

## Responsible Investment Policy

### 1. Introduction

The National Grid UK Pension Scheme (the 'Scheme') Trustee (the 'Trustee') recognises that the Scheme's Responsible Investment (RI) Policy should be updated to reflect the Trustee's current views. These views are founded on the increasing materiality of Environmental, Social and Governance (ESG) factors which, in giving rise to reputational, operational and regulatory risks for the Scheme's investments, can materially impact the quality and sustainability of long-run investment returns. Moreover, the Trustee, in distinguishing between financial and non-financial ESG factors, recognises that it is the former that potentially pose the most significant financial risk to the Scheme.

The Trustee's investment belief 5 ("Governance of Investments") states that investing sustainably is consistent with the Scheme's mission of taking full account of longer term return drivers and risk. By exercising good investor stewardship and by taking financially material ESG factors into account in its investment process, the Trustee believes the Scheme is better positioned to deliver the required long-term investment objective of reaching self-sufficiency in line with predetermined journey plans. RI and ESG considerations are consistent with the Trustee's fiduciary duties and should therefore be incorporated into investment analysis, manager selection and other investment decision making processes.

This updated policy builds on the previous policy, accounting for developments in the RI landscape, also recognising the increasing relevance of such issues to the Trustee and the intention to expand the Scheme's activities in the area.

This policy is based on the Trustee's views of the issues, on the UN-backed Principles for Responsible Investments ("UNPRI"), of which the Scheme is a signatory, and the practicalities of implementation. The UNPRI comprises six aspirational principles designed to encourage and assist investors integrate ESG considerations into their investment processes. This policy, which captures these views and principles, was developed by the Trustee Executive and approved by the Funding & Investment Committee and ultimately the Trustee Board. The Lead Section Employers were consulted regarding this policy and are fully supportive of this approach.

## **2. Definitions**

The Trustee defines RI as an approach to investing that incorporates ESG factors into investment decisions, to better manage risk and generate more sustainable, long-term returns. It should not be confused with ethical investment, or ethical negative screening, which is a specific investment style that screens out companies or activities based on moral or ethical preferences.

In formulating its approach to RI, the Trustee considered a number of potentially financially material ESG factors, including corporate governance, human capital and labour relations, corruption, and environmental standards. With regards to environmental issues, the Trustee considers climate change to be the most material and systemic financial risk factor to the value of the Scheme's assets.

## **3. Purpose & Scope**

This policy aims to set out the Trustee's beliefs regarding RI and ESG factors. It guides the implementation of such beliefs by the Trustee Executive.

The Trustee Executive and external investment managers mandated to manage the Scheme's assets are expected to adhere to this policy. The Trustee, via the Trustee Executive, will monitor compliance with this policy by external managers and the Trustee Executive will also report to the Trustee on its own activities on a regular basis. Where external managers offer unsatisfactory levels of compliance, engagement and communication will be the preferred route of action.

This policy applies to the Scheme as a whole, and to all asset classes invested by the Scheme in all regions and markets and across all strategies. It is acknowledged that not all asset classes are currently at the same stage of development on ESG considerations. Therefore, the Trustee and Trustee Executive will continue to monitor market developments, engage in discussions where appropriate, and update this policy as required.

This policy is relevant to all investment activities undertaken by the Scheme, directly or via external managers, including asset allocation, risk management, manager selection, manager monitoring, voting and engagement.

## **4. Governance**

ESG governance should be as rigorous as other governance arrangements within the Scheme. Governance encourages accountability, which should make this policy an effective tool for incorporating ESG considerations through the investment chain.

The Trustee Board is responsible for final approval and signoff of this policy. The Funding & Investment Committee is responsible for overseeing the policy's execution and implementation. The

Trustee Executive is responsible for executing and implementing the policy in its investment decisions and for monitoring its implementation by the Scheme's external investment managers in their investment decisions. The Trustee Executive will engage in discussions with those managers about the implementation of this policy where relevant.

## 5. ESG Integration

How the Trustee's approach to ESG is integrated across its investment activities is set out below:

- a. **Asset allocation:** The Trustee Executive considers ESG factors as part of its asset allocation decisions where these are relevant and financially material. The focus of this exercise is not only on preserving capital, through the mitigation of ESG risks, but also on identifying better quality and more sustainable long-term investment returns.
- b. **External Investment Manager Selection and Monitoring:** ESG considerations are included in any manager selection exercise as part of both the Investment and Operational Due Diligence processes. The objective is to assess the extent to which ESG is integrated in the manager's philosophy and process (i.e. analysis, voting policy, engagement, and associated policies). Even though expectations will vary according to the manager's asset class and investment style, ESG is an integral component of the manager's assessment.  
The Trustee expects that any other investment service provider to be employed by the Scheme take into account ESG considerations to the extent that they are relevant and financially material and therefore they will also be assessed on their ESG policies and procedures as appropriate.
- c. **Active Ownership and Engagement:** The Trustee believes that active ownership is the most appropriate channel to promote positive ESG practices. As all of the Scheme's assets are managed externally, the Trustee delegates voting to external investment managers and expects each to vote on their portfolio holdings in line with their internal voting policies (which are reviewed by the Trustee Executive periodically) and relevant recognised standards (e.g. the UK Stewardship Code). Any exceptions should be reported back to the Trustee Executive.

The Trustee expects external investment managers to engage with companies on ESG matters. Managers are well placed to do so given their knowledge of the company and access to company management. External investment managers are required to report on their RI and ESG integration processes and also on their proxy voting and engagement activities on a quarterly basis.

- d. **Risk Management:** The Trustee believes ESG should be integral to risk management. Understanding the exposure and the portfolios' sensitivity to ESG factors is essential to

determine the materiality of each specific factor and to inform investment decision making appropriately.

- e. **Monitoring:** The Trustee aims to monitor the impact and progress of its RI activities. This monitoring will be undertaken by the Trustee Executive, and reviewed by the Funding & Investment Committee on an ongoing basis, with an update included on the annual Member communication. As a signatory of the UNPRI, the Scheme commits to report on its RI activities on an annual basis. The reporting framework enables comparison of RI performance versus industry peers, encourages strengthening of internal procedures and summarises the activities for stakeholders.
- f. **Collaboration:** The Trustee backs industry-wide initiatives to encourage and advance RI and to that effect it is a signatory of the UNPRI. In addition, the Scheme may consider other collaborations with asset owners, investors, asset managers, advisers, industry bodies on a case-by-case basis.

## 6. Climate Change

As previously stated, the Trustee believes climate change to be a systematic, long-term material financial risk to the value of Scheme assets. Therefore the Trustee has a fiduciary duty to consider climate change risk when making investment decisions. The Trustee understands that the tools and methodologies available to measure the financial risk of climate change are evolving. However, getting a broad understanding of where the main risks related to climate change are focused can put the Scheme in a better position in mitigating such risks as they unfold. The main actions that facilitate such considerations are:

- a. Better understanding and reporting of portfolio exposures to climate change: the Trustee supports the Task Force on Climate-related Financial Disclosures (TCFD) and aims to incorporate its recommendations into the Scheme's reporting. At this stage, it may be able to report data for only a portion of the Scheme's investments given data availability and methodological issues, as the TCFD recognises.
- b. Ensure incumbent and new external investment managers' approach to incorporating climate change to their investment decisions is understood and improvement is encouraged.
- c. Engage collaboratively with peers and the investment community. The Scheme is a member of the Institutional Investors Group on Climate Change (IIGCC) and will consider other collaborations as appropriate.