



Environmental, Sustainable and Governance (ESG) Assessment Process

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In recent years, asset managers have taken a more robust approach to incorporating ESG factors as part of their investment decision making.

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With increasing pressure from governments and organisations such as the United Nations, legislative changes are being made which force companies to report on ESG related matters.

Asset managers have also come under greater scrutiny too and this has resulted in the majority of fund management groups creating firm wide ESG policies and in many cases setting up a team to advise fund managers and analysts on ESG considerations. These developments have resulted in nearly all fund managers now stating that they consider ESG matters when deciding what companies to own, however, the validity of that statement varies greatly. The 'greenwashing' trend has been evident amongst companies and asset managers.

In order to differentiate between funds which are very disciplined from an ESG perspective and those which are simply quoting generic ESG factors without properly incorporating these into their decision making process, we have developed an internal ratings process. The ratings tool will enable us to apply a score to both individual funds and the model portfolios within which they sit.

As part of our model portfolio service, we offer two different types of ethical portfolios for investors who wish to incorporate ESG factors into their investment strategy: 'Ethical' and 'Ethical Bias'. Within both strategies we attempt to incorporate different methods of investing which consider Environmental, Social and Governance (ESG) issues and we seek to avoid sectors and companies which have poor ratings for key environmental, social and governance criteria.

Within our Ethical Bias strategies, we will attempt to replicate our preferred asset mix for our core 'growth' portfolios. Where

possible, this will be done via the use of funds which have ESG considerations as a key part of the investment process, however, where a suitable ethical fund is not available, we will use the funds selected within our core 'growth' portfolios.

For our 'Ethical' strategies, we will only use funds which have stringent ESG criteria in place. As a result, the allocation across asset classes, geographical regions and sectors may differ from the 'Ethical Bias' and 'Growth Portfolios'.

The investment funds used will incorporate different methods of ESG friendly investing. In some cases, this will be a more traditional negative screening process, which involves avoiding companies operating in certain industries. For example, the majority of ESG funds have no exposure to energy (oil and gas) companies which typically score poorly from an environmental perspective.

The funds will also incorporate newer methods, such as impact based investing, which involves investing in companies that offer a product or service helping to address specific environmental or social issues. For example, one of the long-standing funds we own within our ethical portfolios was designed to ensure any investment the fund makes delivers a positive social outcome within the UK. The fund managers work in conjunction with the Big Issue to assess the suitability of their investment process.





Other impact-based funds we own within the Ethical portfolios target specific companies making our way of life more sustainable, with these funds typically investing in line with the United Nations' Sustainability Development Goals.

The funds we own typically have governance panels in place which comprise independent experts from a range of sectors to help ensure the fund adheres to their ESG process. Fund managers will report to the panel as and when they want to make changes to the investment fund and members of the panel will provide guidance on the suitability of investments from an ESG perspective.

Rating process

As well as conducting qualitative research by speaking to fund management teams to better understand their views and processes with regard to ESG, we have developed a ratings tool to allow for a more direct comparison between individual funds.

The ratings tool enables us to grade funds based on their ESG credentials. Funds are rated with a score of 0 to 5 based on the following criteria:

- Are ESG considerations factored into the investment process?
- Does the fund exclude any sectors or companies based on ESG considerations?
- Does the fund invest to target specific ESG related outcomes – e.g. UN Sustainable Development Goals?
- Are any external/independent bodies consulted to assess the suitability of investments based on ESG factors?
- Does the fund have exposure to sectors with the highest environmental and social risks?*
- The Institutional Shareholder Services (ISS) ESG rating supplied by FE analytics for the fund (from 0 to 5 stars).

*Based on the top 5 highest risk sectors according to the ESG Risk Atlas assessment from Standard & Poor's Global Ratings.

The questions are deliberately broad based so that a rating can be applied to funds which are not focussed on ESG as a core principle of the investment strategy. Criteria which is too specific to ethical or sustainable investing would hinder our ability to assess the ESG credentials of mainstream, 'non-ethical' funds. The question regarding specific ESG related outcomes and the use of external or independent bodies should result in funds which are genuinely focussed on sustainable or impact investing achieving a good score.

In addition, the rating tool has been designed in a way which will lower the overall rating for funds which are 'greenwashing'. For example, a fund may score well on the basis of factoring in ESG considerations to the overall investment process, but still hold investments within sectors that have the highest environmental and social risks. By applying a greater weighting to the question on sector exposure, a fund will be 'downrated' by holding companies in the worst sectors and this therefore ensures that funds are rated based on actual behaviour rather than generic statements regarding the incorporation of ESG.



The key details considered within each criterion are as follows:

Are ESG considerations factored into the investment process?

- Does the manager consider environmental, social or governance issues when deciding on whether a portfolio company is a suitable investment?
- Does the manager consider the impact resulting from positive or negative corporate behaviour? E.g. the potential impact on a stock's valuation.
- Does the manager seek to have a portfolio with a better ESG score or rating than their benchmark? For example, some funds are focused on having a portfolio with lower Co2 emissions than a generic index such as MSCI World.

Does the fund exclude any sectors or companies based on ESG considerations?

- Does the manager have a policy in place to exclude whole sectors? E.g. tobacco, arms, oil & gas.
- Are some companies excluded based on environmental issues, corporate behaviour or the impact on society? For example, some managers exclude Facebook/Meta due to the Cambridge Analytica scandal and the impact that information spread via the platform can have on society.

Does the fund invest to target specific ESG related outcomes – e.g. UN Sustainable Development Goals?

- Are the managers committed to investing in companies which help address issues such as those identified by the UN SDGs and is this stated within the fund's objectives or memorandum?
- Does the manager evidence how portfolio companies are helping to meet these goals and is this monitored over time?

- How many of the portfolio companies generate most of their revenue via operations which appear to directly address the ESG related goals? Is the manager using a non-core part of the business to justify the holding and is this a common theme across the portfolio?
- Do the portfolio companies' operations have a strong link with the ESG related outcomes or is there only a tentative link between the two?

Are any external/independent bodies consulted to assess the suitability of investments based on ESG factors?

- Is there an independent committee in place?
- Do members of any external or independent committee appear to have relevant knowledge or experience that will help steer ESG considerations for the fund managers?
- Is there any evidence of the external committee raising concerns around ESG or challenging the fund manager's decisions?
- Has the manager consulted a company specialising in ESG, e.g. Morningstar Sustainalytics?

Does the fund have exposure to sectors with the highest environmental and social risks?

- Funds which own companies in these sectors are unlikely to have very stringent ESG criteria.
- The Standard & Poor's ESG Risk Atlas uses a thorough assessment process with detailed rationale to rank a wide range of sectors. The 2019 Risk Atlas determined that the following 5 sectors have the highest combined risk from an environmental and social perspective:
 - Oil and Gas
 - Metals and Mining
 - Coal Power Generation
 - Refining
 - Chemicals

ISS ESG ratings

In order to incorporate data from an independent source with access to a broader range of data on funds and their underlying companies, we have used the fund rating from ISS as part of the overall input for our internal ESG fund ratings. Where a rating is not available from ISS, the fund will not be marked down.

ISS ESG is the responsible investment arm of Institutional Shareholder Services Inc. They consider themselves to be the world's leading provider of environmental, social, and governance solutions for asset owners, asset managers, hedge funds, and asset servicing providers. They have more than 30 years of corporate governance expertise and 25 years of providing in-depth responsible investment research and analytics.

ISS ESG enables investors to develop and integrate responsible investing policies and practices, engage on responsible investment issues, and monitor portfolio company practices through screening solutions. It also provides climate data, analytics, and advisory services to help financial market participants understand, measure, and act on climate-related risks across all asset classes. In addition, ISS ESG delivers corporate and country ESG research and ratings enabling its clients to identify material social and environmental risks and opportunities.

The ISS ESG Fund Rating Report aggregates data and information from existing ISS ESG research products and summarizes fund performance based on the ESG performance of the underlying holdings. In addition, data on fund holdings is sourced from Refinitiv Lipper. The ISS ESG Fund Rating reports and data factors are updated monthly and represent a snapshot of the current ESG and Refinitiv Lipper data at the time of data generation.

ISS produce a star rating for each fund based on their own internal reports and criteria. The different criteria and reports which are used by ISS to arrive at each fund rating are summarised below:

- Corporate Rating
- Country Rating
- Governance Quality Score
- Norm-Based Research
- Controversial Weapons
- Sector-Based Screening
- Energy & Extractives
- SDG Impact Rating
- SDG Solutions Assessment
- Carbon Emissions Data and Climate Scenario Analysis
- Voting Analytics.

Example fund ratings

| Name of fund: | |
|--|-------------|
| Artemis Global Income Fund | |
| Criteria | Assessment |
| Are ESG considerations factored into the investment process? | Yes |
| Does the fund exclude any sectors or companies based on ESG considerations? | No |
| Does the fund invest to target specific ESG related outcomes - e.g. UN Sustainable Development Goals? | No |
| Are any external/independent bodies consulted to assess the suitability of investments based on ESG factors? | No |
| Does the fund have exposure to sectors with the highest environmental and social risks? | Yes |
| ISS ESG rating | 2 |
| Rating (out of 5) | 0.50 |

The above fund achieves a poor score. Whilst the manager does consider some ESG criteria when reviewing the portfolio companies, ESG considerations are not part of the core investment process and this is reflected in the portfolio.

| Name of fund: | |
|--|-------------|
| AllianceBernstein Sustainable US Equity | |
| Criteria | Assessment |
| Are ESG considerations factored into the investment process? | Yes |
| Does the fund exclude any sectors or companies based on ESG considerations? | Yes |
| Does the fund invest to target specific ESG related outcomes - e.g. UN Sustainable Development Goals? | Yes |
| Are any external/independent bodies consulted to assess the suitability of investments based on ESG factors? | Yes |
| Does the fund have exposure to sectors with the highest environmental and social risks? | Yes |
| ISS ESG rating | 5 |
| Rating (out of 5) | 5.00 |

The above fund achieves the highest possible rating. ESG factors are a core consideration for the managers and this is demonstrated at each stage of the process. The fund uses an independent panel to determine the suitability of the portfolio companies, with the panel able to veto any decisions if they feel a stock is unsuitable. UN Sustainable Development Goals are adopted as part of the focus on sustainability and negative screening is employed, resulting in no holdings in sectors which have the highest environmental and social risks.

Example portfolio ratings

| Fund | Allocation | Telford Mann ESG Rating |
|--|------------|-------------------------|
| Product Bank Account | 7.00% | N/A |
| Black Rock Overseas Government Bond Index Fund | 6.00% | 0.50 |
| Janus Henderson Strategic Bond Fund | 5.00% | 2.50 |
| L&G Emerging Markets Government Bond Local Currency Index Fund | 6.00% | 2.00 |
| Vanguard FTSE 100 Index Fund | 5.00% | 1.50 |
| Vanguard FTSE UK All Share Index Fund | 6.00% | 1.50 |
| Fidelity American Special Situations Fund | 5.00% | 0.50 |
| HSBC American Index Fund | 6.00% | 2.00 |
| Schroder US Mid Cap Fund | 6.00% | 3.00 |
| Artemis Global Income Fund | 4.00% | 0.50 |
| First Sentier Global Listed Infrastructure Fund | 4.00% | 0.00 |
| JPL Global Equity Income Fund | 4.00% | 3.00 |
| JO Hambro Global Opportunities Fund | 3.00% | 2.00 |
| L&G Global Infrastructure Index Fund | 7.00% | 2.50 |
| Jupiter Asian Income Fund | 5.00% | 1.50 |
| BMO UK Property Feeder Fund | 7.00% | 4.50 |
| L&G UK Property Feeder Fund | 7.00% | 2.00 |
| Gravis Clean Energy Income Fund | 4.00% | 5.00 |
| JPM Natural Resources Fund | 3.00% | 3.00 |
| Portfolio ESG Score | | 2.11 |

The above is a mainstream 'Growth' portfolio, which does not explicitly incorporate ESG related matters into the asset/fund selection process. However, within the portfolio we do own funds which score reasonably well, with some of the funds having specific ESG related objectives. As a result, the overall score is 2.11 out of 5.

Example portfolio ratings

| Fund | Allocation | Telford Mann ESG Rating |
|--|------------|-------------------------|
| Product Bank Account | 7.00% | N/A |
| Black Rock ESG Overseas Corporate Bond Index Fund | 5.00% | 4.00 |
| Black Rock Overseas Government Bond Index Fund | 6.00% | 0.50 |
| L&G Emerging Markets Government Bond Local Currency Index Fund | 6.00% | 2.00 |
| L&G Future World ESG UK Index | 11.00% | 3.50 |
| AllianceBernstein Sustainable US Equity Fund | 6.00% | 5.00 |
| Fidelity American Special Situations Fund | 5.00% | 0.50 |
| HSBC American Index Fund | 6.00% | 2.00 |
| Baillie Gifford Responsible Global Equity Income Fund | 4.00% | 5.00 |
| First Sentier Global Listed Infrastructure Fund | 4.00% | 0.00 |
| L&G Future World ESG Development Index Fund | 3.00% | 4.00 |
| L&G Global Infrastructure Index Fund | 7.00% | 2.50 |
| Schroder Global Sustainable Value Equity Fund | 4.00% | 4.00 |
| Jupiter Asian Income Fund | 5.00% | 1.50 |
| Columbia Threadneedle UK Property Feeder Fund | 7.00% | 4.50 |
| L&G UK Property Feeder Fund | 7.00% | 2.00 |
| Gravis Clean Energy Income Fund | 7.00% | 5.00 |
| Portfolio ESG Score | | 2.92 |

The above is an 'Ethical Bias' portfolio. With most of the funds selected having ESG as a core part of the investment process, the overall score is relatively strong at just under 3 out of 5.

Example portfolio ratings

| Fund | Allocation | Telford Mann ESG Rating |
|---|------------|-------------------------|
| Product Bank Account | 7.00% | N/A |
| Black Rock Overseas Corporate Bond Index Fund | 5.00% | 4.00 |
| Columbia Threadneedle UK Social Bond Fund | 4.00% | 5.00 |
| Schroder Sustainable Bond Fund | 4.00% | 4.00 |
| Royal London Ethical Bond Fund | 4.00% | 4.00 |
| L&G Future World ESG UK Index | 14.00% | 3.50 |
| AllianceBernstein Sustainable US Equity Fund | 10.00% | 5.00 |
| Baillie Gifford Responsible Global Equity Income Fund | 4.00% | 5.00 |
| BNY Mellon Sustainable Global Equity Fund | 7.00% | 4.00 |
| L&G Future World ESF Development Index Fund | 9.00% | 4.00 |
| Schroder Global Sustainable Value Equity Fund | 14.00% | 4.00 |
| Columbia Threadneedle UK Property Feeder Fund | 10.00% | 4.50 |
| Gravis Clean Energy Income Fund | 8.00% | 5.00 |
| Portfolio ESG Score | | 4.26 |

The above is an 'Ethical' portfolio. All of the funds selected for this portfolio have ESG as a core part of the investment process and as a result the overall score is 4.26 out of 5.

Summary

The fund and portfolio rating tools will help us to monitor changes in the ESG profile of our portfolios and the underlying funds, to ensure that clients with ethical preferences are invested in strategies which adequately incorporate ESG considerations into the portfolio construction.

Given the current inconsistencies between ratings agencies and the rapidly changing ESG landscape, we feel that an internal ratings tool is currently the most appropriate method of assessing funds in a consistent manner.

We anticipate our internal ratings process will evolve over time as new legislation and guidance is introduced by regulatory bodies, governments and rating agencies.





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