

Responsible Investing

EFG's ESG Integration Approach

2021



DISCIPLINED BY NATURE. FLEXIBLE BY DESIGN.

The icons alongside represent our investment process. Through a disciplined provision of investment policy and security selection at the global level, regional portfolio management teams have the flexibility to construct portfolios to meet the specific requirements of our clients.

HIGHLIGHTED IN THIS PUBLICATION:

 GLOBAL STRATEGIC ASSET ALLOCATION

 GLOBAL SECURITY SELECTION

 REGIONAL ASSET ALLOCATION

 REGIONAL PORTFOLIO CONSTRUCTION

EFG'S ESG INTEGRATION APPROACH

The ESG considerations contained in this document can change without notice.

Our investment approach is rooted in proprietary fundamental analysis. Environmental, social and governance (ESG) factors are integrated in the evaluation of investments, using our GRIP system.

We believe the integration of ESG factors can improve our understanding of the companies in which we invest. More broadly, paying regard to ESG issues can bring positive change for society and the environment. We recognise, however, that ESG ratings are not perfect and have room to improve. Among the challenges we observe, there is the potential for different methodologies to produce conflicting results. The process of arriving at ESG ratings may also be difficult to comprehend. Therefore, to best meet the needs of our clients, fulfil our due diligence requirements and remain responsible for our judgements, we have built an internal approach to ESG analysis: GRIP our Global Responsible Investing Platform.

We believe ESG integration is most effective when it is fully embedded in the investment process, rather than applying a simple overlay of external ratings. While GRIP is owned and controlled by the ESG team, only a continuous dialogue with financial analysts and portfolio managers and the companies in which we invest can help us to correctly identify ESG issues. Working together we can better identify, analyse and integrate the ESG factors most likely to have a material impact on the long-term performance of an investment.

In the next few pages we will describe the framework we set up for EFG. While we believe it is an advanced integration approach it will continue to evolve. ESG integration is a long term journey.

GRIP

The development of GRIP started more than 10 years ago and the first scores were produced back in 2012. Since then the GRIP has been continuously evolving and improving. The materiality assessment for different industries has been revised several times, especially to take into account new challenges and changes in the regulatory landscape. The organization of the data has become more aligned with the GRI (Global Reporting Initiative) and additional data from new sources have been added across the years.

For every company GRIP defines the relevant key performance indicators (KPIs) that need to be assessed. These reflect the risks to which a company is exposed and are at the centre of our analysis (see Figure 1). These KPIs are evaluated with multiple data, divided into three main groups:

- **Policies:**
Does the company have policies and rules to deal with key issues?
- **Outcomes:**
What are the data we can measure to assess how well a company is managing the risks it is exposed to?
- **Controversies/litigation:**
Are companies “walking the talk” and behaving in the interests of all their stakeholders?

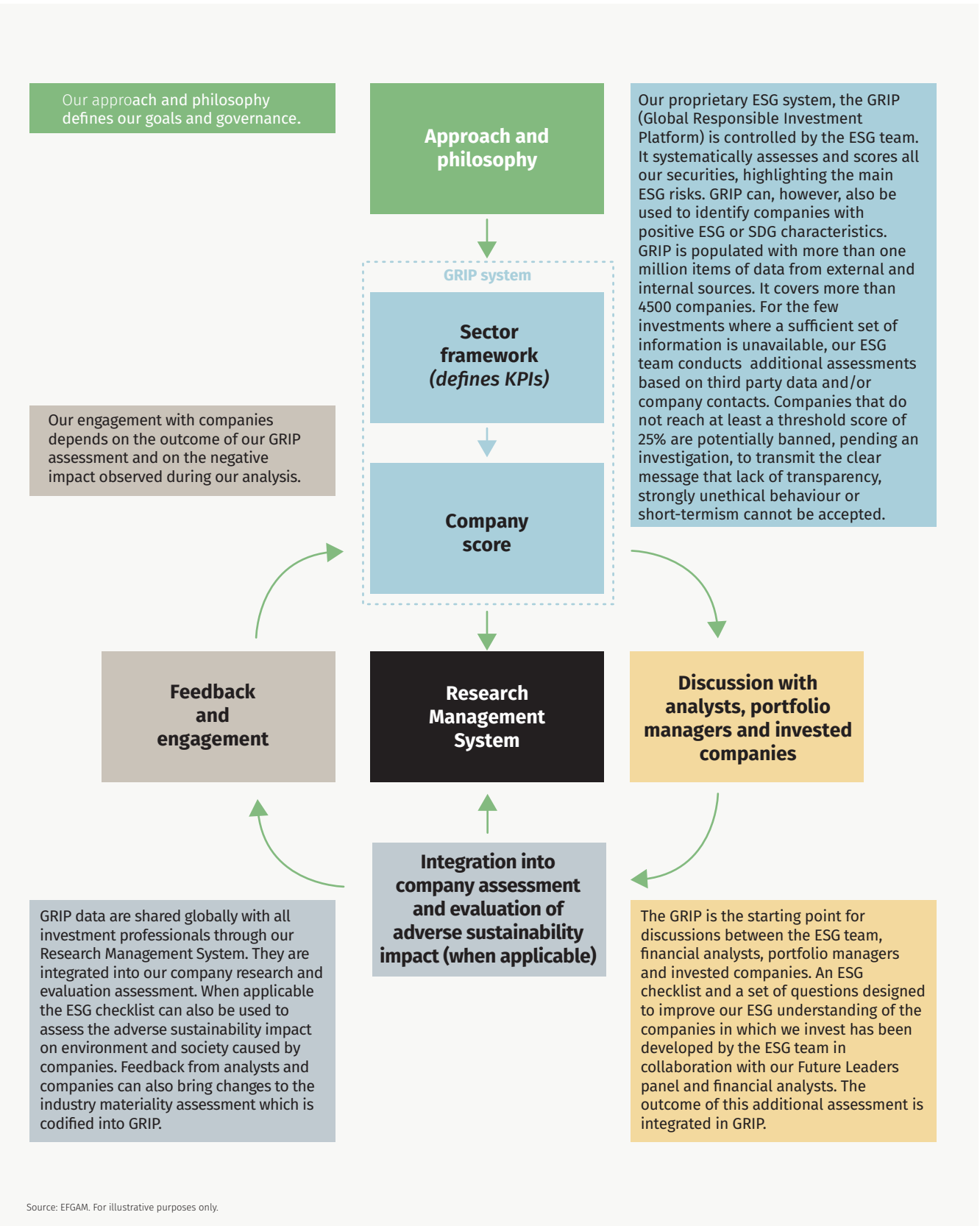
Our many years of experience looking at ESG issues, and the fact that we have built the proprietary GRIP framework, means that we have an advantage when it comes to understanding the underlying issues and interpreting the data. GRIP is much more than an ESG rating system and gives us several unique benefits:

- Our framework is based on the main ESG reporting standards, meaning it can easily adapt to any regulatory change.
- The control we have on the framework allows us to clearly define the material aspects we want to include in our assessment for every industry group.
- We can easily integrate inputs from our analysts around the world and adapt our framework to more accurately capture the nuances between industries, the emergence of new risks/opportunities or specific company issues.
- Controversies are integrated within the GRIP and the assessment scoring. This allows us to control for the risk of ‘greenwashing’ – a company appearing greener than it actually is – which can significantly contribute to the final score.
- The better understanding we have of ESG issues due to the direct handling and analysis of data allows for a better integration into our investment process.

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1. EFG's ESG integration approach



Source: EFGAM. For illustrative purposes only.

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Engagement

Engagement is a natural addition to our investment process. When GRIP identifies a risk that may have a negative impact on financial performance or society, this can trigger the engagement process. The decision is shared by the ESG team and the financial analysts or portfolio manager and follows the rules identified in our engagement process.

We are well aware that embracing an ESG-oriented attitude by invested companies can be highly demanding: this may sometimes translate into implementing new processes, innovating the corporate culture, questioning the way of doing business or aiming to change a company's mindset. Our goal is not to interfere in the management of a company. Rather, it is to point out weaknesses which could be negatively perceived by the market and therefore impact the company's future growth. We therefore actively keep an eye on issues that could be raised by relevant stakeholders of the investee companies such as NGOs, local communities and suppliers. We prioritise issues that are at the crossroad of financial materiality and the UN Sustainable Development Goals (SDGs), many of which have a close mapping to ESG considerations (see Figure 2).

We support the idea that the current global challenges addressed by the 17 SDGs, such as social inequalities, decent work and economic growth and responsible production and consumption, may be effectively met only with the involvement of the private sector. Results of the engagement activities will eventually be communicated through our Research Management System (RMS) to our analysts and fund managers to allow a proper integration of the outcomes in the underlying investment case.

Proxy voting

Proxy voting is a critical component of our ESG approach. In partnership with ISS (Institutional Shareholder Services) we selected a Climate Voting Policy that helps us promoting sustainable business including stewardship of the environment, with a specific focus on climate change issues, fair labour practices, non-discrimination and the protection of human rights, according to international standards, as applicable.

For these reasons we developed guidelines that summarise our positions on various issues of concern and indicate how we generally vote shares.

On a case-by-case basis we may also revisit the voting decision based on the outcomes of GRIP or engagement activities.

Exclusion lists

All EFG portfolios are required to respect an exclusion list that is codified into our investment management software. In addition to companies which are potentially subject to international sanctions, we exclude all companies involved in the production of controversial weapons (such as cluster bombs, anti-personnel landmines, chemical and biological warfare) and companies producing nuclear weapons for countries that have not signed the Treaty on the Non-Proliferation of Nuclear Weapons.

We also removed companies that we think are in clear and direct violation of UNGC (UN Global Compact) principles unless we engage with them or gain reasonable confidence they put in practice mitigation measures to avoid repeating the breach.

2. ESG and the Sustainable Development Goals (SDGs)



Source: EFGAM. For illustrative purposes only. The square numbered boxes show individual SDG goals. We map these to Environmental, Social and Corporate Governance issues and list some of the key considerations which we see as most relevant.

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In addition to the above, we screen out all the companies that fall below our 25% minimum ESG score, as measured by our GRIP system and companies with a coal share of revenues above 30% and no clear exit strategies. Finally we remove from our investable universe companies that breached Global Compact principles unless an engagement process is set-up.

ESG across asset classes

Figure 3 summarises the current practice for integrating ESG across asset classes and the investment process within EFG. Much has been done, but we are aware that sustainable investing is a journey and further progress still lies ahead.

Conclusion

Our ESG integration process, especially when used in conjunction with our engagement process, provides a logical and coherent way of addressing the challenges of responsible investing. Undoubtedly, the process will develop further but the key elements of an effective, practical system are in place.

3. EFG's current practice for ESG integration

	ESG Integration	Additional ESG Actions
Equities and fixed income research	<ul style="list-style-type: none"> → Sustainability Risk analysis required by internal regulations and integrated into investment analysis templates. → Ban of companies producing controversial weapons, coal and in breach of global compact principles* → Restriction of investable universe on the basis of ESG metrics to send a clear message that lack of transparency, strongly unethical or short-term thinking and behavior can't be accepted. 	<ul style="list-style-type: none"> → Sustainability questions for company analysis. → Feedback loop to improve data and ratings. → ESG Checklist to monitor adverse sustainability impact of companies → CO2 risk model based on NCFS scenarios
Long Only funds research	<ul style="list-style-type: none"> → Asset managers scored using Inputs from UNPRI assessment reports and EFG questionnaire. → ESG questions integrated into 3rd party fund analysis. Emphasis on tangible evidence that firm's include ESG in process. 	<ul style="list-style-type: none"> → Portfolio review for Blacklisted companies → Review exclusion lists where available
Hedge funds and alternatives	<ul style="list-style-type: none"> → Sustainability Risk assessment integrated in Due Diligence questionnaire. 	<ul style="list-style-type: none"> → Communication of EFGAM ESG policies and request to produce ESG policies. → Transparency requested on PRI reporting assessment , if existing.
Equity funds	<ul style="list-style-type: none"> → ESG analysis required by internal regulations and integrated into investment analysis templates. → Ban of companies producing controversial weapons, coal and in breach of global compact principles.* → Restriction of investable universe on the basis of ESG metrics to send a clear message that lack of transparency, strongly unethical or short-term thinking and behavior can't be accepted. 	<ul style="list-style-type: none"> → Engagement with companies on the basis of ESG data. → Collective engagement. → ESG Checklist availability to better monitor companies sustainability risk → Proxy voting based on a sustainability overlay. → CO2 risk assessment. → ESG analysis of portfolios..
Fixed income funds	<ul style="list-style-type: none"> → ESG analysis for all issuers required by internal regulations and integrated into investment analysis templates. → Sovereign and Supra ESG analysis. → Ban of companies producing controversial weapons, coal and in breach of global compact principles.* → Restriction of investable universe on the basis of ESG metrics to send a clear message that lack of transparency, strongly unethical or short-term thinking and behavior can't be accepted. 	<ul style="list-style-type: none"> → Collective engagement. → ESG Checklist availability to better monitor companies sustainability risk. → CO2 risk assessment. → ESG analysis of portfolios.
Asset allocation	<ul style="list-style-type: none"> → Climate Risk analysis integrated in AA decisions. → Stress test scenarios for countries and industry groups. 	<ul style="list-style-type: none"> → TCFD (Task Force on Climate-related Financial Disclosures) Reporting.
Advisory	<ul style="list-style-type: none"> → ESG ratings integrated in approved lists. 	

* See Sustainability Risk policy for further details

Important Information

The value of investments and the income derived from them can fall as well as rise, and past performance is no indicator of future performance. Investment products may be subject to investment risks involving, but not limited to, possible loss of all or part of the principal invested.

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