

# Responsible Investment in External Management

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## 1. Introduction

As a long-term investor, PGGM Vermogensbeheer B.V. (PGGM Investments, hereinafter PGGM) is committed to investing responsibly. PGGM manages its clients' External Management investments in order to contribute towards a stable pension for their participants while also taking into consideration its impact on the world. PGGM recognizes that environmental, social, and governance (ESG) factors have a material impact on the financial performance of the portfolio, especially in the longer term. As such, integrating ESG issues into investment analysis and decision-making processes is part of its fiduciary duty.

This guideline addresses PGGM's management of ESG issues with regard to External Management. The guideline is a further refinement of [PGGM's Responsible Investment Framework](#) and its implementation guidelines and the relevant fund prospectus and ancillary documentation. In addition, the obligations arising from compliance with legislation and regulations apply. The guidelines cover all investments made by External Management, effective since 1 January 2021.

## 2. Investment strategy & approach

The External Management department (External Management) of PGGM Investments selects, monitors and manages, on behalf of our clients, funds and segregated mandates which are managed by one or more internal and/or external managers. PGGM Investments recognizes the important role External Management has with regard to responsible investment, which is to ensure that our managers apply our and our clients' policies and guidelines and where relevant, proactively manage Environmental, Social and Governance (ESG) risk and opportunities.

External Management will seek further understanding of the actual activities of the manager in integrating ESG in their investment process. This is included in the selection and monitoring of managers. It is expected that the managers live up to the spirit of the PGGM Responsible Investment beliefs in both their investment processes and in the way that they organize their business. Where relevant the managers are expected to analyse the portfolio companies on their financial merits as well as their ESG performance. External management believes this helps to reduce investment and reputational risk or increase (expected) returns of the portfolio.

By having in place a transparent responsible investment guideline for External Management, as further outlined in this document, and by actively taking into account ESG-related performance in investment decisions,

External Management believes that it offers a positive contribution that is best practice and in line with clients' stated objectives.

The team aims to be fully compliant with obligations arising from legislation and regulations. The relevant standards, codes of conduct or (inter)national initiatives or legislation that apply and have an impact on implementation are discussed below. For more detailed information please see [PGGM Investments website](#).

Besides implementing client policy and complying with rules and regulations, External Management believes that ESG factors can have a material impact on the financial performance of its investments and sees it as its responsibility to capture the value of and mitigate the risks related to ESG factors. In addition to this, we firmly believe that sustainable development can contribute towards stable and good investment returns for our clients in the long term. External Management therefore, where possible and meaningful, aims to actively seek for and contribute to solutions that increase the positive impact of the goals as defined in the [PGGM Responsible Investment Beliefs](#). Moreover, we believe in the driving force of our clients' capital.

## 3. Implementation

### 3.a. ESG-integration

PGGM defines ESG integration as systematically taking into account those ESG factors that have a material effect on investment risk and return. Across its entire portfolio PGGM uses the [Materiality Map of the Sustainable Accounting Standards Board \(SASB\)](#) as the framework to identify material ESG issues per sector. Where relevant, External Management aims to select managers who take the SASB Materiality Map or equivalents into account when analysing ESG risks and opportunities in the investment process.

External Management uses the PGGM Selection and Monitoring Framework (SMF) to assess the quality of potential managers and for ongoing monitoring of current managers. This framework consists of seven categories: Philosophy, People, Process, Performance, Planet (ESG), Platform/Organization, Price/Costs.

The category 'Planet' is the basis to determine the extent to which the external manager has integrated responsible investing in its investment process and to which extent it is incorporated in its day to day operations.

The SMF consists of 2 stages:

- 1 Selection
- 2 Monitoring

### Ad 1 Attention to 'Planet' (ESG) in the Selection stage

In this stage the focus will be on understanding the managers' policies, beliefs and commitments regarding responsible investment and how the manager has organized the responsibility for responsible investment. We assess the managers' degree of ESG-integration and active ownership.

We seek to appoint managers whose objectives and beliefs on ESG integration match those of PGGM and our clients. To score the manager on "Planet" we look at both the company level as the strategy level, based on the "PRI Asset Owner Manager Selection Guide". ESG risks are defined as risks for the financial returns from material ESG factors. During the selection process, it is evaluated how the managers integrate ESG risks in their decision making as follows:

#### ESG Policy:

- What are the manager's beliefs on ESG integration?
- To what extent is ESG integration part of the investment philosophy?
- Does the manager have an ESG policy in place and is it comprehensive?
- Has the manager signed up to the UN PRI or similar initiatives?
- How do ESG policies and guidelines affect investment decision making processes?
- What processes and systems are in place to consistently implement these policies?
- Do engagement activities and proxy voting guidelines reflect ESG policies?

#### Governance of ESG integration:

- Who is responsible for ESG integration at what level?
- What are the skills and competence of the staff in this area, be it a dedicated ESG integration team or portfolio manager who has to implement the policies?
- How are people trained on ESG integration?

As a minimum the manager has to be able to implement the ESG integration requirements as specified in the mandate. The extent to which this plays a role in scoring the manager depends on the importance the client on whose behalf the selection is performed places on ESG integration. If a manager scores poorly on "Planet" this can further contribute to an overall negative score, meaning the manager will not be selected. In general we favor managers that have articulated their beliefs on responsible investment and that have demonstrably integrated ESG risks in their investment process.

### Ad 2 Attention to 'Planet' in the Monitoring stage

The same areas are evaluated on a structural basis when External Management monitors the appointed managers and periodically meets with management. PGGM

determines how ESG factors will be discussed, which assessment criteria apply to them, what reporting requirements and KPIs are laid down and how the ESG performance of the underlying investments are monitored. Before meeting with management, the relevant subjects for the discussion are determined. The integration of ESG risks is a standard agenda item. Where available, the manager's reporting on this topic provides important input to this discussion. We will structurally consider relevant developments and research regarding ESG integration during the review period. The appointed manager will be asked to explain how the investment strategy and decisions by portfolio managers align with our expectations, as stated in the Asset Management Agreement and if and how investment decisions have been influenced by ESG considerations.

The PGGM External Management team manages several mandates and funds that operate in a diverse set of countries and sectors, which gives it exposure to a broad variety of ESG risks and opportunities. ESG is integrated in the investment strategy and approach to help reduce ESG-related investment and reputational risks or increase (expected) returns of the portfolio. Climate-related risks, which are considered a sub-set of ESG risks are therefore covered by the ESG integration process of External Management.

Besides this, PGGM External Management aims supporting PGGM's ambition of assessing and monitoring the exposure of its whole portfolio to climate risks by 2025.

### 3.b. Impact

In addition to a better-performing portfolio, External Management seeks to enhance the positive impact of its investments and to minimize adverse impacts even when they do not directly affect the financial performance.

#### 1. Positive impact: investing in the SDGs

In 2016 PGGM and APG defined Sustainable Development Investments (SDIs) as "investments that yield market-rate financial returns while generating a positive social and/or environmental impact" (i.e. contribute to the Sustainable Development Goals). In 2020 Australian Super, British Columbia Investment Management Corporation joined APG and PGGM in the [SDI-Asset Owner Platform](#) which owns a taxonomy of products and services (solutions) that contribute to the SDGs. With a set of decision rules the taxonomy forms the basis for the classification of investments as 'SDI'.

PGGM largest client's ambition is to increase the SDI volume to 20% of the total portfolio by 2025. The effort to measure portfolio companies' real-world impact, however, is currently limited to seven focus SDGs: #2 (zero hunger), #3 (good health and wellbeing), #6 (clean water and

sanitation), #7 (affordable and clean energy), #11 (sustainable cities and communities), #12 (responsible consumption and production) and #13 (climate action). To estimate and monitor the impact on these focus SDGs, the indicators suggested by the [Working Group on SDG impact measurement](#) of the DNB-facilitated Sustainable Finance Platform are used.

PGGM External Management aims to appoint external managers whose objectives and beliefs on responsible investment closely match those of PGGM and our clients. This includes our client's ambition to create a positive SDG impact. We stimulate the external managers to contribute to these impact ambitions through their investment decisions and, where applicable, by measuring this impact. This will vary per mandate as tracking an equity index is significantly different than managing an impact focused equity portfolio. To a large degree the positive impact of our externally managed investments is measured through our internally developed methodology.

For each of the asset categories that we monitor, PGGM compare their ESG score versus the benchmark and report on this on a monthly basis. There is continuous progress in improving the quality of ESG and impact reporting (like CO<sub>2</sub> reduction), mainly due to investors like PGGM who discuss this topic on every manager meeting and call. We use MSCI, Trucost and Sustainalytics data (and are planning to also use the Entis data once available) to compare the managers to their benchmark and to their peers.

PGGM Responsible Investment department has created a framework to identify which bonds can be defined as Positive Impact Bonds. The investment teams with credit mandates can propose new names to this universe. PGGM RI ultimately defines which bonds are eligible to be defined 'Positive Impact Bonds'. Green bonds are part of these Positive Impact Bonds. All Green bonds are Positive Impact bonds, however not all Positive Impact bonds are green bonds.

Managers who manage an equity impact mandate are expected to conduct a thorough impact analysis of the companies, perform an in-depth analysis of ESG factors and also pay attention to the possible reputation risk. The decision to invest in a company is explained in a 'company paper' in which the positive impact that the company creates. In other mandates, for example, the emphasis is on reducing the carbon footprint. This can be achieved by adjusting the benchmark and removing the companies with the highest CO<sub>2</sub> emissions, or by reducing the CO<sub>2</sub> budget for the portfolio over a certain period of time.

## 2. Adverse impact: minimise negative impact

The social and environmental impact of the capital entrusted to us by our clients is significant. We can stimulate a positive contribution to a sustainable world and have the responsibility to minimise adverse impact. Adverse impacts refers to negative impacts (harm) to individuals, workers, communities and the environment. External Management has embraced this responsibility and integrated it in our investment process along with other ESG issues in the selection and monitoring process

During the selection process, the managers are evaluated on how they report on the eventual negative impact of their activities according to the following guiding questions:

- Does the manager report on ESG-related incidents in portfolio and how it acts to address these?
- Is reporting publicly available?

During the monitoring process described in paragraph 3, the discussion covers incidents regarding ESG integration during the review period.

As from 1 January 2022 at the latest, PGGM shall avoid new investments in companies that are in very severe violation of the OECD Guidelines for Multinational Enterprises (hereinafter OECD guidelines) and/or the UN Global Compact principles. When feasible, PGGM shall undertake best efforts to divest existing exposures to these companies all together and/or shall engage with the companies, or a selection thereof, that are in (very) severe violation of the OECD guidelines and/or the UN Global Compact principles.

Based on its high likelihood and severity, climate change as a driver of adverse impact is prioritized. Clients of PGGM's have committed themselves to the Dutch Climate agreement and to the Paris Climate Agreement to align policies consistent with the objective to limit the global temperature rise to a maximum of 1.5 °C. The ambition is to have a climate neutral investment portfolio by 2050 - in line with the ambition of the European Union and the Paris objectives.

PGGM measures the carbon footprint of the externally managed funds and segregated mandates. The results of carbon footprint measurement will serve to establish a full overview of all carbon data of externally managed assets.

### 3.c. Stewardship (engagement, voting, litigation)

PGGM actively uses its influence as a shareholder to achieve improvements in the ESG field, thereby contributing to the quality, sustainability and continuity of companies and markets. We see it as our responsibility to engage with market parties and companies about their policies and activities. In this way, we attempt to realise ESG-related improvements. PGGM applies customized voting principles across all its listed equities, written down in our [PGGM Voting Guidelines](#).

PGGM itself acts as an active owner for all of its assets, including those managed externally. In practice this means that for example all voting and engagement for listed equity holdings is done in-house and not by external managers themselves.

We do however closely monitor the stewardship behaviour of our external managers. In case there is a misalignment with our own viewpoints, as laid down in our Global Voting Guidelines, policy documents and/or public statements, we discuss this with the external manager in question.

#### Good Governance

PGGM Investments endorses internationally recognized and/or accepted basic principles of good corporate governance and proper checks and balances. It refers to the six basic 'Principles of Corporate Governance' by the Organisation for Economic Development and Co-operation (OECD) and the 'Statement on Global Corporate Governance Principles: Revised' by the International Corporate Governance Network (ICGN). Being a Dutch asset manager with generally only Dutch clients and beneficiaries, our views on specific corporate governance issues are, next to the OECD and ICGN principles, also guided by Dutch law, rules and regulations, the Dutch corporate governance code, and the recommendations of Eumedion (the Dutch representative of the interests of institutional investors in the field of corporate governance) (hereinafter referred to as our 'Dutch Descent'). Accountability, transparency and shareholder rights are key corporate governance issues to PGGM Investments. Locally different views on corporate governance standards and/or local corporate governance codes and/or best practices may be taken into account.

At the request of clients PGGM can act as an active owner on their behalf. When asked, we use the following instruments:

- Engagement: PGGM engages companies and market participants, including regulators. We do this in order to influence the quality, sustainability and continuity of companies and markets. PGGM works closely with analysts and other engagers within and outside of PGGM.
- Voting at shareholder meetings: PGGM votes on all shares of all listed companies in the portfolio according to its own Voting Guidelines. By doing this PGGM can pursue specific ESG objectives on behalf of clients and ensure this is executed in a consistent manner across all portfolios (also see our Voting Guidelines)
- Shareholder litigation: In case of (expected) misconduct, like fraud or corruption, by listed or unlisted companies PGGM can conduct legal proceedings as a shareholder on behalf of its clients

Clients who do not use PGGM services in this area have usually appointed dedicated service providers to undertake their active ownership activities. It is therefore not expected from external managers to act as an active owner on our clients' behalf. We do expect however that external managers keep us informed about their own active ownership activities through regular reporting to allow us to critically review the outcomes. This enables us to judge the external manager's relative positioning with regard to voting as we are looking for managers that ideally are like minded to our clients.

Engagement is undertaken to influence ESG practices and/or improve ESG disclosure, to improve positive impact and/or mitigate negative impact.

Our engagement activities are focused on (improving) portfolio companies measurement of impact, on improved reporting and on integrating the SDGs into the business strategy of portfolio companies.

### 3.d. Exclusion

The [PGGM Implementation Guidelines on Exclusion](#) are applicable to investments in all asset classes, including External Management. The PGGM-wide product-based Exclusion List consists of companies engaged in controversial weapons, tobacco, tar sands as well as thermal coal utilities and mining companies. Exclusions are included in the agreements with external managers. If a manager violates the policy, actions will be taken to remediate the violation.

By excluding companies on the basis of the above elements, PGGM seeks to prevent PGGM-managed investments contributing financially to practices incompatible with the standards and values of PGGM, its clients and their beneficiaries.

## 4. Transparency

Each quarter we provide an update of our responsible investment activities in our clients' quarterly report. This includes information regarding stewardship activities, impact investing and integration of ESG-factors in our investment decisions. Also, any relevant negative impacts and our monitoring of these impacts, are reported. In addition we contribute to [PGGM Investments annual Integrated report](#) and report on our responsible investment activities in the Principles of Responsible Investment (PRI) annual survey.

## 5. Annex

Please note that there is an Annex applicable for this ESG-guideline. This Annex forms an integral part of this ESG-guideline and may be updated from time to time. The applicable Annex is available on our website.