



# ESG Quarterly Report

First quarter 2019

## Nordea 1 – Global Stars Equity Fund



The aim of this document is to describe some of the activities that the Responsible Investment (RI) team has done over the last quarter for this specific fund. This tool, therefore, is not meant to be fully comprehensive, but to allow investors to follow-up on the fund's relevant ESG-related issues (Environmental, Social and Governance) and the main activities that the RI team has been involved in.

### Introduction to the STARS concept

Nordea's STARS funds proactively select high-quality ESG companies with the objective to identify tomorrow's winners, which, we believe, will have sustainable business models and the ability to conduct their businesses responsibly in relation to their stakeholders – employees, suppliers, customers, investors and society at large. Nordea's RI team works together with the fund's financial analysts and portfolio managers in order to deliver a solution that is able to:

- **Outperform the benchmark:** creating added value by enhanced long-term returns.<sup>1</sup>
- **Meet Nordea's ESG standards:** analysing each individual stock to ensure that the fund invests only in companies that respect certain ESG criteria. The idea is to invest in leading companies (rated A<sup>2</sup>) or companies with a sufficient rising ESG profile (e.g. rated B<sup>-2</sup> in the case of the Nordea 1 – Global Stars Equity Fund), thus avoiding the laggards (lower rated companies).
- **Active ownership:** proactively engaging companies and encouraging them to improve their management systems, their ESG performance or their reporting, as well as exercising formal rights in the voting resolutions.

### Engagement is key for active ownership

Being part of Nordea's responsible investment policy, the fund excludes companies involved in the production of

nuclear weapons and cluster munitions as well as companies with large exposure to coal mining (>30% revenues). However, excluding a company from our portfolios is always a last resort: the **STARS concept aims for positive selection** with the objective to influence companies to improve their ESG profiles. **Engagement therefore takes a new dimension with the STARS.** It does not only consists of the traditional forms of engagement, like the exercise of voting rights or entering into a dialogue to encourage companies to improve their management systems, their ESG performance or their reporting. When assessing a company's ESG risk profile we also focus on specific themes utilising UN Sustainable Development Goals. Thus, we distinguish two types of engagement:

- **Risk Engagement:** if a company is not managing its material ESG risks well, the RI team engages with the company on the issue. The ESG risks can be company specific or stem from the country in which the company operates or its industry. Violations of international norms and conventions are also addressed under Risk Engagement.
- **SDG Engagement:** conducted with a specific focus on companies' exposure to certain themes, which might represent a significant material risk for the company. **Nordea believes that companies that align their strategies with the UN Sustainable Development Goals (SDGs) will be successful** in the long-term, because they are adjusting to global society's future needs.

**The UN Sustainable Development Goals (SDGs)** cover a broad range of social and economic development issues as part of the 2030 Agenda. In this edition of the quarterly report we have highlighted 1 UN goal; this goal has been the focus of the engagement activities described in the coming pages.



This is the UN Sustainable Development Goal (SDG) our ESG analysts focused on – during the period covered – when engaging with the companies. The complete list of SDGs can be seen on page 3.

1) There can be no guarantee that this strategy and process will produce the intended results and no guarantee that the strategy will achieve its investment objective. The value of your investment can go up and down, and you could lose some or all of your invested money. 2) ESG rating scale

## Top ESG activities over the quarter

Holding	Current Rating	Proxy Voting <sup>3</sup>	SDG Engagement	Risk Engagement	Activity
Munich Re	A	–	13	Climate change governance	Research/Call
Amazon	B	–	N/A	Labour rights	Research/Call
Booking Holdings	B+	–	N/A	General analysis	Research/Call

<sup>3</sup> Proxy voting refers to the last 12 month-period. Generally we vote in annual reports and most of the Annual General Meetings (AGM) which occurs once a year. If there is no vote, it is generally because the fund was not invested at the time when the AGM happened. Please find out more on [nordea.com/sustainability](https://nordea.com/sustainability) or access directly the [voting portal](#).

ESG rating distribution (from best to worst) applicable to this fund:



Sustainable Development Goals (SDG) utilised in this report:



## Rating changes

There was only one rating changing during the quarter: Apple was upgraded from B- to B+.

## Main highlights of the ESG activities over the quarter

The following activities have been selected to share with investors some of the highlights of the period. Please note that when engaging with companies, the processes might last for multiple quarters, as such we might not necessarily report on the final decisions.

### Amazon

The company is often subject to discussions on a wide range of issues that can be traced back to ESG concerns. We have extensively assessed the company from different angles including the environmental footprint, cyber security efforts and labor management practices. Within the scope of our analysis, we highlighted the company's labor management practices as perhaps the most acute ESG-issue. While we acknowledge positive developments especially at the end of last year, with minimum wage increases for its US based employees, with the full effect yet to be determined as a net positive or negative, we also noticed a red flag regarding norm breaches from one of our service providers concerning an Amazon subsidiary. The flag concerned the subsidiary's labor policy which was allegedly in breach with national regulations. We contacted both the company and the service provider and realized that the issue was overstated as Amazon took adequate actions to address this specific issue.

We acknowledge that there is still room for improvement within the labor management area and will continue to monitor closely along with other aspects in the context of our ESG analysis.

## Booking Holdings

Booking Holdings, also previously known as Priceline, exhibits a relatively straightforward business model that provides an online platform connecting travelers with providers of traveler services. The main ESG challenges relate to cyber security. In a pre-2016/2017 world, this business model would probably have exhibited a low ESG risk profile. This is a good example of how our own risk perception can change significantly within a relatively short time period. GDPR and related regulations have substantially altered the way we assess now the ESG exposure of such companies, including Booking.

We found evidence of a strong commitment from both management and the board concerning cyber security and privacy related issues. The company has relevant policies in place as well as third-party verifications of its systems. As compared to its peers, it still falls short in terms of reporting.

On a positive note, there have not been any significant cyber breaches but nevertheless, the company has been subject to other attacks on its brand by hackers trying to use various techniques to get entry into users' data.

### Munich Re

We engaged with the company to get some background on their decision to stop underwriting new coal business. The pledge to limit or exclude coal from insurance underwriting has become a new norm in the sector where AXA, Swiss Re, and several other insurers have also committed. Munich Re came as a surprise in August 2018, about a week after the CEO publicly declared the company would not consider stopping coal underwriting. Munich Re was therefore first criticised for not committing to such topic and then for having loopholes in its commitment. Our assessment was focusing on why the sector leader in climate change expertise committed so late and in a weaker way than its competitors.

We had an open and hard-hitting conversation with Renate Bleichert, Munich Re's head of sustainability, to understand the reasons behind such story and test the credibility of Munich Re's climate leadership at this point.

In a nutshell, the management board was hesitant to commit to exclude coal due to the size and complexity of Munich Re's energy portfolio. Ultimately, they managed to agree to the standard industry commitment of not underwriting new coal projects, with some country-based exceptions. The sustainability team has a veto right and decides exceptions on a case by case basis. The countries that can be exempt have under 10% electrification rate (based on IEA data), and an exception has only been requested three times since August 2018. It wasn't granted in any of the cases.

Munich Re also pointed out its activities to create innovative insurance products which incentivise the adoption of climate solutions and the roll-out of renewables. This is a small part of the overall product portfolio, and the RI team has yet to be persuaded that it is a sufficiently significant growth driver.

Our key takeaway is that Munich Re is probably a leading climate expert but has a problematic relationship in being a policy leader. Its superior expertise is primarily used, perhaps unsurprisingly, to sharpen premium setting, but top leadership is extremely cautious about any perceived jeopardy to returns. To some extent, the sustainability function is trying to turn very entrenched practices around. We understand external investors' voices have significant weight within the board, and therefore we need to express our views to these investors in a suitable setting. We believe this will influence Munich Re to further progress on the topic. We currently consider sending a letter as there would be a significant reputational benefit should Munich Re superior climate expertise translates into a genuine policy leadership.

### Complete list of SDGs:



Source: [un.org/development/desa/en/news/sustainable/sustainable-development-goals.html](https://un.org/development/desa/en/news/sustainable/sustainable-development-goals.html)

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