reviewing ESG factors when making investment decisions, we engage with portfolio companies on a range of ESG issues (for example greenhouse gas emission reduction). However, please note that the Evenlode funds do not have a sustainability objective.

This document is not intended as a recommendation to invest in any particular asset class, security or strategy.

The information provided is for information purposes only and should not be relied upon as a recommendation to buy or sell securities. For full information on the Evenlode funds, including risks and costs, please refer to the Key Investor Information Documents, Annual & Interim Reports and the Prospectuses, which are available on the Evenlode Investment Management website (www.evenlodeinvestment.com). Recent performance information is shown on monthly factsheets, also available on the website. Every effort is taken to ensure the accuracy of the data in this document, but no warranties are given. Evenlode Investment Management Limited is authorised and regulated by the Financial Conduct Authority. No 767844.

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