TRANSITIONING TO NET ZERO: IS YOUR COMPANY READY?
LESSONS FROM APPLYING THE ABATEMENT CAPACITY ASSESSMENT FRAMEWORK

- **Fraser Pearce**, Independent Board Chair, Trafford Centre
- **Ashley Vogeli**, Managing Director, Strategic Communications, Public Affairs and Communications, CPP Investments
- **Richard Manley**, Managing Director, Head of Sustainable Investing, Global Leadership Team, CPP Investments

INTRO CLIP

RICHARD MANLEY

The real opportunity here is to have a conversation about the optimal transition – that we remove the most greenhouse gases from the business that we could with the least capital outlay into the business.

FRASER PEARCE

That allows you to put that priority into a business plan, into a case, and then make sure that you've got the finance to do it. And, you give the investor in our case CPP Investments the confidence that it's achievable because you've done the work.

ASHLEY VOGELI

Hi, I'm Ashley Vogeli from CPP Investments Insights Institute. The Institute is CPP Investments platform for sharing knowledge and collaborating with fellow investors, CEOs and policymakers to engage on ways to overcome obstacles as we mobilize and maximize capital One area of focus for the Institute is climate change, and especially its impact on long term investors. At CPP Investments, we believe it's time for the world to shift its focus from a top down view of what needs to be done across sectors to address climate change to more of a bottom-up view of what actions individual businesses can take today to abate greenhouse gas emissions.

Now we've all seen them, corporate net zero commitments are everywhere, and whether or not companies deliver on their commitments will impact the long-term viability of their business. Businesses which deliver on their net-zero commitments should preserve their access to capital and thrive over the long term. Those that don't, likely won't. Today I'm joined by CPP Investments' Head of Sustainable Investing, Richard Manley and independent board chair of the Trafford Centre, Fraser Pearce. The Trafford Centre is a shopping centre in the U.K. that CPP Investments owns. The fund has supported the board and its management team while they designed a decarbonization plan for their business. How the centre went about this process and the framework that provided both operators and owners of the company with confidence in the business's decarbonization plan is what we are going to talk about today.

Last year, CPP Investments introduced a novel concept, one we call an Abatement Capacity Assessment Framework or ACA/PAC for short. The fund is piloting the Abatement Capacity Assessment Framework within its own portfolio. The first use of this Framework took ten weeks to complete and at the end provided the board of the Trafford Centre with a robust emissions baseline. One of the most important learnings from this pilot is just how critical it is to have an accurate baseline of companies carbon consumption today in order to develop a decarbonization pathway for tomorrow.

We're going to hear from Fraser Pearce, the Trafford Centre's chair, about his experience using this framework. So, Fraser and Richard, welcome.

FRASER PEARCE

Thanks, Ashley. Hi, Richard. Great to be speaking to you today.

RICHARD MANLEY

Hi, Fraser. Great to be having this conversation and thank you for joining us.

ASHLEY VOGELI

Let's begin by hearing from you, Richard, What is the Abatement Capacity Assessment Framework and what was the inspiration behind it?

RICHARD MANLEY

Thanks, Ashley. I'd say the inspiration for creating the abatement capacity assessment was a by-product of conversations that we were having with directors across our public and private portfolio companies. And really the conclusion that developing a decarbonization strategy is the boardroom equivalent of eating an elephant. It's complex, it's massive. Decarbonizing 100% of the greenhouse gas emissions from the business, not just those that you can control, but those that are impacted by suppliers and customers is really, really complex and not made easier by the fact that we don't yet know the technologies we'll have available to us.

We don't necessarily yet know the regulatory environment we'll be operating in, and we don't always know how our customers' choices will change in the medium term. So really, that got me thinking, what would I want from the management team of the company if I was a board director being asked to approve a medium-term greenhouse gas reduction target, and over the long term, a commitment to net zero?

And what I concluded was I'd want to understand, in the context that the short-term and medium target being set, how did that reconcile with the percentage of the greenhouse gases we'd identified as economic to abate? So if we commit to 50% reduction, is that more than, more or less in line with, or is it wildly different from the percentage of emissions we've identified as economic to abate that as we think into the long term, we're committing to net zero, that's 100% reduction. What's proven and probable today? Is it just 30 or 40% or are we at 90% and only really having to find the last 10% over the course of the next three decades?

ASHLEY VOGELI

Board directors and management teams are facing a significant challenge. So Fraser, can you talk about how Trafford is preparing for a net-zero world? How did you utilize the Abatement Capacity Assessment Framework?

FRASER PEARCE

Where we started, because, as Richard says, this really is a huge area that you've got to cover. We started with our current emissions assessment and an ambition framework, and we did this over a relatively short period of time, a matter of months. We looked at what our ambitions were relative to our peer group, and we did some analysis around that.

We broke down our current emissions in two key areas. As Richard was saying, because we're a B2B business, we're providing space to tenants and then the tenants are B2C, a lot of the emissions are coming from our tenants' activities in transport, in how customers receive goods into the centre, etc. What we tried to do, first of all, was to look at our own emissions, as a landlord and an asset owner, that we were generating and breaking that down into things like natural gas, our own internal vehicles, electricity that we purchased from the great system, our own employees commuting, things that were within our control.

We broke that down so that we could really, one, put some structure around our thinking, but also look at what I would describe as not so much bite size, but manageable projects within that whole abatement capacity and future projected abatement capacity that we could manage at Trafford, that we could really put some resources around, that we could really aim to verify. Because the verification of them and I can talk to you about a bit later because I think the whole data piece and the whole verification piece was a key to our initial current assessment and that's kind of how we started. And once we got to a pretty good understanding of our baseline position, we were then able to talk about our priorities.

ASHLEY VOGELI

Fraser, is it fair to say that the Framework helped provide the Trafford Centre and its board with a clear starting point for your business to decarbonize?

FRASER PEARCE

Because this really is a huge topic area depending on what kind of business you're running and what your emissions are and where they're coming from, you really need somewhere to store and you need a structure to put your baseline assessment across so you can then map that in terms of one) your ambition two) bite sized or manageable projects, you can then start to work on whatever they are economic, whatever they are on economic, whether they are going to involve, in our instance, capital expenditure that may be recoverable or not from our tenants. And you can see your ambition to get to net zero, especially as that looks doable and then you can carry on with your analysis in each of those subject areas, which is something that the Framework provides.

ASHLEY VOGELI

Richard, let's bring this back to CPP Investments. Why does the framework matter to investors like us?

RICHARD MANLEY

Several reasons for that. Ashley, I'd start with first of all that to date most of the debate around decarbonization has focused on what needs to be done, rather than what can be done. And the fact that we need to decarbonize the economy in three decades doesn't actually provide solutions, it provides a challenge. And the beauty of conducting an Abatement Capacity Assessment is that it requires management teams to proactively identify every opportunity at their disposable, whether those drivers of decarbonization are simple efficiency measures, moves to electrify business processes and procure green electricity, or whether those are larger capital investments seeking to deploy abatement or decarbonization low-carbon technologies, there aren't that many levers that corporations have at their disposal to decarbonize the business. But identifying those that are economic now and arming the board and the management team with the opportunity to have a commercial discussion about we can do 30%, when should we seek to do that is, I would say, a highly empowered conversation. And it's also a tremendously intuitive conversation.

It doesn't matter what the drivers are. The fact that we're now having a conversation about how we can get partway to our endpoint economically is a much more business-orientated conversation than I need to get to net zero in three decades. I think the next consideration is the requirement to say if I don't get to 100% with proven abatement capacity, the ability to actually apply a couple of simple scenarios and basically that is that the carbon price is higher over time, allowing us to engage in understanding which other options to decarbonize are likely to become economic.

I think gives the board and the management team the opportunity to have a conversation about how will we ensure that we stay focused on prioritizing when those become economic and integrate them into the business plan. I would say lastly, it's I think it's very helpful to understand for the management team which of these are uneconomic in order to contemplate where they may have to take more drastic action.

So we move there from the what needs to be done to the what can be done. But the reason this is significant for us as institutional investors is that we have thousands of companies committing to attaining net zero, but we have no capacity to determine which of those commitments are more speculative in nature, where maybe the proven and probable abatement capacity is just 30% of the whole or those that we could view as maybe becoming a slam dunk where the proven and probable capacity to decarbonize the business is into the eighties and 90% giving the management team real conviction and starting to communicate not only to the market but importantly their corporate clients, we are not a climate headache, we are a climate solution. And if you partner with those, we can be part of a journey to decarbonize together that is great for your brand and great for our respective businesses. And the significance of that information when aggregated at scale for us as an investor is it helps us price transition risk.

If we can identify which parts of the economy can decarbonize and which parts of the economy can't. We are far better positioned to price risk, but importantly also provide transition capital to those businesses that have a credible pathway to decarbonization over the medium term.

ASHLEY VOGELI

Thanks Richard. Fraser, thinking more broadly about sustainability, what are Trafford's sustainability goals and how do you plan to achieve them?

FRASER PEARCE

Our ambitions, after we carried out our initial assessment, were to focus on provision of renewable energy through our potential onsite generation capabilities. We've got a lot of land at the Trafford Centre, so we were very keen to look at some market-leading electric vehicle charging capabilities that we really felt could help with some of the emissions and put us at the front end of that move towards EV charging particular graphically where the Trafford Centre is based in the U.K.

We wanted to continue what was already a really well-developed commitment to zero waste to landfill and you know, to pick up on some of the things that Richard said a minute ago, some of the really important things that we've done and made some commitments around are where we try to influence behaviors and our tenants' behaviors, particularly through introducing, what we think are, market leading green leases.

We've gone through our standard lease template and we've introduced along with our kind of external advisors that we've been helping here and now legal support, a number of clauses that we want to put in now and where we want to move people over time with encouragement and some of the behaviors that we will be exhibiting in terms of our actions as landlord, we've updated our fit-out guides, so that we're looking at sustainability all of the time when tenants are looking to upgrade their units or when we're looking to do landlord works and we've updated our tenant handbooks so that the whole behavioral piece is locked into our overriding ambitions to get to net zero.

So, it's not just about spending money, it's about driving some behaviors and having the tools and the information. And then I think the other thing that I would pick up on the Richard said that's really relevant for the Trafford Centre is around the whole verification piece. So the investors and our stakeholders and any users of our financial information can have some confidence that what we're saying, we're moving towards one, we report upon it regularly and that they can have confidence in the accuracy of it.

So, what we've been doing is introducing and in this instance investing in a range of new data gathering initiatives and technologies. So, for example, we've introduced some Wi-Fi technology. We're encouraging and mandating in some instances that our tenants provide us with usage information so we can track it. So, water, energy, etc. and that we've got a much, much more accurate view on not where we were in terms of a baseline assessment, but where we're going or want to get to.

So hopefully that answers that question. It's a real Framework to pose all of those things together so that when you're putting a plan together as a board, you've got some confidence that you've got a definable and achievable objectives and then the resources and the tools to do it.

ASHLEY VOGELI

Richard, how does access to this type of info help investors? Why is it so important?

RICHARD MANLEY

I'd say at the moment Ashley the biggest challenge that we have when we look across the portfolio is really discerning which boards and which executives have their arms around the challenge and as a result will convert the challenge into the opportunity the climate has the potential to be for the decades ahead. And it's not just about the data, the data is very helpful to have.

Knowing every issue in the portfolio with the proven probable and uneconomic abatement capacity would be fantastic. But I think a lot of the value actually derives from the conversations that we're able to have today. It's actually knowing that the board did its job and discharged its duty to the company to initiate a conversation with the management team. We have to anticipate in a market like the U.K. where the government has committed the economy to being net zero by 2050, that we need to plan for a world in which we can't emit greenhouse gases.

How will we change our business to align it with that macro reality to ensure that we can create value and thrive for the long term? And knowing that they've identified where their molecules are coming from, they've been able to prioritize that decarbonization and then be able to give us some visibility about which elements of that decarbonization are not quite where they want them to be in terms of economics, but the approach that they're having to iterate and innovate and work with partners to get there.

And then whether it's actually running operations off or ultimately a plan to offset the residual or being able to engage in a business conversation around that rather than a normative conversation around that is I think, where we would like to be. And I'm going to ask questions of Fraser here, because one of the things that I think we observed when we started to see the data come out was I think it was about 5% of greenhouse gas reduction was in the business plan as a byproduct of some reasonably big capital investments that had to be made to maintain the operational performance of the space. But I think that one of the first outputs that came out of the abatement capacity exercise was that about three times that so another 15% could be delivered for about one 20th of the capital outlay and certainly that prompted a question for all of us, like why do we not do this the other way round?

And it wasn't the board or the management team were not thinking the right ways. They did not have access to the information to say, let's go get this next 15% because the capital outlay associated with it is a drop in the ocean. And I think for us it's knowing that those conversations are happening. I think we all know they want to do the right thing, it's helping empower them to do the right thing that is where this becomes powerful for us as a capital provider.

FRASER PEARCE

With the Trafford's Centre, when we got our arms around where our emissions were coming from and we'd extrapolated the analysis into what was economical to abate by our ambition objectives by the time in the future, and we were able to look at the materials we have there, that's what allowed us to set our priorities right, which is what you're referring to, Richard.

And when you then look at some of the cost of those things and you look at some of the lifecycle implications of our maintenance plans, business as usual, you can quite easily say as our management team as a board, why don't we do that now? Right, because that is, you know, what you might describe as relatively low expense.

It's got to be done and it's actually going to tick off X percent of our projected abatement. And that allows you to put that priority into a business plan, into a case, and then make sure that you've got the finance to do it. And you give the investor in our case, CPP Investments the

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confidence that it's achievable because you've done the work. you've gone through it very methodically, piece by piece.

ASHLEY VOGELI

It's evident from Fraser's comments that the Trafford Centre has done a tremendous amount of work thinking about its own decarbonization pathway. This is a rapidly moving space dependent on several different levers as you've both outlined. So what words of wisdom do each of you have for others who are maybe trying to eat the proverbial climate elephant, to use Richard's analogy?

FRASER PEARCE

Use the structure because it provides a methodology and a way of approaching the work that you need to do so that you can arrive at a set of bespoke priorities for your business. So, we're talking about the Trafford Centre, which is a landlord of a super prime regional shopping centre within your portfolio, CPP investments.

And broader than that, there's going to be lots and lots of different business models so some complex, some simpler than others. And I think if you use this kind of standardized approach, what you get out of it at the end is a series of manageable projects that you can cost. You can understand what the abatement potential is and then you can have the discussions around how those priorities, your investor’s priorities and how are you going to track the achievement of that so that everyone can see that you verified it and things then become really much more easy to get the kind of support.

So, the value in doing this is for the Trafford Centre, we get a bunch of resources that would otherwise not be there in the form of human capital and potentially more physical capital to do the things that are only going to make our centre fit for purpose. As Richard says, the U.K. government's ambitions for 2050. This is only going to get harder as we go along and if we don't change, irrespective of our knowledge of future regulations and all of those kind of things, we will become irrelevant also by doing these things with confidence and in a structure, we make ourselves much more open to other sources of finance and capital in the capital markets and that can only be a good thing. And if you don't do it, obviously the reverse is going to be the case, right? You're not going to be able to access capital and it's going to become a self-fulfilling prophecy.

RICHARD MANLEY

On a micro level, I'd like to say to have many, many more conversations with boards and management teams like this, that they did this work at a bottom-up level and it helped, I suppose, break the logjam and actually empower them to go and identify with confidence and prioritize with confidence, the most efficient way to decarbonize the business. We talk about the transition, but actually the real opportunity here is to have a conversation about the optimal transition that we remove the most greenhouse gases from the business that we could with the least capital outlay into the business. And that has to be something that we need to prioritize here.

So, I say at a micro level that this empowers more management teams to have these conversations. And as far as replicate the journey that we've seen with Trafford at a macro level, I think it will be very, very important as more companies provide what we've described as 28 year forward looking guidance to the market. You know, when you start to make representation to the market that you will have removed 100% of the greenhouse gases from your business by the middle of the century, I think unfortunately there is a commensurate increase in the burden of proof that the market will expect from management teams. That is very bold guidance to provide to consumers of that data and where it is done rigorously and with the kind of output you start to see when you've calculated the projected abatement capacity, I think that goes a long way to reduce risk for the companies and capture the benefits that Fraser's outlined in terms of trust and confidence for employees, trust and confidence with customers, trust and confidence with regulators, but also capital providers is very important and I do feel that as we start to now initiate conversations about how we regulate issuer reporting associated with climate change, the ability to have a conversation about should that be a requirement when companies provide a long-term guidance to substantiate that guidance with projected abatement capacity, we think is a conversation that needs to be had and that the answer is, is probably it should be the conclusion. And maybe one last thing I'd add is a lot of companies, as they do this work, are identifying levers they have to decarbonize that are actually commercially very sensitive. And I think those are due to the marginal abatement cost curve work and identify a specific process at a specific price point is an important driver of that decarbonization strategy, have a natural reluctance to share that with the market and may be part of the beauty of the projected abatement capacity matrix is you don't need to be that granular.

You need to put it in the right scope of one, two or three, and you need to put it in the right bucket of economic. Now, economic at a higher carbon price, economic at a much higher carbon price. or not economic at all. And I think the ability to engage with consumers in a manner that's intuitive doesn't compromise any commercially-sensitive insights and is going to impart confidence in the consumer is an opportunity that we should seek to capture.

ASHLEY VOGELI

Thank you, Richard and Fraser, for joining me to discuss the Abatement Capacity Assessment Framework and the Trafford Centre's experience using it to help determine their decarbonization pathway. For all listeners. If you're interested to learn more about the Abatement Capacity Assessment Framework, please visit our website at cppinvestments.com.