Sustainable and Responsible Investment

Equity

November 2021
BLI – BANQUE DE LUXEMBOURG INVESTMENTS S.A.

Contents

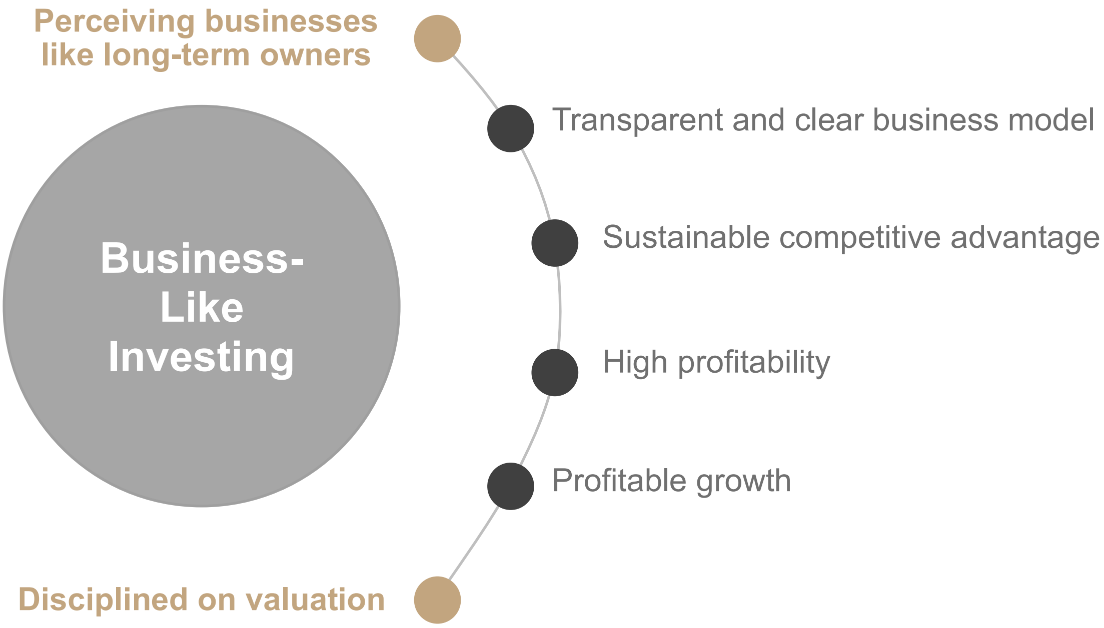
ESG Equity Investment Strategy

Scope

The methodology described below applies to all investments in equities made within the BL and SICAV BLB sub-funds.

Investment Principles

Our investment philosophy, known as **« Business-Like Investing »**, implies that managers do not simply trade securities but adopt an entrepreneurial mindset when investing in a company. **This long-term approach, which aims to understand the different aspects of a company before investing in order to measure the different risks associated with it, is highly complementary to an ESG approach.**



The key investment principles of Business-Like Investing are as follows:

- **Thinking & investing with a long-term horizon**

Equity markets reflect the fundamentals of the underlying companies only over the long term.

➔ Anticipating short-term market fluctuations is a futile exercise. The manager focuses on fundamentals and takes a long-term view (full market cycle).

- **A conviction-based approach**

The benchmark is only used to measure and compare the performance.

➔ In line with BLI's active investment style approach, the structure of the portfolio deviates significantly from the composition of the market index.

- **Keeping it simple**

The risks of an investment increase when its parameters are not properly understood. In order to reduce investment risks and increase returns, the manager focuses on his area of expertise.

➔ Through the application of a disciplined methodology based on an in-depth internal fundamental analysis, the manager seeks to better understand the company's fundamentals in order to reduce risk.

- **Valuation**

« The price paid determines the return »

➔ The manager calculates the intrinsic value of the potential investment candidate. Positions are only initiated if the stock price offers a discount to the company’s fair value (margin of safety). The objective is to reduce the risk of incurring significant losses while increasing the potential for capital appreciation (upside potential).

ESG

BLI's ESG equity investment policy relies on distinct yet interlinked pillars:

Pre Investment	Intra Investment	Post Investment
Exclusions	ESG Integration	Engagement & Voting
Controversies screening		Controversies follow-up

1. Exclusions

Our approach can be described as prudent, conservative and highly selective. By focusing on companies with strong competitive advantage and high yield characteristics that generate strong free cash flow, some sectors are either underrepresented or not included at all in our portfolios. These include, for example, financial institutions, commodities, airlines or other capital-intensive or complex industries.
Accordingly, it is unlikely that our strict investment principles will result in investments in very harmful or controversial companies and/or activities. Investments in sectors that are more often considered unethical have also been limited in the past.

Nevertheless, various exclusions have been adopted. Three types are distinguished here:

- → Exclusion due to controversies - companies that show severe controversies are excluded.
- → Exclusion due to violations of the United Nations Global Compact
- → Exclusion of certain industries - companies active in the coal and controversial weapons industries are excluded.

More information and details can be found in our exclusion policy here.

2. Controversies Analysis

Investment candidates and investments are monitored on an ongoing basis to identify substantial ESG events that could affect a company's business model, reputation and thus potentially BLI's investment case. Hence, BLI's SRI team receives daily alerts based on data from MSCI ESG Research for any kind of relevant controversy impacting investee companies.

The screening is in a first step based on the controversy flags attributed by MSCI (green, yellow, orange and red). Companies subject to a red flag are flagged for removal from BLI's investment universe within three months of the status change[1].

Companies subject to an orange flag (severe controversies), are screened to perform a more in-depth analysis using different data sources - own research, external service providers and media sources as well as information provided by the companies in CSR reports or their website. **Based on this in-house research performed by the SRI team, an opinion is formed in collaboration with the fund manager on the materiality of the controversy at hand for the company's long-term business model and BLI's investment case. Lastly, the analysis serves as a basis to identify engagement opportunities, meaning a situation favourable for advancement or success.**

New severe controversies are analysed as they emerge, otherwise the analysis is reviewed semi-annually to include new information in the assessment.
BLI fund managers receive regular status updates on the controversy assessment, which are used in the active ownership process as well as ensuring a holistic investment decision process incorporating extra-financial data is in place.

3. ESG Integration

The fundamental analysis is an important step in identifying and quantifying the strength of a company's competitive advantage and assessing its long-term potential. Elements such as profitability levels, balance sheet strength, capital intensity or past capital allocation are taken into account when assessing the strength of the company's fundamentals. Determining the potential for free cash flow generation as well as the in-depth analysis of the company's growth drivers are also important steps in the analysis.

In terms of valuation model, BLI uses a modified discounted cashflow model[2] to calculate the intrinsic value of a company. The calculation of this intrinsic value serves as a reference point for initiating positions without overpaying, as well as for weighting positions in the portfolio. In addition, it provides the manager with an indication of the value of the company based purely on its existing business and current profits (no-growth value), allowing him to better assess the growth priced into the share price. This is once again, an important element to assess the risk associated with the investment.

Integrating ESG in the valuation process, in the investment decision and thus in the final portfolio allocation is in line with BLI's bottom-up stock picking approach focused on selecting quality values by applying a long term, entrepreneurial view. **The additional extra-financial data allows the fund managers and the SRI team to get an even better picture of all risks as well as opportunities facing an investment candidate in order to make better informed decisions.**

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[1] The fund manager in charge has the possibility to present to the ESG Committee reasons for the company to remain eligible. The approval is carried out by a simple majority vote. The fund manager does not have a voting right.

[2] Bruce Greenwald et al. (2001). "Value Investing: From Graham to Buffett and beyond", Wiley Finance

In practice, we consider the ESG rating (AAA-CCC) provided by our provider, MSCI ESG Research. Defined bandwidths determine the ESG adjusted discount rates to be applied in the valuation model.

The rationale: A company with a solid ESG profile will be attributed a lower cost of equity, which in turn leads to a higher fair value whereas an ESG laggard will be penalized with a proportionately higher cost of equity and hence a lower intrinsic value.

The Rating Scale

MSCI Rating	Step	Adjustment to the CoE
AAA	-0,15%	-0,30%
AA	-0,15%	-0,15%
A	0,00%	
BBB	0,15%	0,15%
BB	0,15%	0,30%
B	0,15%	0,45%
CCC	0,15%	0,60%

CoE adjustment due to ESG Rating

We believe that the rating provided is a valid and appropriate indicator for the risks and opportunities a company is subject to in terms of ESG. Generally speaking, we agree that higher ESG ratings are associated with a business model where the downside risks are either managed more effectively or the company is less exposed.
In case of an ESG rating change the fund manager will adapt the valuation model accordingly.
The bandwidths are the result of a continuous dialogue between the fund managers and the SRI team. They are based on long standing experience and are subject to change as we gain further insight. The methodology is reviewed at least annually to ensure that it continues to meet our expectations. In the rare case a company is not rated by MSCI, the fund manager considers the average rating of his portfolio as anchor. As a result, a non-rated company gets downgraded accordingly if the average rating of the portfolio in question is BBB or lower. Otherwise, if the average rating of the portfolio is equal to or higher than A, the initial non-ESG adjusted cost of equity is used in the valuation.
Several sub-funds, namely the BL-Equities Europe, BL-Equities America and the BL-Sustainable Horizon apply further ESG criteria in line with the label ISR that can be found in the respective ESG policies.

4. Active Ownership

4.1. Voting

In order to manage the voting policy at Shareholders' Meetings (AGMs) as efficiently as possible, **BLI has decided to collaborate with a specialised external supplier, Institutional Shareholder Services Inc. (ISS).**

ISS provides BLI's teams with the information necessary to prepare the votes (dates of the meetings, agenda, etc.) as well as voting recommendations, supplemented by background information to help understand the proposed recommendations.

As part of its ESG investment and voting policies, **BLI subscribes to ISS' sustainability voting policy.** The sustainability policy aims to support shareholder resolutions based on standards that enhance long-term shareholder and stakeholder value while aligning the interests of the company with those of society as a whole. Fund managers will have the possibility to adjust the vote and deviate from the sustainable voting recommendation by ISS but need to be able to justify their decision.

This voting policy is consistent with the fund's objectives in the following areas:

- **Environment**: BLI votes in favour of resolutions calling for the reduction of greenhouse gas (GHG) emissions. More generally, BLI votes in favour of resolutions seeking information on the financial, physical or regulatory risks related to climate change that the company faces in its operations and investments or on the way it identifies, measures or manages these risks.
- **Social**: With regard to the respect of Human Rights, BLI generally votes in favour of the company's adherence to internationally recognised standards and principles, such as the United Nations Global Compact or the standards set by the International Labour Organisation (ILO). Votes in favour of proposals related to ILO principles aim to promote rights at work, encourage the creation of decent jobs, develop social protection or strengthen social dialogue in the field of labour.
- **Governance**: BLI votes in favour of resolutions promoting an adequate board composition. This is not limited to but includes questions of board independence, remuneration, balance between male and female representatives, competencies that are in line with the function. BLI deems this aspect important as it ensures in theory that the right level of controls and ownership of ESG issues are in place in order to prevent fraud, corruption and other serious violations.

4.2. Engagement

Engagement consists of a constructive dialogue between institutional investors and investee companies to discuss how they manage ESG risks and seize business opportunities associated with sustainability challenges.

Engagement may form part of our monitoring of companies or represent an escalation of concerns we have identified. As active managers we are well positioned to take actions on the back of our engagement efforts.

BLI, via its engagement efforts seeks to improve ESG related disclosure, change company's behaviour to align their practices with internationally recognized norms or commit to change. This is in light of mitigating risks by gaining a better understanding of a company's own view concerning its risk exposure and management, identify ESG opportunities by coming across pioneers and best practices as well as promoting positive impact in line with the 17 SDGs.
We use the opportunity to meet the management of companies as part of our active investment process and as a key element in our stewardship oversight of client assets. In the event that dialogue with the companies fails, or if the measure proves necessary and judicious for other reasons, BLI reserves the right to submit resolutions to the AGMs in the best interest of the investors and the desired impact.

The decision to undertake individual or collaborative engagement is in part determined by:

- The influence BLI can exercise on a company thanks to our ownership level and tenure, our proximity to decision makers and the investees geographical location
- The incident assessment as well as the urgency and severity of the issue at hand shown by the extent of stakeholders affected, media coverage of the incident and NGO involvement alongside the level of reputational and financial risk associated with the incident.

4.2.1. Individual Engagement

Individual engagement is either conducted by the fund manager himself and/or by the SRI team. Explaining our ESG standpoint and addressing issues to be discussed can be done by correspondence with a company's board, investor relations team or during company visits.
The controversies analysis performed in the investment process serves as a basis for engagement efforts where we challenge companies on their delivery of corporate strategy, financial and non-financial performance and risk, allocation of capital and management of environmental, social and governance issues.
We engage to understand the approach management is taking and test how far they are being good stewards. We also encourage companies held in client portfolios to establish and maintain high levels of transparency.
Overall, we raise ESG or other concerns with companies where we believe that to be in the interest of investors, identifying company specific or systemic risks.

4.2.2. Collaborative Engagement

Collaborative engagement is a way to cooperate and co-lead with other investors a dialogue with investee companies to bring about positive behavioural change, thereby enhancing credibility and giving greater weight to an initiative. The participation in these initiatives further enables the industry to realise economies of scale and the pooling of resources, expertise and power of several investors to address important global issues such as climate transition, the movement towards a circular economy and the abolition of forced labour and child labour in the supply chain.

As of 2021, BLI will be looking to actively engage with companies as a supporting investor in initiatives lead by the UN PRI or other investor-led initiatives.

Addendum

⁎ BL Sustainable Horizon

The BL-Sustainable Horizon Fund has a **dual objective**: a financial objective (stemming from our fiduciary responsibility as asset manager) and an impact objective. These two objectives are closely related and interdependent.

Aware of the undesirable effects of an excessively capitalist system that places too much emphasis on shareholder satisfaction to the detriment of the company's other stakeholders, the manager seeks, by taking ESG criteria into account in its stock selection process, **to identify companies that serve not only the interests of shareholders but also those of their employees, suppliers, customers, as well as those of the environment and the community at large. The aim is to contribute to the achievement of a better balance in economic, social and environmental matters.**

More specifically, the manager aims to particularly achieve concrete environmental, social and governance objectives, i.e. the limitation of global warming, the implementation of quality working conditions within companies, the respect of Human Rights (as defined by the United Nations), the existence of independent and equal Boards of Directors (BoD) (Men/Women).

In addition to BLI's formal exclusion policy, the manager excludes from his investment universe companies that generate **more than 5% of their revenues through the following activities: conventional weapons, tobacco, gambling, GMOs, alcohol, nuclear and fossil fuels**.

The pure ESG selection is then done through two complementary approaches :

- Quantitative screening based on MSCI ratings, whereby a company must present an average rating (each factor being equally weighted) greater than 5 and not have a score for an individual factor (E, S or G) less than 4.
- Thematic selection to **invest in companies which, through their activity, contribute directly or indirectly to the achievement of the UN's Sustainable Development Goals (SDGs).**

SUSTAINABLE DEVELOPMENT GOALS

The complete methodology and investment policy can be found here.

⁎ Precious Metals - Gold

In some of BLI's portfolios, investments in precious metals related stocks or gold-related stocks serve to protect the portfolio against risks linked to inflation, geopolitics or more generally loss of confidence in paper money.
While this makes sense from a financial point of view, the social and environmental impact and our efforts to mitigate the ESG-related risks must be addressed. Water usage, chemical waste, CO_2 emissions, labour practices and safety issues are regular topics when it comes to the mining sector. To tackle these issues, BLI has implemented a Best-in Class approach when it comes to investments in gold-related

stocks. This should ensure a level of ESG performance that implies an open and progressive mindset towards sustainability within the targeted companies and requires the respect of certain ESG norms.
In practice, two minimum standards must be respected in order to be eligible for investment:

1. Respect of the UN Global Compact: Companies must pass the UN Global Compact compliance check by MSCI. We will engage with companies figuring on the Watch List and the outcome must be published and satisfying. Companies failing the compliance check, are excluded from the investment universe.
2. Minimum rating of BBB: only companies with an MSCI rating of BBB and higher are eligible for investment.

The resulting impact of this approach is that (as of July 2020) approximately 50% of the gold-related stocks are not eligible for investment.

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