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Glossary of Responsible Investment Terms

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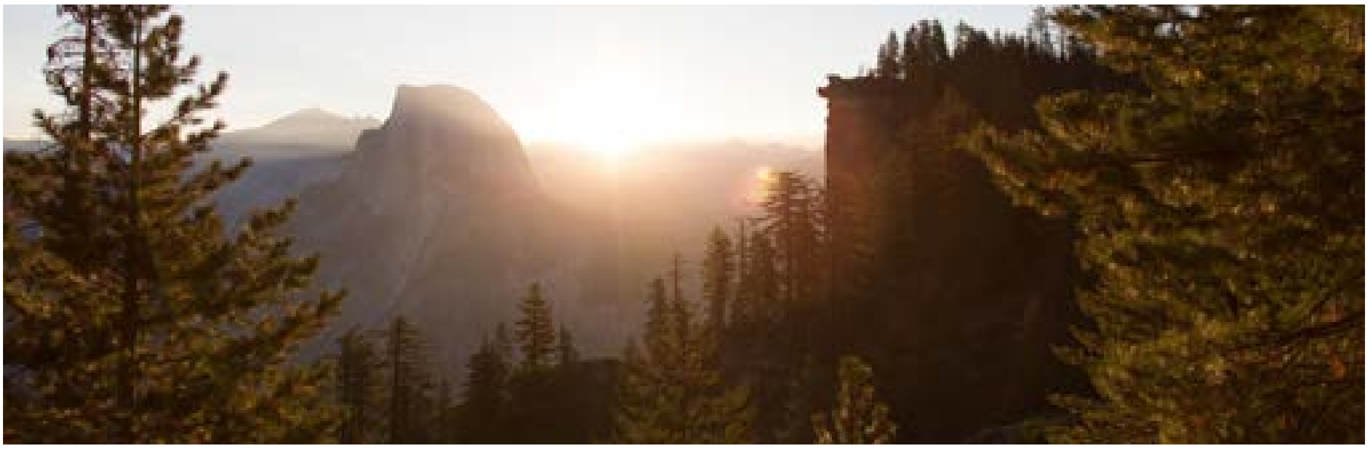


Activist Investing

An approach to equity investing that aims to bring about changes in corporate behavior with a view to enhancing shareholder returns.

There are many different flavors of activism or engagement – from antagonistic, public debates that play to the media, to more benign, behind-the-scenes negotiations.

Activist investors are more outspoken in their approach than active investors, typically buying a large shareholding in a company and aggressively advocating change, generally by sponsoring campaigns to change board composition, influence M&A, and other restructuring. Ethical, Social and Governance (ESG) issues are becoming more common in activist campaigns.

Active Ownership

Engagement with companies by asset owners with the intention of influencing their policies and practices, including on ESG issues.

One way for traditional active equity managers to get involved is through a two-way discourse, which brings outside perspectives that help companies to improve. At its core, positive active behavior is about enhancing shareholder value and helping companies to achieve their potential.

Voting at shareholder meetings is another means of having your voice heard and bringing about positive change.

Best In Class

A term used to describe a company that is a leader in its sector. Within the context of responsible investing, it refers to companies that excel in meeting ESG criteria relative to their peers.

Adopting a best-in-class investment strategy typically means investing in companies that are highly rated in terms of their ESG credentials.

Carbon Footprint

A portfolio's carbon footprint is the sum of a proportional amount of each portfolio company's emissions (proportional to the amount of stock held in the portfolio).*

A carbon footprint is a useful quantitative tool that can inform the creation and implementation of a broader climate change strategy.

Assessing a carbon footprint can be used for a variety of purposes, for example, to identify which activities contribute the most to a footprint, and for setting a target for reducing emissions.

The Greenhouse Gas (GHG) Protocol Corporate Standard classifies a company's GHG emissions into three "scopes". Scope 1 emissions are direct emissions from owned or controlled sources. Scope 2 emissions are indirect emissions from the generation of purchased energy. Scope 3 emissions are all indirect emissions (not included in scope 2) that occur in the value chain of the reporting company, including both upstream and downstream emissions.

*Source: PRI Principles for Responsible Investment

Carbon Neutral

By reducing a carbon footprint to zero, an individual, organization, event or product would become carbon neutral.

A carbon neutral footprint means the sum of the GHG (CO_2e) produced is offset by natural carbon sinks and/or carbon credits. Carbon Trust Certification certifies organizations and products to PAS 2060 – the internationally recognised certification standard for the demonstration of carbon neutrality.

Carbon Trust Certification

The Carbon Trust is an independent, global certification body for carbon footprints and certifies organizations and products to PAS 2060.

PAS 2060 requires robust measurement and a plan for achieving reductions and offsetting using high quality carbon credits. The Carbon Trust recognises only Gold Standard carbon credits.

Carbon Neutral footprint certification enables companies to gain an internationally recognized, fully independent measurement that can be used to communicate a product's resource efficiency, to drive sales, reduce costs and increase brand loyalty.

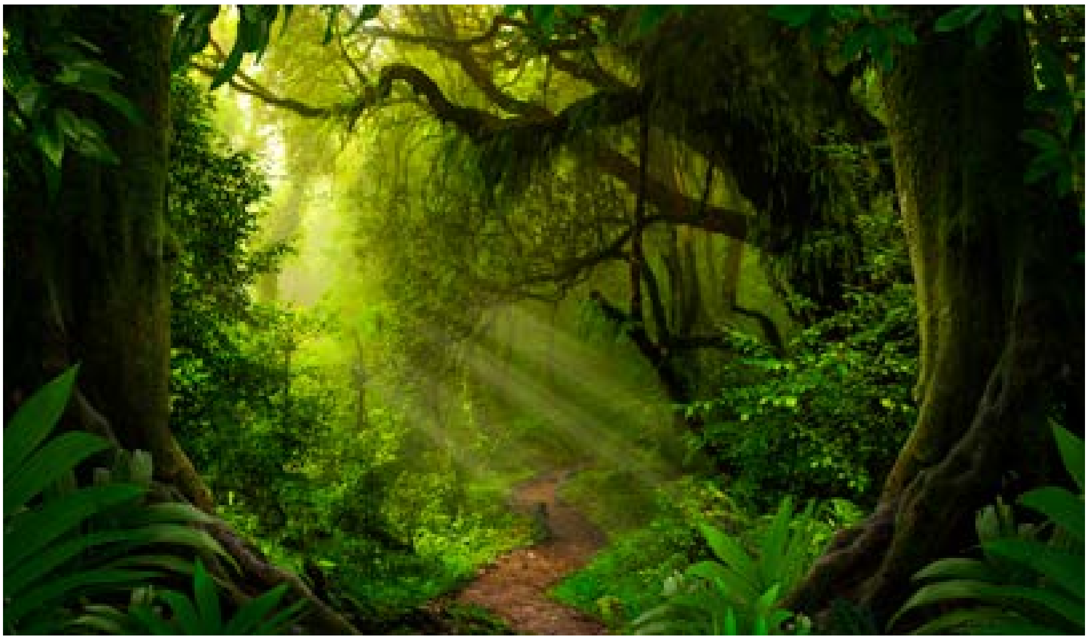
Carbon Sinks

Natural environments with the ability to absorb more carbon dioxide from the atmosphere than they release.

The principal carbon sinks, which help to lower the greenhouse gas levels in the atmosphere, are oceans, plants, forests, grasslands and soil. Oceans are a major storage system for carbon dioxide (CO_2), and by absorbing CO_2 from the atmosphere to use in photosynthesis, plants and trees are able to transfer some carbon to soil as they die and decompose.

According to a study published in The Nature Research Journal, 93% of carbon dioxide is stored in algae, vegetation and coral under the sea, but oceans are not able to absorb all of the carbon dioxide released from the burning of fossil fuels. The study suggests that the oceans have absorbed a smaller proportion of fossil-fuel emissions, nearly 10% less, since 2000.

Source: Worldwatch Institute: http://www.worldwatch.org/node/6323
Nature Research Journal Research abstract "Reconstruction of the history of anthropogenic CO2 concentrations in the ocean"
https://www.nature.com/articles/nature08526#



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Clean Energy

Energy sources that are not derived from fossil fuels (such as coal, oil and natural gas). These include biomass, geothermal, hydroelectric, solar, and wind.

These are also described as 'renewable' sources of energy. Unlike fossil fuels, a renewable resource can be used repeatedly and replaced naturally.

Nuclear energy is sometimes described as a clean energy source because it generates zero emissions and uses much less land than solar power systems and wind farms. However, a by-product of nuclear energy from uranium-fuelled nuclear cycles is highly toxic radioactive fission waste, which is dense in comparison to other forms of waste and can be recycled, but is potentially very harmful to health and the environment.

The growth in demand for clean and renewable energy is expected to continue as the world recognizes that fossil fuels will eventually run out and moves towards a zero-carbon economy. New technologies are leading to new and efficient means of producing and storing clean energy to meet rising demand. Ongoing innovation should continue to push down costs and make traditional fuel sources increasingly uncompetitive. Companies are also increasingly realizing that a better environment provides healthier societies and bottom lines.

Climate Risk

The risk relating to the impact on natural and human systems from the negative effects of climate change.

Curbing rising temperature levels is a primary focus in addressing climate risk. Concerns are mounting that a failure to prevent global temperatures from rising more than two degrees Celsius above pre-industrial levels this century could have catastrophic consequences.

In December 2015 in Paris, parties to the United Nations Framework Convention on Climate Change (UNFCCC) reached an agreement to combat climate change and accelerate actions and investments needed to transition to a sustainable low carbon future. The Paris Agreement's main goal is to keep global temperature well below two degrees Celsius above pre-industrial levels, while pursuing efforts to limit the temperature increase even further to 1.5 degrees Celsius.*

The United Nations Intergovernmental Panel on Climate Change (IPCC) was established by the World Meteorological Organization (WMO) and United Nations Environment Programme to provide an objective source of scientific information. The IPCC provided more clarity about the role of human activities in climate change when it released its Fifth Assessment Report. According to the UN, the report "is categorical in its conclusion: climate change is real and human activities are the main cause." The IPCC Sixth Assessment Report is planned for publication in 2022.

Unless investors pay close attention to how companies are preparing for the direct and indirect effects of climate change, the long-term impact on operations could be significant and could present risks, and opportunities, in investment portfolios.

*Source: UNFCCC: https://unfccc.int/process-and-meetings/the-paris-agreement/the-paris-agreement

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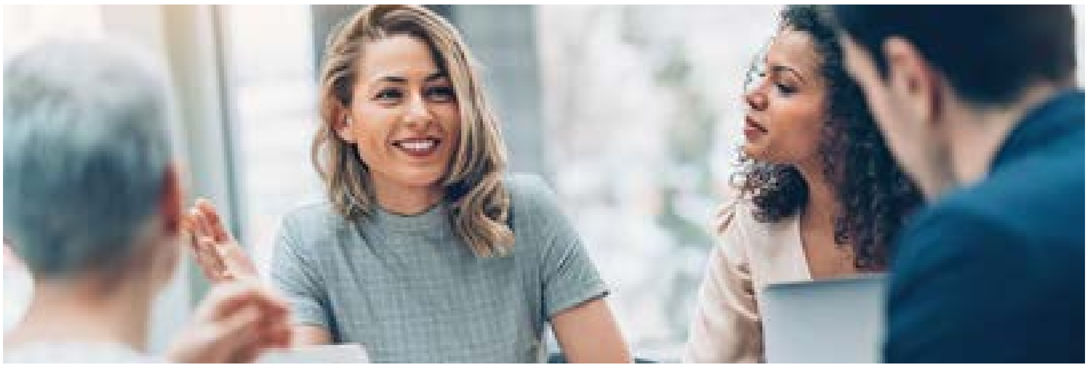
Corporate Governance

The procedures, processes and practices by which a *company* is controlled and directed.

The governance framework should make clear who is in authority as well as how decisions are made and acted upon. Most companies are governed by a board of directors, which sets the company's strategic aims and is responsible for overseeing a management team tasked with implementing the strategy.

An effective governance structure takes into account the interests of all stakeholders, for example, customers, employees, suppliers, shareholders, investors, regulators, auditors and the wider community affected by the company's activities.

Corporate and system failures such as the Enron Corporation scandal in 2001, and the global financial crisis in 2008, combined with an increasingly complex regulatory environment, have sharpened the focus on good governance in recent years. Good corporate governance, alongside adherence to environmental and social criteria, can be a significant factor in contributing to the long-term value of a company.



Engagement

Interaction between two parties, such as a company and its shareholders.

According to research by the Principles for Responsible Investment (PRI), there is "growing evidence that engagement by investors with companies on ESG can create shareholder value."

The research highlights three ESG engagement dynamics that create distinct types of value for companies and investors: (1) communicative dynamics—engagement enables the exchange of information between corporations and investors, creating 'communicative value'; (2) learning dynamics – engagement helps to produce and diffuse new ESG knowledge amongst companies and investors, creating 'learning value'; and (3) political dynamics – engagement facilitates diverse internal and external relationships for companies and investors, creating 'political value'.

Engagement can be an integral part of an active investment manager's approach. It provides them with the opportunity to share their investment philosophy and corporate governance values, and, importantly, to affect positive change with issuers. In addition, it augments their research and provides insight into company strategy, competitive positioning and efforts to manage risks and opportunities, including those related to ESG issues.

ESG Integration

An approach that explicitly considers ESG factors in research and integrates their economic impact into the fundamental investment analysis, which informs the final investment decision.

For example, when looking at companies with exposure to fossil fuels, analysts would incorporate how stranded assets—potentially unusable assets from oil, coal and gas projects—might impact their forecasts, as well as the regulatory landscape. This could lead to underweight positions in companies with material coal exposure and an undefined plan to transition to a low-carbon economy, or an overweight in companies with a clear transition strategy in place.

Investors who identify a company facing an ESG issue can engage with the company to review the concern. Such engagement may also result in identifying investment opportunities.

ESG Ratings

Scores given to companies to identify how they manage and are exposed to material ESG factors.

Ratings providers, such as MSCI, research and rate companies relative to their peers. MSCI researches and rates companies on an "AAA" to "CCC" scale according to their exposure to industry-specific material ESG risks and their ability to manage those risks relative to peers.

Sustainalytics' ESG ratings are designed to help investors identify and understand financially material ESG risks at the security and portfolio level. They are categorized across five risk levels: negligible, low, medium, high and severe. The ratings scale is from 0-100, with 100 being the most severe.

Ethical Investing

An investment approach that is guided by the investor's moral principles and values, including religious beliefs.

Ethical investing is generally associated with negative screening, that is, the exclusion of companies or sectors from an investment portfolio, if such companies/sectors are not deemed to be compatible with the investor's ethical beliefs, such as companies which manufacture tobacco or weapons.

It is important to distinguish between ethical investing as a values-driven approach to investing done through a screening approach, and ESG integration which is guided by consideration of ESG factors, how a company is managing those factors, and how they are priced into the investment.

Managers who are committed to a responsible investment strategy typically focus less on exclusion and more on the long-term stewardship of companies in the belief that positive engagement will lead to improvements in both sustainability and investment performance.

Exclusion

The practice of excluding certain companies or sectors from an investment portfolio, which investors may choose to do for a variety of reasons, such as ethical concerns, or to meet specific investment criteria. This is a negative screening approach.

Exclusions are often based on broad beliefs about industries, countries and risks and can potentially positively or negatively impact the return streams of portfolios; investors should carefully consider such impacts.

Fiduciary Duty

A legal obligation of one party to act in the best interest of another. The obligated party – the fiduciary – is typically entrusted with the care of money or property.

Within an investment context, fiduciary relationships include asset managers and their clients, boards of directors and their shareholders, and trustees and their beneficiaries.

Green Bonds

Bonds whose proceeds are used to fund new or existing environmental or climate projects.

Green bonds cover a wide range of finance options: energy, transport, waste management, building construction, water and land use. Some definitions also include communications and information technology.

According to Bloomberg New Energy Finance (BNEF), US$580 billion of green bonds were sold in 2018 with a further US$170 billion to US$180 billion expected to be sold in 2019. The market is expected to keep growing, with Europe alone needing about 180 billion euros (US$203 billion) of additional investment a year to achieve 2030 carbon emission reduction targets set by the European Union in the 2015 Paris Agreement on climate change.

Issuers from more than 50 countries have sold green bonds, including supranational institutions such as the World Bank and the European Investment Bank, governments, corporates and municipalities. The first emerging-market green bond was issued in South Africa in 2012. Poland opened the sovereign market in 2016, followed by France, Belgium and Ireland. The US is the largest source overall, led by The Federal National Mortgage Association (FNMA), and local governments selling notes to finance infrastructure such as sewerage upgrades.

Greenwashing

Organizations accused of 'greenwashing' are those which present themselves or their products as more environmentally friendly than they truly are.

From an investment perspective, it's important to understand how a strategy is invested to ensure it aligns with how it is marketed. The growing interest in, and demand for, more responsible investments has seen a number of product launches labelled so as to capitalize on this trend. Green bonds, for example, are typically self-labelled. Buyers and investors should scrutinize the extent to which an investment is genuinely 'green' and interrogate an asset manager's investment process in this regard.

Impact Investing

Intentionally targets a specific social and/or environmental goal and measures the financial return and social or environmental impact.

Impact investment strategies may be private or public, for example, funding for specific projects, such as schools or hospitals, or aligned with a specific theme, such as clean water, or the UN Sustainable Development Goals (UN SDGs). The advantages of impact investing include the fact that funds can be allocated directly to projects.

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Materiality

In responsible investing, materiality helps identify the key ESG information to integrate into an investment.

A long-established concept in financial accounting procedures, materiality is defined by the International Accounting Standards Board: “Information is material if omitting, misstating or obscuring it could reasonably be expected to influence the decisions that the primary users of general purpose financial statements make on the basis of those financial statements, which provide financial information about a specific reporting entity.”

Financially material ESG factors, such as corporate governance, social and environmental policies, supply chain management, and health and safety policies, can have a significant impact on a company’s potential growth and performance. In its latest Sustainability Reporting standards, the Global Reporting Initiative (GRI), “which aims to help businesses and governments worldwide understand and communicate their impact on critical sustainability issues such as climate change, human rights, governance and social well-being,” has sought to clarify its definition of materiality. It says that relevant topics are those that can reasonably be considered important in reflecting an organization’s economic, environmental and social impacts, or influencing the decisions of stakeholders. In this context, “impact” refers to the effect an organization has on the economy, the environment and society.

For some investors, ESG materiality may be paramount, even if financially immaterial; such investors may seek to engage with companies to drive better social value rather than financial value.

Source: Source: International Accounting Standards Board
Access Definition of Material (Amendments to IAS 1 and IAS 8) on eIFRS (subscription required)

Negative Screening

An approach that narrows the investment universe for a variety of reasons, such as ethical concerns, or to meet specific investment criteria.

Negative screening typically excludes investment in companies in certain industries, such as alcohol and tobacco companies, weapons manufacturers and producers of fossil fuels. It is often based on broad beliefs about industries, countries and risks and can potentially impact the return streams of portfolios; investors should carefully consider such impacts.

See Exclusion >

Positive Screening

The opposite approach to negative screening, which applies a specific threshold of ESG criteria to identify investment candidates, often using a best-in-class approach relative to peers.

For example, ESG research providers publish ratings and indices to help investors distinguish between companies that score better or worse on ESG criteria, including those in industries that are often considered problematic, such as energy.

Proxy Voting

Allows a legally authorized agent to vote on someone else's behalf.

For example, shareholders who do not wish to attend a company's annual general meeting (AGM) may vote by proxy by allowing someone else to cast votes on their behalf, or they can vote electronically or by post.

Before an annual shareholder meeting, shareholders receive information containing a Proxy Statement. The proxy documents include information about the company's performance, such as insight into its governance and management operations, items on the agenda, and details the qualifications of management and board members. This serves as a ballot for a variety of issues including officers' remuneration, the election of the board of directors and ratifying the appointment of auditors. Proxy statements must be filed with regulatory authorities, such as the Securities and Exchange Commission (SEC) in the United States, on an annual basis before the company's annual meeting.

Responsible Investment (RI)

Responsible investing is a framework that encompasses many different ways to consider ESG issues.

It is not a one-size-fits-all proposition. Many terms are used to describe RI approaches, which can be very confusing for investors.

According to the Principles for Responsible Investment (PRI) "Responsible investment is an approach to managing assets that sees investors include environmental, social and governance (ESG) factors in:

- their decisions about what to invest in;

- the role they play as owners and creditors.

It aims to combine better risk management with improved portfolio returns, and to reflect investor and beneficiary values in an investment strategy. It complements traditional financial analysis and portfolio construction techniques."

Responsible investing is often used as an umbrella term. Among the approaches that fall into this category are ethical investing, impact investing, mission-based investing, socially responsible investing, sustainable investing, thematic investing and values-based investing.

Sources: Principles for Responsible Investment https://www.unpri.org/

Sin Stocks

Shares in companies engaged in activities that are considered to be morally or ethically unacceptable.

Ethical investors typically exclude sin stocks from companies in certain industries, such as gambling, pornography, alcohol, tobacco and weapons manufacturers.

Social Impact Bonds

Bonds designed to improve the social outcomes of publicly funded services.

Providers are typically NGOs or charities that wish to fund the working capital needs of a project. Payments are usually subject to specific social outcomes being achieved.

The UK is a pioneer in the development of Social Impact Bonds (SIB) and continues to be a leading proponent. The first SIB was implemented in Peterborough prison in 2010 to reduce reoffending rates. As at July 2018, 45 SIBs have been launched in the UK with over 100 worldwide, covering a diverse range of initiatives, including integrating refugees in Finland, supporting homeless people in Canada, and getting young children ready for kindergarten in Chicago.

Socially Responsible Investment (SRI)

An investment strategy that aims to take into consideration a positive social outcome alongside a financial return.

Investors can do this in several ways; some choose to exclude investment in companies that produce products which they consider to be harmful (such as alcohol, tobacco and weapons); others seek out companies engaged in positive activities, (such as renewable energy, community housing and social justice).

SRI strategies can employ thematic asset allocation in order to align a portfolio's target securities with specific themes, such as clean water, or the UN Sustainable Development Goals (UN SDGs). ESG integration in research allows for more comprehensive financial forecasting and risk analysis at the security level; and active engagement helps promote positive change at companies, which can also be a driver of stronger investment returns.

Stewardship

According to the International Corporate Governance Network (ICGN), stewardship can be defined in general terms as the responsible management of something entrusted to one's care.

This suggests a fiduciary duty of care on the part of those agents entrusted with management responsibility to act on behalf of the end beneficiaries. In an investment context, institutional investors are the agents acting on behalf of beneficiaries, who are often long-term savers or members of pension funds.

A positive approach to stewardship encourages engagement between shareholders and company management and/or directors on a range of issues including company strategy, capital allocation, executive compensation and other ESG matters to help ensure that the company's strategy and management are aligned with shareholders' interests.

Active investment managers may proactively implement their stewardship duties throughout an investment process, have robust corporate governance and ESG integration practices in place, use an integrated approach to evaluating and monitoring investments, and are active owners and shareholder advocates.

Source: ICGN (International Corporate Governance Network) https://www.icgn.org/

Stranded Assets

Investments that can no longer generate a viable return in the foreseeable future and have become worthless.

This term is generally used to refer to assets that belong to utility companies and companies involved in the extraction of fossil fuels, such as oil, gas and coal. A variety of factors can lead to assets becoming stranded, including regulations that limit the use of fossil fuels, a change in demand, such as the shift towards renewable energy, or legal action.

The Paris Agreement initiated by the United Nations Framework Convention on Climate Change, which deals with greenhouse gas emissions mitigation, adaptation and finance (signed in 2016), signaled an increase in ambition for targets, which could leave more assets stranded in future.

According to a study in Nature, International Journal of Science, an estimated one-third of oil reserves, half of gas reserves and 82% of known coal reserves should remain unused in order to meet global temperature targets under the Paris Agreement.

Climate change risk management, including carbon asset risk, is becoming a significant governance issue for corporations, governments and municipalities.

Source: *Nature*,International Journal of Science https://www.nature.com/articles/nature14016

Sustainability

The characteristics that enable a defined entity, such as a company, industry or market, to continue indefinitely.

In 1987, the United Nations Brundtland Commission defined sustainability as "meeting the needs of the present without compromising the ability of future generations to meet their own needs." Sustainability is often used with reference to ecological concerns but applies to a wide range of ESG issues.

See Sustainable Investing >

Sustainable Investing

Often used interchangeably with responsible investing, a sustainable investment strategy takes a long-term view aiming to generate returns from investments which simultaneously contribute to a positive environmental or societal outcome.

This involves taking account of ESG factors and their impact. Environmental stewardship and social equity are increasingly viewed as important for a country's long-term economic health. For example, China's new five-year plan formalized a shift away from the level of economic growth to the quality of economic growth. This means that China is now focused on preventing major financial risks, alleviating poverty and reducing pollution. For China –and many other countries – sustainability is a prerequisite for continued long-term growth.

Thematic Investment

A top-down investment approach that focuses on investments in one or more specific social or environmental categories.

Examples of themes include resource scarcity, renewable energy, women and empowerment. Thematic portfolios often seek to identify and exploit themes that have the potential to drive profits across industries such as climate change, health and empowerment.

Thematic investing can also provide an attractive diversification element to an overall portfolio, potentially enhancing returns while reducing portfolio risk.

Organizational Bodies

- Cambridge Institute for Sustainability Leadership
- Carbon Disclosure Project (CDP)
- Carbon Trust
- European Sustainable Investment Forum (EuroSIF)
- Global Reporting Initiative (GRI)
- Global Sustainable Investment Alliance (GSIA)
- Gold Standard
- International Corporate Governance Network (ICGN)
- Organization for Economic Co-operation and Development (OECD)
- Principles for Responsible Investment (UNPRI)
- Sustainalytics
- Task Force on Climate-related Financial Disclosures (TCFC)
- United Nations Global Compact
- UK Sustainable Investment and Finance Association (UKSIF)
- UN Sustainable Development Goals (SDGs)
- MSCI
- World Meteorological Organization (WMO)

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