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TCFD Entity Report LMR Partners LLP

June 2024

lmr partners

Compliance Statement

The disclosure set out in this report for LMR Partners LLP complies with the requirements under Chapter 2.2 of the FCA's ESG Sourcebook, and other relevant sections.



Shane Cullinane

Partner and Chief Operating Officer, LMR Partners LLP

Introduction

This report sets out LMR Partners LLP's ("LMRs") disclosures in accordance with the recommendations of the Taskforce for Climate-related Financial Disclosures (TCFD), and is consistent with the four pillars (Governance, Strategy, Risk Management, and Metrics and Targets), and associated disclosures laid out in the TCFD recommendations, the TCFD Annex, as well as other supplementary guidance.

Governance

At LMR, oversight of risk factors is strictly driven based on whether the risk factors in question are likely to be financially material to the performance of the specific asset classes managed. For this reason, LMR does not privilege oversight or attention based on how risk-origins are labelled – such as whether they are 'climate-related' – but instead regards all potential sources of risk and opportunity through the lens of what is likely to impact investment performance.

With respect to financial materiality, LMR notes that for the majority of asset-classes represented in the portfolios managed - over 88% of which are derivatives, approximately – there is no established consensus methodology for reliably and consistently evaluating climate-related risk. Moreover, LMR notes that these derivative instruments are, by-and-large, excluded from the PCAF methodology recommended within the TCFD Annex (and, by extension, the FCA Handbook), for assessing key metrics like carbon intensity.

Processes for Oversight

Due to these dual considerations – focus on financial materiality, and the absence of reliable climate assessment methodologies – LMR has not established a dedicated process for the escalation of climate-related risks in particular. Accordingly, climate-related risks are not expressly considered when reviewing and guiding strategy, major plans of action, risk management policies, annual budgets, or business plans. Neither are climate-related risks expressly, or formally, considered when setting the firm's performance objectives or when overseeing major capital expenditures, acquisitions, or divestitures.

Instead, potentially material risks – irrespective of category – are channelled through LMR's Risk Committee, which includes, and has active participation from, all individual Partners of the firm that comprise the firm's governing body.

In relation to climate-related goals, LMR cannot set meaningful or credible climate-related targets in the absence of accepted methodologies by which to baseline the current state, and track progress.

It is noted that this approach does not exclude or dismiss consideration of climate-related factors, in principle. Instead, it limits consideration to circumstances in which the Risk Committee and, by virtue of individual Partner membership of the Risk Committee, the firm, believes there is a credible methodology for appraising the degree to which such factors are, or are not, material to investment performance.

Management Role in Assessing/Managing Climate-related Risks and Opportunities

The absence of widely adopted and recognised climate assessment methodologies across most of the asset classes managed limits the extent to which management can credibly form meaningful assessments of climate-related risks and opportunities.

LMR does collaborate with third-party advisors and consultants, who assist in keep in the firm apprised of developments in climate risk assessment that may be relevant to asset classes managed, and therefore to the firm's disclosure obligations under FCA regulations going forward. LMR actively seeks out information on regulatory developments and evolving industry standards from third parties, ensuring that the firm's governance practices align

with prevailing expectations. These regulatory developments will be raised by LMR's compliance team to the Risk Committee, if deemed relevant or appropriate.

Strategy

As referenced in the 'Governance' section, there is currently no widely-accepted, reliable methodology for assessing the climate risk exposure of derivative instruments, which are several degrees removed from the underlying assets or economic activities that may be directly impacted by climate change and the transition to a low-carbon economy. This precludes formalised identification of climate-related risks and opportunities other than at a very general or qualitative level.

LMR considers short-term time horizons to be 1-3 years, medium time horizons to be 3-5 years, and long-term time horizons to be 5-10 years. These horizons are based on the typical holding periods and maturities of the derivatives instruments in managed portfolios, as well as the firm's overall strategy and business planning cycles.

Operationally, we know that over the medium- to long-term, suitably credible - and widely-accepted - methodologies may emerge for assessing financially material climate-related risks across traded asset classes. Assuming this occurs, the availability of such methodologies may introduce an element of market risk to the extent that asset managers adopting and implementing such methodologies could be expected to gain a competitive advantage (due to information asymmetry), over those who do not, enabling them to capitalise on improved visibility of climate-related risk and opportunity factors. The advent of such methodologies, if subsumed into the PCAF framework, would also trigger expanded reporting obligations in relation to the carbon intensity of portfolio holdings.

LMR does not anticipate climate-related issues arising over immediate or short-term time horizons.

In relation to sectoral and geographical risk, LMR's investments are globally diversified and span multiple sectors. A insignificant percentage of holdings are exposed to the Oil & Gas industry as a whole. Portfolio exposure is not concentrated in any geographic regions or industries in which we expect climate-related risk factors to pose financially material impacts. LMR will continue to monitor this aspect and refine our analysis as more robust data and assessment tools become available.

Strategically, LMR deem that the best response to this outlook is to stay attuned and apprised of the latest developments in climate risk assessment methodologies that intersect the asset classes of which our portfolio is comprised. This entails regular dialogue with counterparties, monitoring of market trends and regulatory developments, and staying abreast of emerging research and methodologies for assessing climate risk in financial portfolios.

At this time, however, we are unable to identify more specific climate-related issues that we believe are likely to have a material financial impact on our firm in the short-, medium-, or long-term.

Given the considerations outlined above, LMR have not identified any climate-related issues that have materially affected its business, strategy, or financial planning to date. LMR's products and services, which heavily utilise derivative instruments, have not undergone significant changes due to climate-related considerations, nor have we made substantial investments in climate-related research and development, adaptation or mitigation activities, or modifications to our operations.

Climate-related issues are not currently a direct input into our financial planning process, as we have not identified any that we believe will have a clear, quantifiable impact on our revenues, costs, assets, or liabilities over our planning horizon. We do not utilise climate-related scenarios to inform our strategy and financial planning at this time.

Impact on Trading Strategies

In theory, it is possible for climate-related factors to affect rates trading strategies, to the extent that acute climatic tail-risks, such as extreme weather events, could cause significant damage that central banks consider temporarily lowering interest rates (or slowing the pace of rate hikes), so as to stimulate post-damage economic recovery. While there is some limited precedent for this (e.g. Fed moderation in pace of planned rate hikes following Hurricane Katrina, or Bank of Japan easing of monetary policy in the aftermath of the 2011 tsunami), extreme weather events

do not typically alter the course of a national economy over the medium term, and central banks generally tend to continue with their existing monetary policy path rather than making unscheduled rate cuts. In reality, therefore, the likely impact of such events on rates trading is expected to be low.

Climate-related and GHG Reduction Targets

LMR have not made any commitment to GHG reduction given that – absent credible methodologies for assessing the GHG profile of derivative instruments – there is no reliable means by baselining current carbon intensity and, therefore, no mechanism by which we can either set targets, or track progress towards them.

However, as a firm that is intrinsically focused on risk management and the careful evaluation of all factors that could impact investment performance, we are committed to staying apprised of ongoing developments in climate risk assessment where these introduce credible, and widely accepted, methodologies that intersect the asset classes primarily traded.

Due to the challenges in quantifying the exposure of derivatives to climate-related risks, we have not conducted a formal scenario analysis to assess the resilience of our strategy under different climate outcomes, such as a 2°C or lower scenario. We acknowledge that our strategy may need to adapt in the future as the transition to a low-carbon economy progresses and as the physical impacts of climate change become more apparent, but the specific implications for our business remain uncertain at this time.

As a firm, we are committed to maintaining a resilient and adaptable strategy in the face of all types of risks, including those related to climate change. We will continue to monitor developments in this area and will adjust our approach, as necessary, to ensure the long-term success of our business and the best interests of our clients.

We recognise that the assessment and disclosure of climate-related risks is an evolving area, and we are committed to enhancing our understanding and transparency over time. As more robust data, assessment methodologies, and industry best practices emerge, we will work to align our approach with these advancements and provide our stakeholders with increasingly decision-useful information on how we are managing climate-related risks and opportunities.

Risk Management

LMR does not employ distinctive or specialised processes with respect to the identification or assessment of climate-related risks.

As stated in earlier sections, the assets managed are principally comprised of derivative instruments. At the time of writing, there does not currently exist any credible or widely accepted methodologies for identifying, tracing, characterising, or assessing climate risk exposure in relation to this asset class. This is partly due to the manner in which derivative instruments are often several degrees removed from underlying assets or economic activities that may be directly impacted by climate change and the transition to a low-carbon economy.

To the extent that managed assets are comprised of equities or corporate debt assets (including corporate bonds and convertible bonds), the combined exposure of these assets amounts to less than 1.5% of overall assets and is split between more than 16,000 individual holdings. On a per-holding basis, this exposure averages less than 0.00001%, which is prohibitively small for any form of meaningful engagement on climate-risk or any other issue.

These conditions prohibit meaningful identification and assessment of climate-related risks across all products and investment strategies. There are no applicable exceptions in the case of any particular investment strategy or product.

Materiality determinations are based on assessments of the potential financial impact of climate factors relative to other risks faced by the firm. The prioritisation process ensures that climate-related risks are appropriately integrated into decision-making processes and risk mitigation strategies.

As mentioned previously, LMR collaborates with a third-party advisor who specialises in climate risk assessment, to leverage existing risk classification frameworks and definitions, ensuring alignment with evolving industry best practices, enabling LMR to refine its risk analysis as credible methodologies for assessing climate risk evolve.

Metrics and Targets

LMR does make limited use of GHG emission metrics in relation only to those asset classes which are:

- a) Indicated by the PCAF framework; and
- b) Where we have practical access to reliable GHG emission / emission intensity data.

LMR is aware that GHG emissions data (in relation to equities and corporate debt) may be used, in principle, as an indicator of corporate exposure to potential carbon taxation and other transition factors which may, in theory, serve to limit, or otherwise constrain, the relevant financial performance of those assets. However, as stated in earlier sections, LMR's exposure to these asset classes amounts to less than 1.5% of overall assets. In practice, therefore, while LMR tracks GHG emission metrics where required by regulation, these metrics cannot be said to guide our risk assessment in any substantive manner or to locate opportunities, or to inform our strategy.

Likewise, TCFD recommendations calls for firms to consider including metrics on climate-related risks associated with water, energy, land use and waste management, where relevant and applicable. TCFD also calls for firms to provide their internal carbon pricing, where relevant. In LMR's case, these additional climate risk related indicators are not relevant or applicable to the vast majority of assets managed and, therefore, we do not expect them to materially impact financial performance. For this reason, these metrics – along with GHG emission metrics – do not feature in remuneration policies at the firm.

To the extent that LMR discloses GHG emission metrics for asset classes covered by the PCAF framework, we will track how these evolve over historic periods and will include the time series in future reports, as required under regulation.

Portfolio-level GHG Emissions

The following table displays Scope 1, 2 and 3 GHG emissions intensity figures in relation to all holdings that fall within the ambit of the published PCAF methodology referenced in the TCFD Annex (with the exception of sovereign debt assets).

GHG data on all PCAF assets (except sovereign debt)	
Scope 1 WACI (mtCO ₂ e/\$M)	4.35
Scope 2 WACI (mtCO ₂ e/\$M)	0.59
Scope 3 WACI (mtCO ₂ e/\$M)	22.72
Scope 3 WACI (mtCO ₂ e/\$M) Downstream	20.84
Scope 3 WACI (mtCO ₂ e/\$M) Upstream	1.88

Calculated GHG emission data on sovereign debt assets relies on information that has been sourced from IMF and World Bank registers. It is displayed separately, as it was not possible to disaggregate by Scope.

GHG data on all PCAF assets (except sovereign debt)	
All-scope WACI (mtCO ₂ e/\$M)	0.16

The aggregate of WACI figures across all PCAF assets, including sovereign debt assets, is provided below:

GHG data on all PCAF assets (except sovereign debt)	
Total WACI of all PCAF assets (mtCO ₂ e/\$M) (including sovereign debt)	27.82

Historical Periods

As this is LMR's first TCFD disclosure, there is no historical or baseline data from which to perform trend analysis.

Notes on Data Availability

It has already been noted that GHG data in relation to sovereign debt was not available in scope-disaggregated form. However, aggregated data coverage on sovereign debt is 100%.

Data coverage in relation to other PCAF assets varies, peaking around 70% within Scope 2 where grassroots reporting is most comprehensive.

LMR commit, tentatively, to improving the current level of data coverage for those asset classes covered by the PCAF framework such that, over successive years, we close data gaps and approximate full coverage. Our commitment is tentative and depends on the ongoing availability – and methodological comparability – of GHG emissions data.

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