Sustainable and Responsible Investment at BLI

Overview

November 2021
BLI – BANQUE DE LUXEMBOURG INVESTMENTS

Sustainability at BLI[1]

Sustainable and responsible investing has gained momentum across the investment chain and it is a natural evolution for us as long-term investors to embrace it. It is an evolutionary process and the state of the world cannot radically be changed at once but taking incremental important measures as asset managers is a step in the right direction. Good intentions are not enough; they should be based on solid foundations, clear principles as well as explicit and achievable objectives.

According to the United Nations Principles for Responsible Investment (UN PRI), "responsible investing is an investment approach that seeks to integrate environmental, social and governance (ESG) factors into investment decisions in order to better manage risk and generate long-term sustainable returns."

Given the numerous definitions and approaches, ranging from sustainable and responsible investment (SRI) to social impact investing, green investment and ethical investment, it is important for BLI to define its own responsible investment approach. A certain degree of subjectivity is unavoidable when formulating an ESG policy, but having a strong anchor is important. Thus, our starting point was to build upon the definition by the UN PRI. It enables us to set the tone for a transparent and clear communication with investors.
When our first general ESG policy was published in 2017, ESG analysis was primarily a way to mitigate the risks of our portfolios. The focus was on identifying and avoiding the 'bad apples', mainly through the exclusion of the most controversial companies. This global approach was coupled with specific sustainable investments such as microfinance or via the BL Sustainable Horizon, BLI's flagship SRI equity fund.

Since then our approach has strengthened to become more proactive and applicable across asset classes. Thereby we now take a large number of ESG aspects into account from the pre- to the post investment stage. Extending our investment approach in 2019/20 constitutes a logical next step to our long-term oriented, conviction-based principles we have applied for years. The systematic and integral consideration of non-financial factors has been enabled through easier access to quality specialized research as well as our growing experience in SRI investing. The updated process allows us to gain the most comprehensive view of potential risks and opportunities affecting investment candidates in order to make better informed investment decisions.

The long term has been the corner stone of our investment philosophy since the beginning. In that respect, we focus on companies, bond issuers and third-party funds committed to the creation of sustainable long term returns, respecting not only the financial interests of shareholders (or creditors in the case of a bond investment) but also those of employees, suppliers, customers, communities and the environment. With time these entities should perform better thanks to less exposure to ESG risks and/or a better management of these risks. Extra-financial research helps us to implement our strongest conviction in order to generate sound value for our client.

[1] Where reference is made to investments, this document applies only to SICAV BL, SICAV BLB and SICAV BL FUND SELECTION.

As a signatory of the United Nations PRI, BLI is committed to honour the 6 principles and contributing to the improvement of the wider global financial sector by promoting best practices. More on our commitment can be found in the “Reporting and Promoting” part of this document. Lastly, we are committed to exercising our role as an active shareholder by voting at annual general meetings and communicating transparently on how we exercise our voting rights.

We consider the approach of investing sustainably to be a learning process and expect our strategy to evolve over time in order to reflect the progress made in the field as well as our thinking in terms of ESG.

Overview

The sustainable investment strategies of the BLI funds are multidimensional and adapted to the specificities of each fund. A general overview is given below:

	Fund	Exclusions	ESG Integration	Controversy monitoring	Engagement	Universe reduction	Impact or SDG focus	Micro-finance	Green Bonds
Equity	BL-American Smaller Companies	✓	✓	✓	✓				
	BL-Emerging Markets	✓	✓	✓	✓				
	BL-Equities America	✓	✓	✓	✓	✓			
	BL-Equities Asia	✓	✓	✓	✓				
	BL-Equities Dividend	✓	✓	✓	✓				
	BL-Equities Europe	✓	✓	✓	✓	✓			
	BL-Equities Japan	✓	✓	✓	✓				
	BL-European Family Businesses	✓	✓	✓	✓				
	BL-European Smaller Companies	✓	✓	✓	✓				
	BL-Global Equities	✓	✓	✓	✓				
	BL-Sustainable Horizon	✓	✓	✓	✓	✓	✓		
Mixed	BL-Global Flexible EUR	✓	✓	✓	✓				
	BL-Global Flexible USD	✓	✓	✓	✓				
	BL-Global 30 / 50 / 75	✓	✓	✓	✓				
Bonds	BL-Bond Dollar	✓							
	BL-Bond Euro	✓	✓				✓		✓
	BL-Bond Emerging Markets Sustainable	✓	✓				✓	✓	✓
	BL-Bond Emerging Markets Euro	✓	✓	✓					
	BL-Corporate Bonds Opportunities	✓	✓	✓					✓
	BL-Global Bond Opportunities	✓	✓	✓			✓	✓	✓
Multi gestion	BL-Fund Selection Smart Evolution	✓	✓				✓		

- The exclusions defined in BLI's exclusion policy are applied to all the above funds. As for BL-Fund Selection Smart Evolution, it considers the exclusions of the funds in which it invests.

- For equity and mixed funds, BLI integrates the company's ESG rating into the cost of equity in order to favor the most sustainable companies and penalize those that are lagging. ESG integration is always complemented by controversies monitoring, analysis of companies' ESG inappropriate behavior and inherent risks, and engagement, the act of contacting invested companies to influence their sustainability performance, as outlined in our engagement policy.

- Our ISR labelled equity funds also apply a 20% reduction in the investment universe, eliminating companies lagging on ESG issues.

- The impact or focus on the SDGs strategies target and measure (in the case of the bond funds) the impact of our investments on the financing of the SDGs. Impact is generated through various such as microfinance or green bonds.

All of the sustainable and responsible investing policies as well as BLI’s engagement and voting policy can be found here.

Reporting & Promoting

Adherence to the United Nations Principles for Responsible Investment

BLI became a signatory to the United Nations Principles for Responsible Investment (UN PRI) in July 2017. In line with our commitments to the UN PRI we seek to promote responsible investment practices focused on the longer term and centred around a variety of stakeholders both internally and externally. A heightened awareness and cooperation of different stakeholders is important if we as a society want to achieve targets set at international and national levels.

The 6 principles of the UN PRI are as follows:
1. Signatories will incorporate ESG issues into investment analysis and decision-making processes.
2. Signatories will be active owners and incorporate ESG issues into their ownership policies and practices.
3. Signatories will seek appropriate disclosure on ESG issues by the entities in which they invest.
4. Signatories will promote acceptance and implementation of the principles within the investment industry.
5. Signatories will work together to enhance their effectiveness in implementing the Principles.
6. Signatories will report on their activities and progress towards implementing the Principles.

Annual ESG Report

BLI publishes an annual ESG review to showcase the progress made thus far, measure the impact of our activities, share lessons learned and areas for growth going forward.

This report includes:
- Results of our proxy votes,
- Summary of our engagement activities,
- Snapshot of our controversy analysis,
- Carbon footprint performance alongside other relevant ESG measures,
- A summary of the investment thesis of the fixed income and multi-management funds.

Primary External ESG Research

The quantitative ESG rating used in the investment process is based on ESG ratings issued by MSCI. MSCI calculates an exposure score indicating a company's level of exposure to each specific issue based on its industry combined with its geographic location.
MSCI then analyses the company's ability to manage its exposure to the various risks identified. The analysis of controversies is also a key component of the ESG assessment process conducted by MSCI. To obtain a final rating (AAA to CCC), the weighted averages of the scores for the main issues are aggregated and the company scores are normalised by sector. Companies with a good performance receive a preliminary score of 10, while those with a poor performance receive a 0. Any company not included in the official benchmark that scores higher or lower than the sector will receive a score of 10 or 0 respectively.

Once all exceptions are taken into account, the final adjusted sector score for each company is a ranking between best (AAA) and worst (CCC).
These assessments of a company's performance are not absolute but are explicitly intended to be relative to the standards and performance of companies in the same sector.

The table below summarizes the 37 key factors analysed [2] :

3 pillars	10 themes	37 key factors	
Environment	Climate change	Carbon Emissions	Financing Environmental Impact
		Product Carbon Footprint	Climate Change Vulnerability
	Natural resources	Water stress	Raw Material Sourcing
		Biodiversity and land use	
	Pollution & Waste	Toxic emissions and Waste	Electronic Waste
		Packaging Material and Waste	
	Environmental opportunities	Opportunities in Clean Tech	Opportunities in Renewable Energy
		Opportunities in Green Building	
Social	Human Capital	Labour Management	Human Capital Development
		Health and Safety	Supply Chain Labour Standards
	Product Liability	Product Safety and Quality	Privacy and Data Security
		Chemical Safety	Responsible Investment
		Financial Product Safety	Health and Demographic Risk
	Stakeholder Opposition	Controversial Sourcing	
	Social Opportunities	Access to Communications	Access to Health Care
		Access to Finance	Opportunities in Nutrition and Health

[2] Source : MSCI ESG Research Ratings Methodology, January 2019, p.8.

Governance	Corporate Governance	Board	Ownership
		Pay	Accounting
	Corporate Behaviour	Business Ethics	Corruption and Instability
		Anti-Competitive Practices	Financial System Instability
		Tax Transparency	

Other external sources used in the analysis:

- Bloomberg ESG data,
- Company data and reports,
- Research broker.

Governance and Organisation

Definition and Implementation of the ESG Policy

The strategic direction and decision-making power lies with the board. On the other hand, BLI's ESG council, the "Comité Investissement Socialement Responsable (CISR)", acts as the governing body for the implementation of the strategic ESG projects.
Once the strategic goals are defined, the SRI team develops the practical implementation in continuous dialogue with every impacted team at BLI. The adopted measures affecting the fund management are being integrated into the portfolios by the fund managers and analysts, with the continuous assistance of the SRI team.

Monitoring of the RI Policy

An automatic alert system has been put in place so that the manager(s) and the SRI strategist(s) are notified immediately in the event that the ESG data of a company included in the portfolio is modified by the extra-financial research provider MSCI.

In addition a formal procedure for monitoring ESG investment policy risk and compliance has been defined for article 8 and 9 funds. This procedure is designed to ensure compliance with the various aspects of the ESG policy, i.e. the exclusion criteria and compliance with the ESG thresholds established in the valuation process. Every month, the Head of Risk Management produces a report regarding the compliance with the guidelines on these various criteria. Once a year, a separate report summarizing the analyses performed during the period is prepared.

Comité ISR

BLI has its own Sustainability Committee, the "Comité Investissement Socialement Responsable (CISR)". This committee acts as a discussion forum and governance body on ESG-related issues. As such, it assists and advises staff in the application and day-to-day management of the responsibilities arising from the various ESG policies.

The council acts as a discussion forum and governing body for ESG issues within BLI. It is responsible for regular reviews of industry developments and for the sound implementation and cautious revision of the ensuing timeline and policy. The permanent committee members are representatives from all relevant BLI teams. The CISR aims to promote an ESG culture throughout the BLI workforce by communicating transparently about the discussions that take place at CISR sessions, and every BLI employee who wishes to do so has the opportunity to attend the meetings. However, only permanent members of the CISR have a right to vote.
Decisions on responsible investment are integrated into our portfolios by the managers with the assistance of the CISR and the SRI team. All decisions are taken in collaboration with the relevant BLI teams.

SRI Team

BLI has a team dedicated to ESG research that works with all fund managers, all universes combined. Initially, when the PRI were signed, the ESG policy was defined within the Product Management team, where one person was particularly dedicated to this aspect. It was decided in 2019 to create the position of SRI strategist and to attach him to the management team. In March 2020, the team expanded to include a second person.

The SRI team is furthermore supported by BLI's *Comité ISR* and uses extra-financial data from MSCI providers, Bloomberg ESG, broker research and data published by the companies themselves.
The SRI analysis is carried out by the SRI team in collaboration with the fund managers and analysts. The fact that the SRI team is integrated into the management team encourages discussion and consideration of ESG issues in the investment process.

Corporate Social Responsibility (CSR)

BLI's developments are in line with and inspired by its parent bank's CSR policy which focuses on four major areas: the sustainability of the bank through good governance and ethical conduct, human and sustainable relations with employees, support for the ecological, social and societal transition and the reduction of our environmental footprint.
More on Banque de Luxembourg's CSR policy can be found in its non-financial report here.

Exclusion policy

BLI introduced its first formal exclusion policy in June 2021. While some areas (business involvement and behavioural) were already excluded through different investment policies focused on clear competitive advantages and financial stability, the newly released document had the ambition to serve as minimum threshold. In it, BLI identifies several types of exclusions:

- Controversy-based exclusions are intended to protect the reputation of investors and to avoid them becoming embroiled in controversies when scandals arise.
- Exclusions due to non-compliance with the United Nations Global Compact
- Sector exclusions: Controversial weapons and companies involved in the coal value chain.

In case the SRI team and/or the Head of Risk Management discover that a company held in a portfolio is no longer in compliance with our exclusion policy, he notifies the relevant investment manager(s). They can either choose to exclude the security in question or defend the case before the SRI Committee based entirely on ESG arguments.

Following the case defense, the SRI Committee votes on the security's retention. For the decision to be taken, two-thirds of the SRI Committee must be present. A qualified majority of two-thirds of the participants is required for the vote to pass.

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