Octagon

Responsible Investment

New Zealand Equities Fund (as at 31 December 2024)	Fund	Benchmark
% of Portfolio reporting Scope 1 and 2 emissions (by market value)	99%	100%
Weighted Average Carbon Intensity (WACI), tCO2e	33	33
Portfolio Emissions (Scopes 1+2), tCO2e per $1m invested	**18**	**18**

Listed Property Fund (as at 31 December 2024)	Fund	Benchmark
% of Portfolio reporting Scope 1 and 2 emissions (by market value)	98%	100%
Weighted Average Carbon Intensity (WACI), tCO2e	11	6
Portfolio Emissions (Scopes 1+2), tCO2e per $1m invested	**2**	**0**

New Zealand Equities Fund

LARGEST CONTRIBUTORS TO PORTFOLIO WEIGHTED AVERAGE CARBON INTENSITY

Listed Property Fund

LARGEST CONTRIBUTORS TO PORTFOLIO WEIGHTED AVERAGE CARBON INTENSITY

Climate-related disclosure regime in New Zealand

The high-level intention of New Zealand's climate-related disclosures legislation is to support a better allocation of capital towards activities that are consistent with a transition to a low-emissions, climate-resilient future.

New Zealand's climate-related disclosures are detailed in the following three standards (our recommendation is to start with Standard 3, followed by Standards 1 and 2.

- **Aotearoa New Zealand Climate Standard 3**; the standard's objective is to establish principles and general requirements to enable the provision of high-quality climate related disclosures.[2]
- **Aotearoa New Zealand Climate Standard 1**; the standard's objective is to enable primary users to assess the merits of how entities are considering climate-related risks and opportunities, and then make decisions based on those assessments.[2]
- **Aotearoa New Zealand Climate Standard 2**; this standard recognises that it may take time to develop the capability to produce high-quality climate-related disclosures, and that some disclosure requirements, by their nature, may require an exemption, this Standard provides a limited number of adoption provisions.[2]

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Even though the Aotearoa New Zealand Climate Standards disclosures regime only began back at the beginning of 2023, it is already subject to review. The Ministry of Business Innovation and Employment (MBIE) is currently engaging with a wide range of stakeholders, to consult on sensible improvements that could be made to New Zealand's regime[3] and the External Reporting Standards Board (XRB), the Government entity responsible for translating legislation into the actual reporting standards for reporting entities, also elected to re-engage with participants in the final quarter of 2024. Both reviews are an explicit acknowledgement that climate reporting entities (CREs) have been facing reporting challenges, in terms of both cost and complexity.

Octagon Asset Management (OAM) is the investment manager of the Octagon Investment Funds (OIF). Forsyth Barr Investment Management (FBIM) holds a registered managed investment scheme (MIS) licence and is the entity responsible for the climate-related disclosures of the OIF (which OAM is the investment manager).

Currently, if the total funds under management (FUM) within the schemes that FBIM is the Manager of exceed $1 billion, then FBIM will be defined as a CRE and required to report under the Climate Standards disclosures regime. FBIM expects to the exceed the $1 billion FUM mark at the end of the scheme year on 31 March 2025.

FBIM could elect to voluntarily adopt the New Zealand Climate Standards, ahead of its legal requirement to do so, but our collective thinking is not to early-adopt a series of standards that are highly likely to be significantly changed.

We think that New Zealand's reporting regime should be better aligned with Australia's (to mitigate the risk of listed entity Trans-Tasman flight) and that the cost of producing climate statements is excessive.

We'd also add that in the reports that we've seen it has been extremely difficult to compare activities and outcomes cross CREs (noting that we're experienced professionals). We've also wary of the large number of assumptions and general uncertainty in the information and data presented, meaning that any information is conditional and likely subject to material change, in our view.

New Zealand's climate-related disclosures legislation had good intentions for investors and capital allocators; its execution remains a work in progress. Something OAM will note in our feedback to MBIE during their current consultation on the regime.

[1 and 2] Reference NZ CS 1, NZ CS 2 and NZ CS 3

[3] Adjustments to the climate-related disclosures regime, MBIE, Discussion document December 2024

Our RI Policy in action: Fonterra

ESG integration refers to the process of incorporating Environmental, Social and Governance considerations into the investment decision process. Here at Octagon, we believe that material ESG issues will, in the long-run, impact company operating and/or share price performance. For this reason, evaluating ESG risks has always been a part of our investment process. We utilise our own ESG Risk Assessment framework to help us identify these risks (and opportunities). Through this framework we make use of company disclosures, data from ESG data providers and external ESG ratings. One example of this policy in action relates to an exposure in our New Zealand Equities Fund: dairy co-operative Fonterra (which we access through the Fonterra Shareholder's Fund FSF:NZX).

A starting point for our analysis is a company's Forsyth Barr CESG rating, which in this case identifies that the company's weakest area is in the 'carbon' category and that another material consideration relates to capital structure - investors in FSF do not have voting rights in relation to Fonterra Co-operative Group (FCG:NZX). Only farmers supplying Fonterra have the right to vote on core operations. Not surprisingly, when shares in the same economic entity have different rights, the shares trade at different values.

A weak score in the carbon category makes sense; Fonterra is New Zealand's largest producer of greenhouse gas emissions (directly from factories and transport, but more meaningfully, indirectly through the on-farm emissions from its suppliers). Despite our exposure to Fonterra being only ~1.4% of the New Zealand Equities Fund it is responsible for ~14% of the fund's Scope 1 and Scope 2 emissions.

Clearly, greenhouse gas emissions are a material ESG risk for the company across several fronts. Directly there could be cost imposts from acquiring carbon credits to neutralise emissions. There could be less direct impacts from reduced access to global markets or price discounts on international platforms. Substitution effects where milk is swapped out of some nutrition based options is also a potential outcome of not improving carbon outcomes. All of the above potential outcomes are currently uncertain and hard to value. When an outcome is highly uncertain, we need a higher return (usually through a lower share price) than a more certain one.

The flipside to an ESG risk, however, is often an ESG opportunity, generated by the way a company manages its ESG risks. Through review of company disclosures, we can see Fonterra has set ambitious emissions reduction targets and has made actual progress towards them

at a time when some other companies are walking-back previous commitments. For example, Fonterra has a target to reduce Scope 1 and 2 emissions from manufacturing operations by 50.4% (2018 baseline) by 2030. As of 2024 they have achieved a reduction of 18.5%, thanks to actions such as converting several boilers from coal to wood pellets. FSF is also investing in and trialling many innovative treatments and processes to reduce on farm emissions. Should any of these be materially successful, not only would it lower emissions, but it could also be a significant earnings contributor as the technology is commercialised globally.

We regard FSF's capital structure as a traditional 'Governance' risk. There are no specific steps Fonterra can take to remove this risk inherent within FSF in its current form. The risk should therefore manifest in the share prices of the two securities that give exposure to the economics of the Co-op. If it is seen that the structure favours one group of shareholders over another, then the disadvantaged shareholders need a higher return to compensate them for the higher risk. Successive years of actions by the board to act in the interests of all shareholders equally can reduce the size of the extra return needed.

The purpose of our ESG Risk Assessment framework is to draw an analyst's attention to specific issues, which we can incorporate into our overall view of the company and provide specific topics to address in company engagement. To us, ESG integration is a way to 'hone-in' on some of the risks that have always been present in financial markets, such as Governance risks, while also allowing us to dig deeper into some potential 'newer' risks such as carbon emissions and carbon pricing.

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