



*Andra AP-fonden*  
Second Swedish National Pension Fund - AP2



AP2's approach to  
the transition towards  
a low-carbon economy

# CEO statement

In December 2015, 195 states agreed on a global climate agreement to reduce climate emissions. The agreement establishes that the global increase in temperature should be kept well below two degrees Celsius and that countries should strive to limit the increase to 1.5 degrees. The Paris Agreement bolstered the Second AP Fund's (AP2) view that we are currently at the start of a transition into a low-carbon economy and that our work to integrate climate considerations into risk assessments and investment decisions is ever more important.

Because AP2 is a long-term investor, it is obvious to us that our asset management needs to take into account the risks and opportunities associated with climate change and our transition into a society with zero net greenhouse gas emissions.

Climate is one of AP2's focus areas and our ambition is to develop our portfolio in line with the two-degree target. In order to make this possible we work actively to include various types of climate information in our analyses and investment processes. Based on the fund's mission, we are also seeking out investments that contribute towards our transition into a two-degree society.

The fund's climate work has been developing for several years. We began working with climate issues in a more structured manner as early as 2008-2009. Back then the focus was on what consequences a global carbon price would have on our equity portfolio. As part of this project we calculated our equity portfolio's carbon footprint. We learned a lot from these calculations, but they did not result in any changes to our asset management due to the fact that the 2009 Copenhagen Climate Summit failed to deliver a consensus. In order to increase the transparency surrounding carbon emissions from AP2's investments, the fund has been reporting the equity portfolio's carbon footprint since 2014. The aim is that, in the long term, all asset classes will be included in the report. All the AP funds have been collaborating on benchmarks and carbon emission reporting since 2015.

Autumn 2013 saw the initiation of a new climate projects and the creation of an internal working group for the analysis of climate risks. This time the focus was on fossil fuels. The project



aimed to define the fund's position with regard to fossil fuels and to identify financial risks associated with fossil fuels becoming stranded (i.e. assets falling in value due to climate concerns). This project resulted in the fund divesting in companies that extract coal exclusively and in oil and gas companies that have invested heavily in new high-cost projects. The group tasked with this project continued with the power sector and analysed financial climate risks for companies with coal-fuelled power stations. This project also resulted in divestments. AP2 performs an update of these analyses annually which is communicated externally. You can read more about these projects on [www.ap2.se](http://www.ap2.se).

For AP2, climate work involves more than risk management. We also consider investment in climate-smart projects and companies as an opportunity. Several studies show that, in purely financial terms, an organised transition to a low-carbon society is the most beneficial scenario for long-term investors. In order to be able to assess our portfolio we need to have an idea of what the 'target' looks like as well as benchmarks that can be used for assessment. That is precisely why we are constantly working on these issues.

I hope that this document will help you understand why and how AP2 works with climate issues.

A handwritten signature in black ink, appearing to read 'Eva Halvarsson'. The signature is fluid and stylized, with a long, sweeping flourish extending upwards and to the right.

Eva Halvarsson, CEO



An aerial photograph of a mountain valley. In the foreground, a winding road with traffic curves through green fields and small houses. A large lake is in the middle ground, surrounded by a village with red-roofed buildings. In the background, steep, forested mountains rise under a blue sky with light clouds.

# A long-term investor – for all generations

AP2 is one of the buffer funds within the Swedish pension system. The fact that we manage pension capital means that we need to take a long-term approach. The capital managed by the AP2 should contribute to the pension payments for different generations being as even as possible. The fund's mission is to maximise returns at a low risk so that the negative impact of automatic balancing (the so-called brake) on pensions is as small as possible.

The analyses performed by the fund to assess future pension payments are based on a 30 to 40-year outlook. Consequently, it is natural for AP2, as a long-term investor, to work with sustainability issues as these will have a major impact on the development of society.

Because climate change and the transition to a low-carbon society is one of the main challenges of our time, it is obvious to AP2 that climate should be one of its focus areas.

# We take responsibility for climate issues and contribute to the transition to a low-carbon economy

Climate issues, and above all climate change, represent both huge risks and big opportunities for long-term investors such as AP2. Climate change is deemed to have the potential to impact long-term returns considerably. The starting point of our climate work is to lessen the financial risk and leverage the opportunities by contributing to the transition. AP2's climate ambition is to develop our portfolio in line with the two-degree target. This is achieved by integrating climate analysis into the investment process and by, based on the fund's mission, contributing to the transition into a two-degree society.

Our climate ambition is to develop our portfolio in line with the two-degree target.

This is achieved by:

Integrating climate analysis into investment processes

Based on the fund's mission contributing to a transition into a two-degree society

## How we integrate climate analyses into the investment process

The fund has an internal fossil fuel and financial climate risks working group. Analyses are performed based on the fund's mission to take ethics and the environment into account without compromising the overarching target of high returns, meaning that they are based on a financial risk perspective.

The group began by establishing the fund's position with regard to investments into fossil energy and analysing the financial climate risks associated with coal and energy companies. This analysis resulted in the fund divesting in around 20 companies, half of which are coal companies.

A financial climate risk analysis has also been performed for the power sector. AP2 believes that the power sector is at the start of a transitional period which will see coal-based power being phased out. The analysis resulted in the fund divesting in approximately a fourth of all electricity-producing companies.

The fund performs an annual follow-up of these analyses, based on established criteria, to determine which companies meet the criteria.

## How we contribute to the transition

AP2 wishes, to not only adapt to future changes, but to help contribute to the transition to a low-carbon economy.

We do this through:

- Investment in sustainable strategies
- Dialogue with companies
- Dialogue with decision-makers

Furthermore, several fund employees speak at seminars and conferences about the fund's climate work, both in Sweden and internationally.

### *Investment in sustainable strategies*

Creating a low-carbon society requires, among other things, a transformation of the energy and transport system. This represents challenges and opportunities that give rise to important economic and business-related questions. AP2's investments in green bonds and forest assets are two examples of investment based on sustainable strategies with a positive climate impact.

### *Collaboration with organisations*

AP2 works on climate issues in various ways, both toward companies and together with other investors and organisations. For example, AP2 has been supporting the CDP's (formerly the Carbon Disclosure Project) work to make more corporations report climate data for many years. Investors can obtain various types of climate data from the CDP, including data relating to the carbon emissions of various corporations. AP2 takes a positive view on corporations reporting climate data to the CDP.

AP2 is also a member of the Institutional Investor Group on Climate Change (IIGCC). The IIGCC primarily works to influence policy-makers to develop clear long-term guidelines for climate policy. The IIGCC was very active in the run-up to the Paris climate conference and demonstrated, through its collaboration with sister organisations in the US and Australia, that investors are concerned by climate change and supportive of strong measures. The IIGCC also helps investors to work actively on climate issues by publishing reports on how asset owners can integrate climate considerations into various asset classes, organising seminars on relevant topics such as, for example, the measurement of equity portfolio carbon footprints, and coordinating investor initiatives relating to specific companies, e.g. shareholder proposals for extended reporting on the companies' strategies for various two-degree scenarios.

### *The AP Funds' collaboration*

The AP Funds collaborate on measuring and reporting their carbon footprints. In autumn 2015 the funds agreed on shared metrics. All funds have, in a common fact sheet, highlighted the benefits and disadvantages of this metrics, which has been received positively by both Swedish and international investors.

### *Internal commitment*

AP2 also works to limit its own direct climate impact by lowering its electricity consumption, reducing air travel, increasing train travel and promoting increased use of telephone/video/web meetings and increasing its employees' awareness of climate change.



# Sustainability as part of the asset management model – creates long-term returns

Naturally, the main way in which AP2 can contribute to a transition towards a low-carbon economy is through the fund's investments. All departments within AP2's asset management work actively to integrate sustainability into its analyses and investment processes. The way in which this is done depends on both investment strategy and asset class.

The fund is responsible for both the management and the ownership of its capital and works actively on environmental, ethical and corporate management issues from both of these perspectives. By driving sustainability issues, we can help the portfolio companies identify opportunities and risks at an early stage, which will have an impact on our returns. We believe that a long-term, responsible approach to the environment, ethics and corporate management increases the value of the companies. By integrating the financial analysis with environmental, ethical and corporate management analysis in our management, we can create a better basis for our investment decisions.

Within fixed-income, AP2 has been investing in green bonds since 2008. These bonds finance environmental projects that are often linked to various climate aspects, for example, investment in energy efficiency.

Some of the private equity funds in which AP2 has invested focus solely on renewable energy. The fund is also invested in funds that in turn invest in young companies that often develop products or services that help limit resource consumption.

The fund works actively in the property sector, where there is considerable scope for energy optimisation. Energy is an important issue as the property sector is responsible for up to

30 per cent of global greenhouse gas emissions, and for up to 40 per cent of energy consumption. In order to be able to better monitor and assess the sustainability work in AP2's property investments, the fund is a member of the Global Real Estate Sustainability Benchmark (GRESB).

AP2 has been investing in forestry property since 2010. Forests represent important carbon sinks, meaning that they store carbon dioxide, thus lowering the amount of carbon dioxide in the atmosphere naturally.

## *World-class asset management*

AP2's vision of providing 'world-class asset management' can only be achieved if sustainability is integrated into the management. This is because sustainability issues are important to social development and future economic development and thus also to the fund's capital returns. Knowledge and information about climate change and the transition to a low-fossil society that has now begun is therefore important to AP2 as a long-term investor.

Sustainability issues and the integration of sustainability in analysis and investment processes therefore play a key role in the fund's asset management activities.

” Within private equity allocation AP2 has, as a long-term investor, been investing in renewable energy sources, environmental technology and technology-driven companies for several years. We believe that the number of attractive and financially competitive investment opportunities within renewable energy and environment technology will increase as a natural result of market and world developments and an increased focus on climate issues.”

**Camilla Axvi**, Head of Private Equity

” Information and knowledge are of crucial importance when it comes to ensuring good climate work. That is why the fund is working to improve the climate reporting of the companies that we invest in, but also to develop our own reporting with regard to the description of financial climate risks, investment in sustainable strategies and our organisation’s direct climate impact.”

**Christina Olivecrona**, Sustainability Analyst

” Investing in green bonds is a way of channelling investment to projects with a positive impact on the climate while at the same time ensuring equivalent returns. Increased interest in green bonds is positive as it means increased focus on the climate issue and that we, as investors, can implement sustainability aspects in our fixed-income portfolio in a clear way.”

**Lars Lindblom**, Fixed-income portfolio Manager

” Climate issues represent a major challenge to companies and investors, as well as to others. Policy changes are required in order to meet the UN’s climate targets, and this will alter the operating conditions for many organisations. This involves financial risk for some of our investments and new opportunities for returns in the future. We work continuously, within the framework of our mission within the pension system, to develop our ability to lower our risks and identify new opportunities.”

**Hans Fahlin**, Chief Investment Officer





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