BRITISH AIRWAYS PENSIONS

Responsible Investment Report 2019

Airways Pension Scheme (APS)
New Airways Pension Scheme (NAPS)

Foreword

This report highlights how the Trustees have included environmental, social and governance (ESG) activities in their investment approach. We, British Airways Pension Investment Management Ltd (BAPIML), carry out responsible investment activities for the Airways Pension Scheme and the New Airways Pension Scheme (the Schemes). This report summarises these activities from 1 April 2018 to 31 March 2019.

The Trustees have achieved significant ESG milestones in this reporting period.

New ESG committee

The Trustees of both Schemes formed a joint ESG committee in December 2018. This committee supports the main boards to develop ESG responsible investment activities in line with regulations and industry standards.

Updated Scheme documents

The Schemes' statements of investment principles (SIPs) have been updated to:

- reflect the new responsible investment policy, and
- meet the Department for Work and Pensions' requirements in communicating the ways they have considered financially relevant ESG factors.

These have been published on the Scheme websites.

New investment beliefs and responsible investment policy

The ESG committee's first task was to develop a set of investment beliefs and a responsible investment policy. Over six months, the committee worked with consultants, advisers and us to form its beliefs and draft a new responsible investment policy. The sponsor and Trustees then approved the policy.

Constant changes in the responsible investment industry

The responsible investment industry is changing quickly. We and the ESG committee expect that our responsible investment activities will continue to evolve.

Front cover: South Quay Development

BRITISH AIRWAYS PENSIONS

Contents

Glossary

Affiliations	Affiliations are formal connections with industry groups which aim to promote a shared objective or purpose.
AGM	Annual general meeting.
Biodiversity	Refers to the variety of life on earth, including plants, mammals and micro-organisms.
CDP	Formerly known as the Carbon Disclosure Project, CDP is a not-for-profit charity that runs the global disclosure system for investors, companies, cities, states and regions to manage the effect they have on the environment.
Cross-shareholding	Cross holding happens when a public company owns stock in another public company. So, technically, cross-shareholding is where listed companies own shares issued by other listed companies.
G20	An international forum for governments and central banks from the European Union and 19 other countries.
Governance	Governance is the term used to describe how organisations are directed, controlled and led.
Investee companies	A company or organisation in which an investor makes a direct investment.
Investment beliefs	Investment beliefs describe the Trustees' views on how investment markets work and set the direction for investment policy, investment practice and organisational culture.
Pre-emptive rights	Pre-emptive rights give a shareholder the right to buy extra shares before they are available to the general public (if shares are issued in the future).
Proxy voting	Proxy voting is where a person or organisation nominates someone to vote on their behalf if they are unable to vote in person.
Remuneration	Remuneration is payment received for services or employment. Remuneration can include base salary, bonuses and any other financial benefits an employee receives.
Sponsor	The Schemes' sponsor is British Airways Plc.
Stewardship	Stewardship is the job of supervising or taking care of something, such as an organisation or property. From an investment perspective stewardship refers to working with investee companies to promote good governance and create long-term value for shareholders. Voting is an important part of active ownership and gives shareholders a way to influence company management.
Stewardship Code	The Stewardship Code is a part of UK company law and is designed to protect the interests of British savers and pensioners by making sure their investments are managed responsibly.
Sustainability	The effect of causing little or no long-term damage to the environment.
Trustees	The Trustee of the Airways Pension Scheme (the APS Trustee) and the Trustee of the New Airways Pension Scheme (the NAPS Trustee).

1. Listed Equity and Corporate Bonds

Stewardship, monitoring, working with others and proxy voting

Stewardship activities are a key part of our responsible investment practice. They focus mainly on:

- monitoring and working with investee companies in the portfolios, and
- proxy voting in relation to those investments.

Our involvement with other companies focuses on helping fund managers to better understand a company's financial performance and long-term strategy. We also work with company management to encourage changes in corporate behaviour, particularly if this will increase the value of the Schemes' holdings.

We manage and apply the Schemes' proxy voting rights, using Institutional Shareholder Services (ISS) for research and voting recommendations to support this process. This section includes case studies which highlight our responsible investment activities in listed equity and corporate bonds. It also provides a snapshot of this year's global proxy voting activity.

Listed Equity

UK

Governance concerns in the UK have focused on remuneration and director elections.

Our UK team votes on every resolution at every shareholder meeting that takes place for companies we hold investments in. In the year to 31 March 2019, we voted at 186 meetings. In 18% of those meetings, we voted against management on one or more resolutions.

Remuneration and director elections have been the main areas of concern. For director elections, there has been a small change in emphasis, with issues arising from non-executive directors holding too many positions at other companies ('overboarding') rather than from the length of directorships and the independence of directors.

We also have an active engagement programme with the companies we invest in. Our involvement with companies usually takes place at board level with the chief executive or chief financial officer. Our UK equity team is unusual in that it has, for many years, managed its small and medium-sized company exposure as a separate sub-fund. The number of companies we work with in any year varies between 150 and 250.

Board Structure at Euromoney PLC

It is common for voting activity to span a number of years to have a meaningful effect in the UK.

Our UK equity team's relationship with the international media company Euromoney plc is an example of long-term involvement. We made our initial investment in March 2010 at a price of £5.

Euromoney had been a quoted subsidiary of the Daily Mail and General Trust (DMGT), and DMGT had kept a shareholding of more than 50% in the company and a strong presence on its board. This board presence meant that it was difficult for the executive team to make independent decisions and structure key board committees (audit and remuneration). It also undermined minority shareholders' confidence in the company's pay policies.

We voted against resolutions at every AGM from 2010 to the present. We maintained a productive relationship with the executive management team during this time. But we also expressed views at every opportunity that it would be in all shareholders' best interests if DMGT reduced its stake to below 50% and allowed Euromoney to move towards a more conventional corporate profile. By the time of the 2019 AGM, we were working with an entirely new executive team and DMGT had sold all of its shares in Euromoney.

As a result of this the Euromoney board structure has improved, with genuinely independent non-executive directors and an acceptable pay structure. The stock price at the time of writing is £13.86.

DMGT may have sold its shares regardless of minority shareholders' opinion. However, our long-term involvement with the Euromoney executive management team meant that they agreed fully with our views. And the collective actions of the minority shareholders undoubtedly strengthened their position when it came to discussions with DMGT.

North America

Shareholder proposals

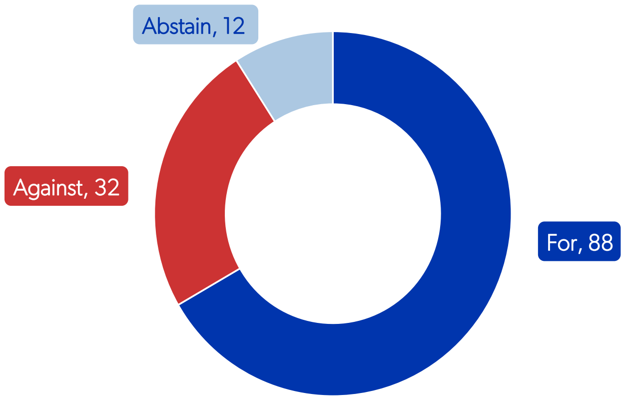
Shareholder proposals are filed by shareholders and not by the company's management. If regulation is slow to change, for example, shareholders can make a proposal to push for social or environmental progress in the market.

In North America, we voted on 132 shareholder proposals – more than in any other region. The pie chart below shows how we voted.

Gender Pay Disclosure at Facebook

We supported a shareholder proposal on gender pay disclosure at Facebook. We believe that increasing diversity reduces risk as it makes sure a range of views are heard. This in turn supports better decision-making and improved returns for shareholders.

Total number of shareholder proposals voted in North America



We supported a range of proposals calling for more information to be provided on inequality in business relating to gender, ethnicity and background. This was to highlight current diversity issues and allow shareholders to monitor management's progress in tackling them. (In comparison to the US, the UK has taken the lead internationally by requiring companies with more than 250 employees to publish their gender pay balance.)

This information has been helpful in highlighting unfair pay and opportunities in many US companies with UK operations. It has highlighted the technology industry as having a major issue with diversity and equal pay and opportunities.

Diversity at Amazon

There has been a major increase in the number of diversity-related shareholder proposals in North America. We supported shareholder proposals at Amazon for an independent chairperson on its board and a diversity policy for the board. Amazon's board lacks ethnic diversity and is under-represented by women. Having an independent chairperson will also help to increase accountability and reduce risk at a company that is often in the public spotlight.

Thanks to shareholder activity, Amazon announced that its nomination and corporate governance committee will include a list of diverse candidates, including women and minorities, for all director vacancies. As a result of this, the shareholders felt their concerns had been met and withdrew their proposal.

Europe

Politics and regulation drive sustainability in Europe.

During 2018, European countries stepped up their efforts to combat climate change. This was particularly driven by the increased support for green political parties across Europe. As a result, other political parties were forced to act and adopted environmental policies focusing on climate change. This shift in policy has led some of our investee companies to adjust their targets and move towards a way of working that is less damaging to the environment.

Agriculture is another area of change towards greener practices in Europe. The G20 has tasked Germany with developing an arable farming plan by 2019. France is also working to encourage the Environment Council of the European Union to protect biodiversity.

New energy initiatives in Europe provide investment opportunities

Both the German and French governments announced new energy plans in 2018. Germany will end coal generation and France will end carbon-based generation as part of a climate plan. Both of these have prompted change at leading utility operators in the European portfolio.

- The German electric utility company E.On sold Uniper, completing its exit from generating conventional energy and focusing in future on renewable energy.
- Another German electric company, RWE, will soon stop producing lignite coal.
- The French electric company Engie pledged to support the French climate plan by investing in low-carbon technology.

These trends have made the utility sector more interesting to us for investments as society continues to demand more electricity and renewable energy.

European policy shifts towards more sustainable practices in agriculture and chemicals

Yara, a Norwegian chemical company, now promotes developing sustainable farming techniques, for example:

- using data and digital tools to increase yields
- using green ammonia to produce fertiliser, and
- using waste materials to recycle and limit water usage.

In 2018 the German chemical company BASF began to use more digital technologies to:

- manage its research and development
- improve its use of resources and reduce its harmful effect on the climate, and
- increase food yield and nutrition.

Japan

Increased pressure from institutional investors maintains progress on diversity and achieving an independent board.

During 2018, we voted against 34 proposals for the Japanese portfolio. Fourteen of these proposals were director elections where we considered that the board was not independent enough. We will vote against a proposed director if they are not classified as independent, particularly if they are connected to the company and being elected to the audit committee.

Pressure from institutional investors for independent board members

We voted against two director elections at Sysmex Corp, a Japanese healthcare company. We did this because only 16.7% of board members were independent.

Both proposals passed, but 12% of the company's shareholders agreed with us and voted against. At the AGM in 2019, the company proposed an additional outsider, classified as independent, so board independence has now improved to 25%.

We believe the company's board structure can improve further but appreciate the steps it has taken to meet shareholders' expectations.

Japanese company boards have traditionally been known for their low levels of independence and poor diversity. When outside directors were appointed, they were often drawn from the company's keiretsu (business network) and had long-standing ties with management through close banking or commercial relationships. However, this is now starting to change. According to ISS, in their 2018 proxy voting review, 99% of Japanese boards now have at least one independent director (from outside the company) and in 38% of boards, at least one-third of the members are independent. This is not yet at an acceptable level (in developed markets, we expect more than 50% of board directors to be independent) but it is a great improvement.

We are also starting to see an increase in the number of female board directors appointed. Board-level representation has been limited by the low number of women in senior roles. This has been hard to change since the ambitious inclusion targets set by Prime Minister Abe in 2013 were reduced. However, it is encouraging that 31% of Japanese boards now have at least one female director, up from 27% in 2017 and just 9% in 2012.

Developed and Emerging Asia

Governance standards throughout Asia are constantly evolving.

The most common issues stem from companies owned by the state or by the families who founded them (founding families). Often they have underestimated the market's desire for independent, suitably qualified boards to provide direction, encourage good capital management and produce good shareholder returns. In Asia, most of our votes against management proposals take place when:

- very high levels of stock have been issued without the protection of pre-emptive rights, or
- directors are not suitably qualified or sit on too many boards.

Corporate Structure at Hyundai Motors

Hyundai Motors manufactures good-quality vehicles but has a persistently poor corporate structure and governance standards. Cross-shareholding is common in Korean companies as founding families try to keep control when the number of shares they hold falls. Hyundai's profitability has been balanced by these factors, leading to low returns on equity and shares trading at a discount when compared with its competitors.

We have consistently encouraged Hyundai management to find a solution to cross-shareholdings and introduce more independent directors. One investor proposed two suitably qualified outside directors to strengthen the board's expertise and sit on the audit committee, and we voted for them. Unfortunately the candidates did not receive the number of votes required.

We believe Hyundai can increase its value if the cross-shareholding is reduced and the company stops investing in non-core projects.

Emerging Markets

We work with companies to improve communication.

Emerging markets is the area where we vote against management most often. It is also the area where we see the greatest number of special meetings.

During 2018 we voted at 251 meetings. At these meetings we voted against management on 348 proposals, representing just under 41% of the total number of votes we made against management.

Corporate governance practice in emerging markets often falls below standard due to poor communication and low levels of board independence. For example, when a company fails to communicate the name and relevant information for a proposed director, we will vote against their election. Where possible, we try to improve communication standards by working with investee companies.

Improving communication in an emerging market

Dino Polska is a food retailer based in Poland. At its 2018 AGM, the company proposed to elect five new supervisory members to the board but did not provide the candidates' names. As no names were provided, ISS recommended voting against the unknown board members and we agreed.

We have had an active relationship with the company since it became a public company by selling its stock to the general public through a new process called an 'initial public offering'. So, when we voted against the new board members, the company contacted us to find out why. We explained that investors expect a higher level of information and would like to know the person they are electing for each position. The company then assured us that in future all nominee names would be made public before AGMs.

During the most recent AGM, all names of candidates were announced before the meeting and ISS recommended voting for all items on the agenda.

Corporate Bonds

During 2018 popularity for green, social and sustainability bonds continued to rise.

Green, social and sustainability bonds usually have the same status as 'non-green' bonds but the investment can only be in a green or social purpose. The increase in the number of these bonds highlights the investment industry's appetite for responsible investment.

Positive feedback to these features from traditional corporate bond funds and ESG specific funds has allowed companies to issue bonds on slightly better terms (lower interest rates). International organisations, utility companies and housing associations have been among those who have taken advantage of this.

With the increased focus on how green bonds are defined, the International Capital Markets Association (ICMA) produced guidelines to make the process clearer and simpler. The ICMA Green Bond Principles provide bond issuers with guidance on the main issues involved in launching a credible green bond. They also support investors by making sure they receive the information they need to assess the environmental effect of their green bond investments.

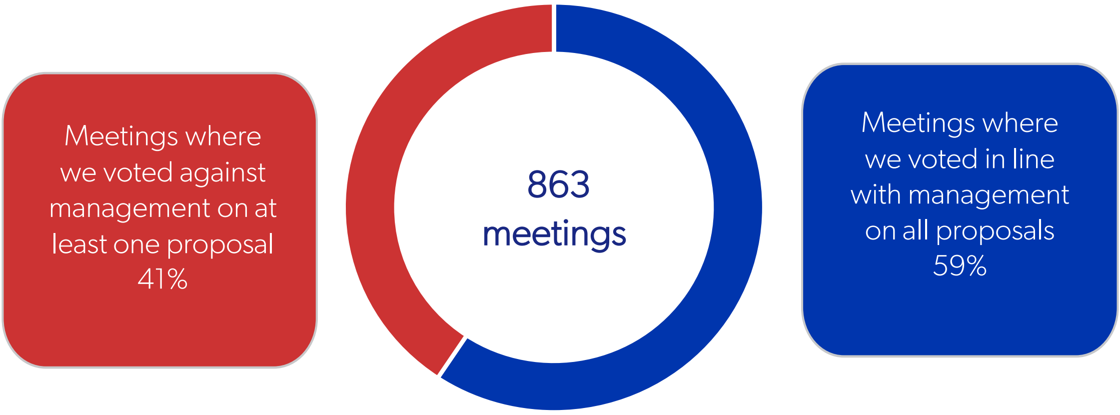
Green bond issuer follows ICMA principles

Anglian Water is one of the green bonds we have invested in. These bonds follow the ICMA Green Bond Principles. Anglian Water will use the proceeds from these bonds to:

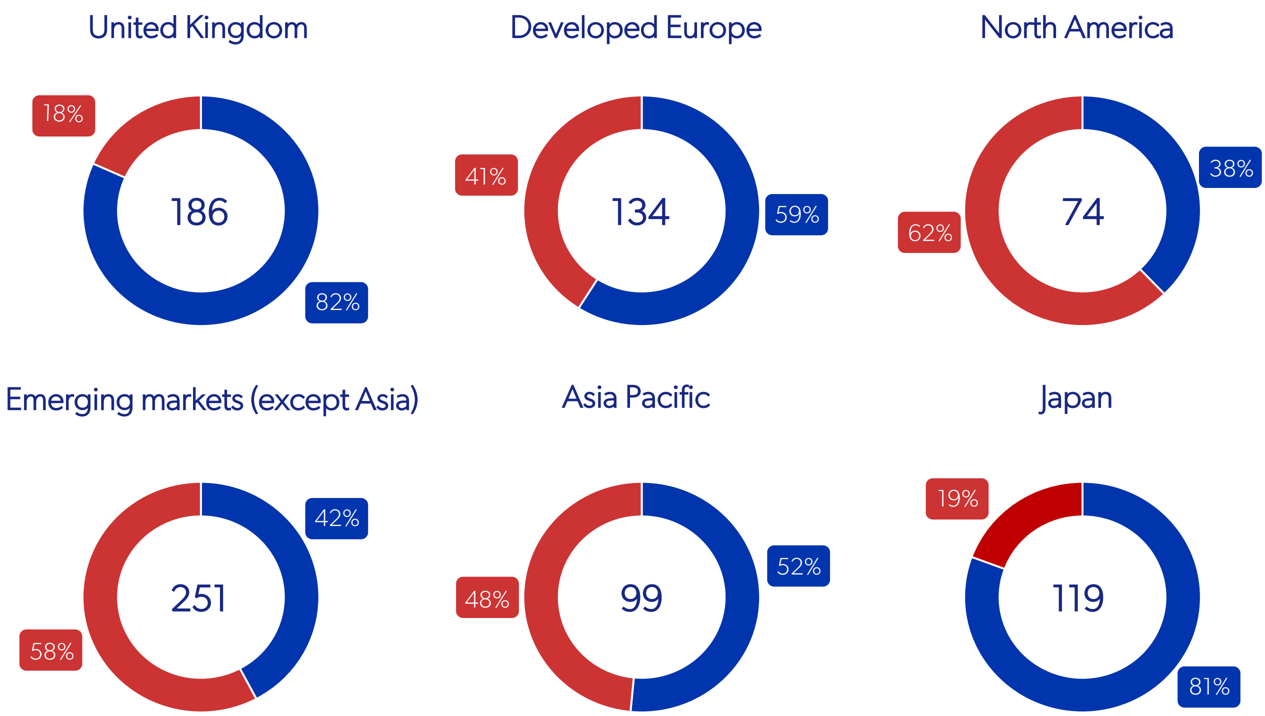
- reduce levels of greenhouse gases that are released by reducing unnecessary water usage and becoming more energy-efficient
- tackle the long-term effects of climate change (for example, flood risk), and
- develop water-recycling projects.

Shareholder Meetings

Between 1 April 2018 - 31 March 2019 we voted at shareholder meetings. On average we asked to vote on 14 proposals at each meeting. During this financial year, we voted against management on at least one proposal at 41% of the meetings.



Shareholder Meetings by Region



Analysis of proposals voted on

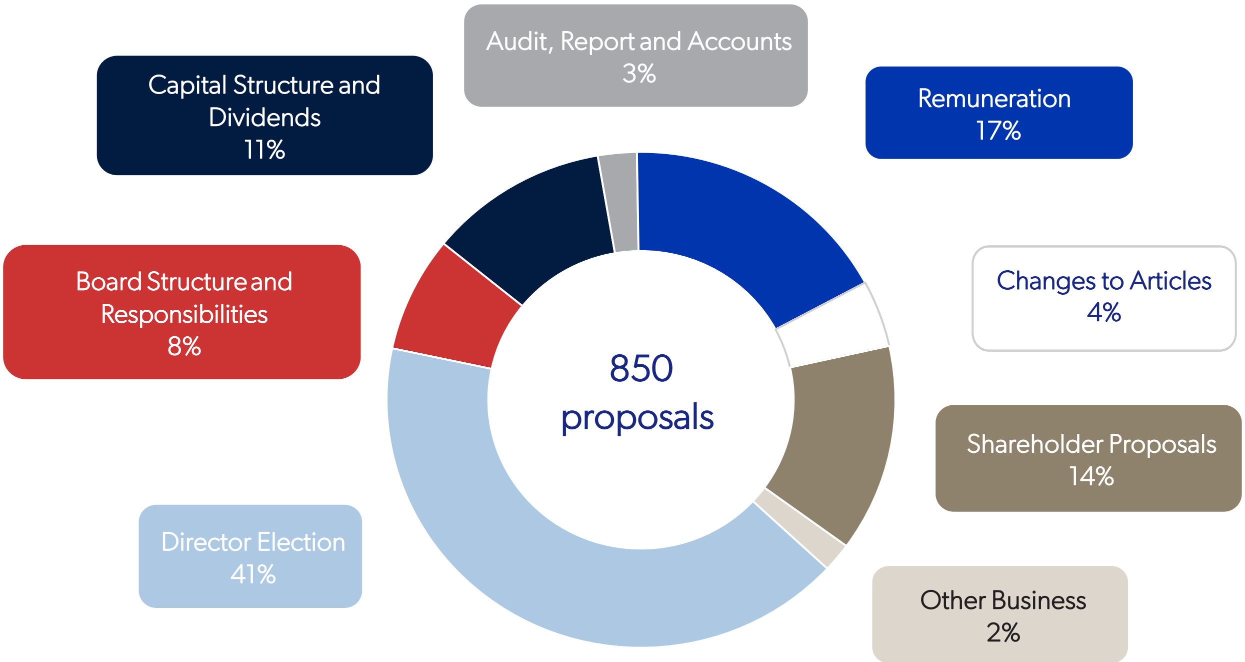
Proposals where we voted against management

At these 863 shareholder meetings we voted on 11,586 individual proposals in total. We voted against management on 850 proposals, as shown by the first pie chart below.

Proposals where BAPIML voted against management by category

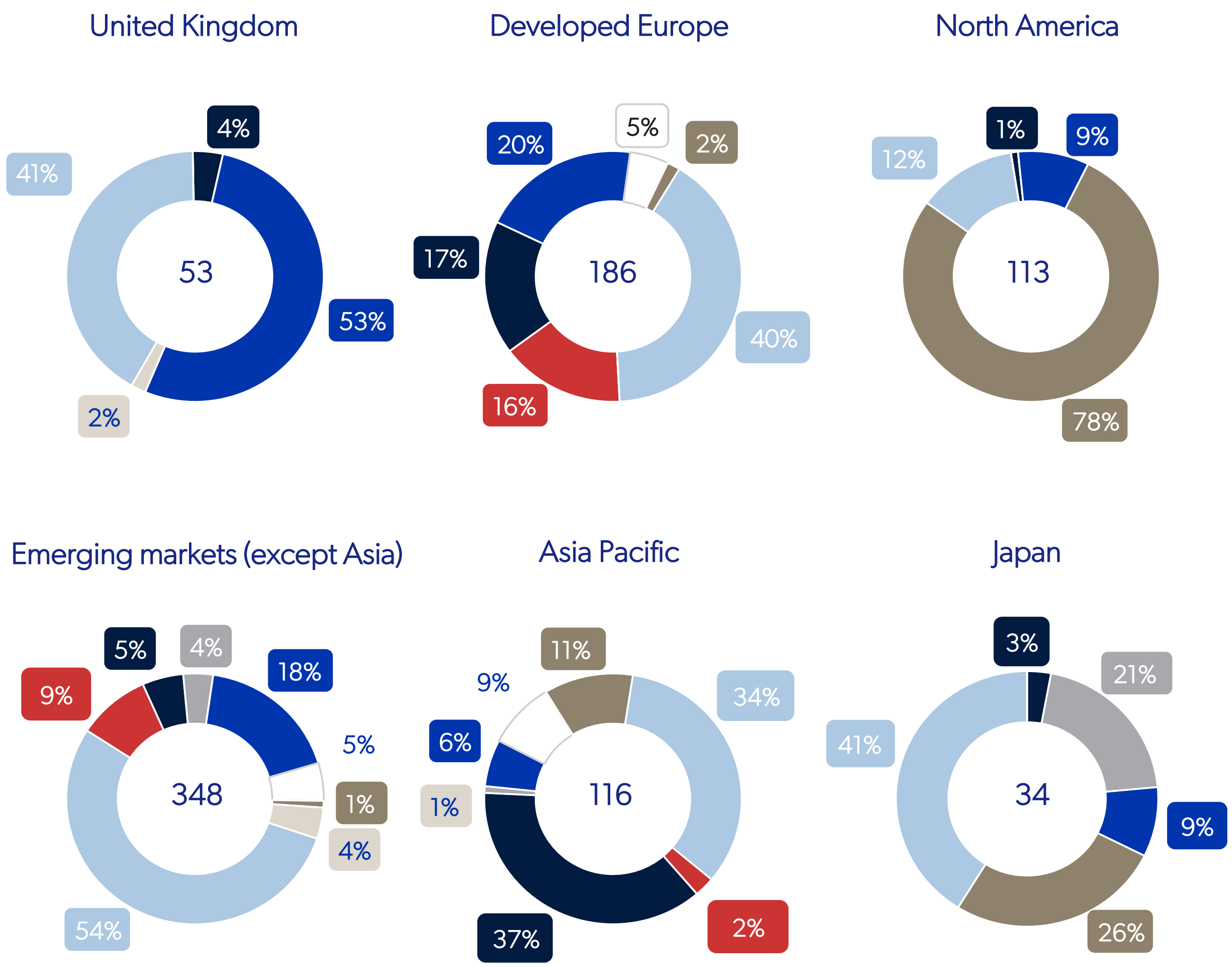
The pie chart below shows the 850 proposals we voted against by category. Director election is the most common area where we disagreed with management. This was often because of:

- our concerns about the director's lack of independence from management
- fears they may be overstretched by sitting on too many boards, or
- concerns that they were not acting in the best interests of shareholders.



Analysis of proposals voted on (continued)

Proposals where we voted against management by region



Proposal Categories

Remuneration	Director election	Shareholder proposals
Capital structure and dividends	Board structure and responsibilities	Changes to articles
Other business	Audit, report and accounts	

2. Private Equity and alternatives

With private equity and alternatives industries, we carry out most of our ESG activities before investing – during our research into managers or funds. We take great care during this process to examine governance, communication and transparency issues, as once the investment has been made, there is little flexibility to change terms or influence the investment policy.

The private equity and alternatives industries are increasing their ESG efforts.

The private equity and alternatives industries continue to expand their resources and focus on ESG. More and more firms are hiring ESG professionals and reviewing related matters as part of their quarterly or annual reporting. European managers are still ahead in acting on and monitoring ESG matters. However, North American managers are becoming more focused on this area.

Limited partners like us often ask general partners (the fund managers) to demonstrate they have a structured approach to managing ESG risks and opportunities. This has led many general partners to formalise their ESG programmes so that they can manage ESG issues more effectively.

As part of our own ESG efforts, we have added an ESG section to the questionnaire we send to each manager before committing to a new fund. We also cover ESG as a separate section in internal investment recommendations. This helps us make sure that funds making new investments are considering ESG risks and taking suitable steps to tackle any issues.

ESG is still relatively new to the private equity industry. We expect that larger managers will be more active with ESG matters in their portfolio as they will have greater resources – for example, to hire dedicated ESG professionals and invest in systems to manage ESG issues. However, smaller managers are increasingly building their ESG resources too.

For example, we are invested in a fund that has an ESG committee. The committee meets several times a year to review its activities and those of its portfolio companies. Committee members are professionals from across the firm, including investment professionals representing each of the geographic areas and sectors they invest in, and other members of the team.

The committee decides the firm's approach to ESG issues, including setting ESG priorities and appointing investment teams to promote its ESG strategy. Members of the committee seek out opportunities to improve their own ESG knowledge by attending conferences, holding meetings with investors and management teams, and keeping up to date with the latest publications.

An investment fund's ESG approach in practice

One example of an investment meeting ESG criteria is a contract logistics operator in Brazil that provides warehousing, picking and packing, and delivery services for high-value-added products. The company currently has five distribution centres with a total storage and handling area of over 80,000 square metres.

This company has successfully connected its teamwork, productivity and business success to two specific ESG priorities, diversity and supporting local communities. The company's apprenticeship programme identifies young people from disadvantaged backgrounds and provides them with job training or professional opportunities. Senior leaders in the company support its inclusion programme by offering opportunities for people with disabilities such as hearing, sight and physical difficulties.

The company also developed corporate policies and partnerships for:

- hiring new staff
- improving working conditions
- delivering training sessions, and
- including mentoring initiatives as part of its programmes to retain staff and assess their performance.

In 2018, the programme's first year, the company hired more than 80 employees with disabilities, representing over 5% of the total workforce.

3. Property

Maintaining high ESG standards is an increasingly important factor in improving performance for our property portfolio. We share our priorities with our managing agents and development teams. They make sure the properties meet all legal requirements and take a responsible approach to employing staff on-site.

Our property team continues to take forward ESG standards and improve performance across our property portfolio.

In late 2018 we began to develop a reporting template to record and analyse information about ESG standards and performance across our property portfolio. We identified 70 ESG measurement criteria, including:

- selecting materials
- planning and designing public spaces, and
- making sure properties are energy-efficient and have the necessary building certification in place.

We will consider these criteria when making decisions across the portfolio. The information we collect will help us measure performance and identify further areas for improvement.

Positive improvements for a new distribution warehouse development in Banbury

The new template helped identify key areas for improvement at this development, including:

- making a contribution towards public art
- creating a new cycle path
- choosing materials responsibly, including efficient cooling refrigerants
- redirecting more than 70% of waste generated from the development away from landfill, and
- introducing a waste management plan for the site.

Procedures are in place to make sure that the properties are managed in a way which reduces their effect on the environment – for example, by removing any spillages that may harm the environment.

Contracts for employment on-site pay the national living wage, or more where possible. Contractors must demonstrate that they offer local businesses the opportunity to compete for work and give local people the opportunity to apply for jobs. They must also encourage involvement in local communities.

4. Member Enquiries

We received 35 enquiries on three campaigns at the annual meetings of Bayer AG, McDonalds Corp and Restaurant Brands International Inc (including 22 enquiries from non-members).

We did not hold Restaurant Brands International or McDonalds assets in the funds we manage for APS and NAPS.

There were 13 Scheme member enquiries on a counterproposal at the Bayer AG annual meeting to vote against agenda item 2. This item moved to approve discharge of the management board for the 2017 financial year. Formal discharge of the board is a routine vote of confidence in the company's management and policies. The shareholder counterproposal was mainly concerned with risks to stockholders arising from the company's production of neonicotinoids (neonics).

The European Commission banned the outdoor use of three neonics on flowering crops in 2013, and in 2018 voted in favour of a near total ban on the outdoor use of all neonics by the end of that year. This means that the pesticides can only be used now in closed greenhouses.

Bayer AG announced it would follow the European Commission's guidelines and respect the ban, as it has with flowering crops previously.

As there were no major governance or oversight concerns with the management board's activities, we voted in favour of item 2 to discharge the management board in line with ISS research recommendation. The vote passed with 97.2% approval.

Please visit the 'Scheme documents' page of the member website www.mybapension.com for more details on the Schemes' responsible investment activities. If you would like more information on ESG and can't find the information on the website, you can email us at esg@bapensions.com.

5. Affiliations, initiatives and future aims

Affiliations and initiatives

As investor signatories, we support the CDP as a way of improving the communication of non-financial factors. In 2017 we became members of the International Corporate Governance Network, which promotes effective standards of corporate governance and investor stewardship.

We are also members of the British Venture Capital Association, the Institutional Limited Partners Association, the Alternative Investment Management Association and Invest Europe. These organisations promote best practice in the private equity and alternatives industries and set standards for governance and transparency.

In January 2019 the Financial Reporting Council consulted on a new stewardship code. The ESG committee is committed to supporting this code when it is published. Although we are currently ranked as tier 1, the ESG committee is aware that we may not meet all the requirements to remain at this level. We will, however, work towards meeting best practice.

In March 2019 we joined the Investor Mining & Tailings Safety Initiative following the catastrophic tailings dam failure at the Córrego do Feijão mining facility in Brumadinho, Brazil. The failure of the dam led to the loss of more than 245 lives and 25 people missing (as of March 2019). The initiative is calling for new, independent, publicly accessible international standards for managing tailings dams. The initiative has also written to 683 extractive companies asking for more information about the way they manage tailings storage facilities.

Future aims

The joint responsible investment mission statement highlights the importance of ESG considerations as a financial risk which needs to be managed and considered over the long term. The Schemes' new responsible investment approach will be based on a framework of integration, stewardship, monitoring and reporting, and continuous improvement. Trustee directors recognise that best practice will not happen immediately. The Schemes will develop their responsible investment approach over time.

Under the new responsible investment policy we must build financially relevant ESG factors (including climate change) into our investment decision-making processes across all asset classes, at portfolio level and at asset level. In 2020, we will publish an annual report on the new responsible investment policy and the requirements of the updated statement of investment principles, alongside the responsible investment report for 1 April 2019 to 31 March 2020.

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