storebrand

Solutions

- Sustainable Investments

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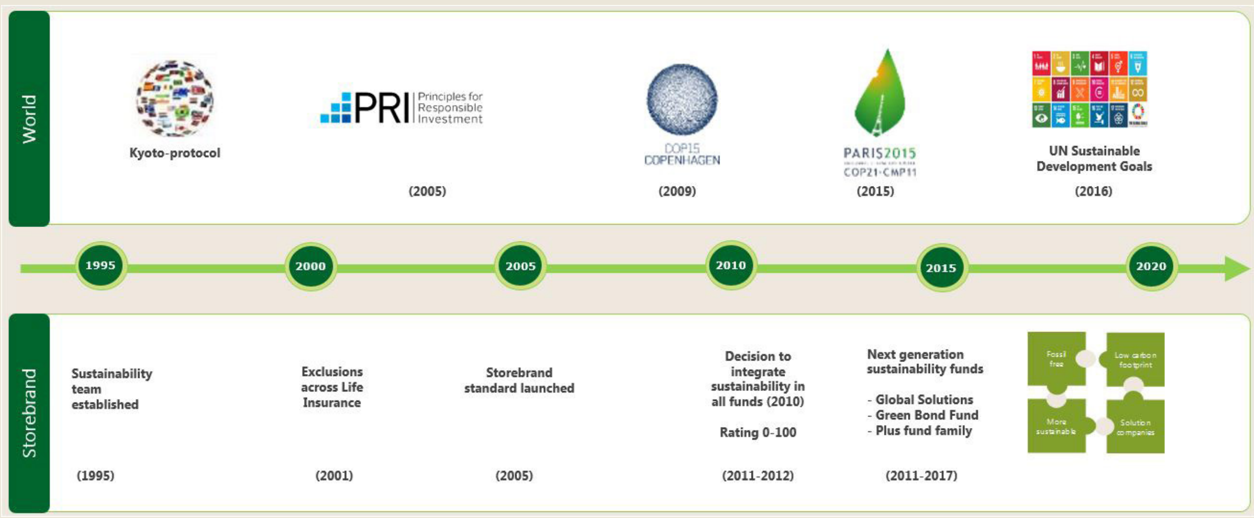


Private Power in a Dysfunctional Political World

Matthew Smith
Head of Sustainable Investments

Sometimes it takes a genuine threat to shake people up and stimulate new solutions from unlikely sources. It seems the recent spike in forest fires in the Amazon basin is just such a threat. Borne out of the laissez faire environmental policies of the Bolsonaro government, the fires demonstrated ever so clearly how fragile the Amazon ecosystem has become and how close we are to an ecological "tipping point". A point where clearing has reached such an extent as to threaten remaining forest areas. With loss of tree cover comes loss of rainfall, and in the summer months the forest becomes a tinder box, greatly exacerbating seasonal fires. In essence, we risk seeing much of the forest transform into savannah like grassland with only a fraction of the once rich diversity of life intact. In addition to loss of bio-diversity, the burning of the forest releases enormous stores of carbon into the atmosphere, speeding up climate change.

In the face of this ever-worsening crisis, what is staggering to witness is the total inadequacy of the national and international political response. In a bout of domestic populism, the Brazilian government has conspired to turn the entire issue of Amazon protection into a question of national sovereignty. Not that the international stage provided much consolation. At the recent G7 meeting, the world's largest economies managed to concoct a $20 million save the Amazon scheme that both proved inconsequential in itself and fired up under President Bolsonaro's seething post-colonial hangover. The Amazon for the time being is Brazil's responsibility alone, and no amount of posturing from Western nations seems likely to alter this uncomfortable fact. Even the drying up of Norway's multi-billion dollar forest fund, conditional on effective forest management, has proved powerless to alter Brazil's course.

What then can be done to alter this destructive course of events and bring effective forest management to one of the world's most important ecosystems? Part of the answer lies far from the halls of political power, in the private sphere of financial capital.

Recently an international coalition of 230 Investors, with USD $16.2 trillion in assets under management, signed a call for corporate action on deforestation. Investors from around the world have recognized the financial and environmental risks associated with deforestation and are using the power inherent in their investments to try to force change. The call to action asks companies to publically map their own operations and supply chains and to follow up with monitoring and verification that deforestation is under control. Many of these investors are also members of existing commodities based investor coalitions, that are already putting pressure on high-risk companies. Producers and Traders of commodities such a Palm Oil, Soy, Timber and Cattle in particular, are under the spotlight.

Not surprisingly, the call to action has made headlines in Brazil and forced the Bolsonaro government into a public defence of its record on de-forestation. What seems clear is that despite the Brazilian government's defiance of international political pressure, they are not likely to risk a widespread private investment drought, caused by environmental concerns. Moving forward, the important development needed now, is for all of these 230 investors to use all of the tools at their disposal to ensure that the call to action has the teeth to affect meaningful change. To this end investors must be very clear in their continuing dialogue with companies, that they risk shareholder activism, public criticism and at worst divestment should they continue to cause rainforest destruction. In this way, the private financial sector will be able to demonstrate just how much can be achieved in ecosystem preservation. All that is required is a common purpose and some serious monetary clout.

Climate Action:

PRI acknowledges Storebrand

In September 2019, PRI recognised Storebrand Asset Management as a leading signatory and included us in the PRI Leaders' Group 2019. The Group highlights PRI signatories that demonstrate responsible investment excellence.

Storebrand Asset Management was one of the founding signatories of the Principles for Responsible Investment (PRI) in 2005. Since then, PRI has grown to be the largest and most geographically diverse organisation for responsible and sustainable investments globally. Each signatory is required to report on their progress annually and these reports are published on the PRI website.

In 2019, PRI launched the PRI Leaders' Group. The signatories selected demonstrated breadth of responsible investment excellence and leadership within a chosen theme. The theme for this year is selection, appointment and monitoring of external fund managers.

While there were eight Nordic asset owners among the total 47 selected globally, Storebrand is the only Norwegian asset owner in the PRI Leaders' Group 2019. Storebrand was specifically recognised for fund selection in Private Equity investments.

Commenting on the news of Storebrand's inclusion in the Leaders' Group, CEO of Storebrand Asset Management Jan Erik Saugestad said: "This is an important recognition of our systematic work on sustainable investments. We will use this role actively to share our experience and to motivate other investors to intensify their efforts in sustainable investment".

Facts about Principles for Responsible Investments (PRI)

- **Established in 2005**
- **Total AUM of members: USD 86.3 trillion (2019)**
- **Total number of signatories: 2372 (2019)**
- **Six principles for responsible investment that members commit to**
- **Annual public reporting and assessment for all members**
- **Multiple collaborative groups for engagement including palm oil and cattle/soy**

> This is an important recognition of our systematic work on sustainable investments. We will use this role actively to share our experience and to motivate other investors to intensify their efforts in sustainable investment.

News to note

Deforestation of the Amazon rainforest

The Amazon rainforest is the largest rainforest in the world, covering an area of 5,500,000 km2. It represents over half of the planet's rainforests, and comprises the largest and most biodiverse tract of tropical rainforest in the world. The majority of the forest is contained within Brazil, with 60 percent, followed by Peru with 13 percent, Colombia with 10 percent, and with minor amounts in Venezuela, Ecuador, Bolivia, Guyana, Suriname and French Guiana. The cattle sector of the Brazilian Amazon, incentivized by the international beef and leather trades, has been responsible for about 80 percent of all deforestation in the region, or about 14 percent of the world's total annual deforestation, making it the world's largest single driver of deforestation. By 1995, 70 percent of formerly forested land in the Amazon, and 91 percent of land deforested since 1970 had been converted to cattle ranching. Much of the remaining deforestation within the Amazon has resulted from farmers clearing land or mechanized cropland producing soy, palm, and other crops. Source: Wikipedia.

Storebrand deforestation policy – a call to eliminate deforestation

Our new policy is a call on companies to eliminate deforestation and we encourage higher standards and collaboration with other investors to help companies to improve. The policy calls on companies to demonstrate a commitment to eliminating deforestation by taking the following steps, amongst others:

- Stronger awareness and governance regarding deforestation risks, including oversight at Board level;
- Publish a commodity-specific deforestation policy with quantifiable, time bound commitments covering the entire supply chain and sourcing geographies;
- Introduce traceability across the entire commodities supply chain; and
- Monitor and verify processes to ensure that suppliers are complying with the company's deforestation policy.

Global electric car fleet may reach 250 million by 2030

According to the International Energy Agency (IEA) more than 2 million electric vehicles hit the road last year, bringing the total to more than 5 million along with 260 million electric two-wheelers and 460,000 electric buses. Looking ahead, the IEA estimates that sales of electric cars could reach 43 million in 2030 bringing the global fleet to 250 million. China will likely remain the largest market. The agency has stressed the importance of public policy, charging infrastructure and a fall in costs for continued EV uptake. Source: International Energy Agency's Global EV Outlook 2019 report.

Storebrand's Sustainability Framework

Spiros Alan Stathacopoulos
Director of International Clients and Distribution

In 1996, Storebrand was the first Norwegian company to establish a sustainable investment department. In the quarter century that followed, Storebrand proceeded to build one of the most experienced ESG analysis departments in the Nordic region. In 2005 we introduced the Storebrand Standard across all asset classes and since 2010 ESG analysis has been steadily integrated into the daily risk management and the company selection processes of Storebrand's fund managers.

Our Sustainable Investments team represents a vast array of experience (from left): Philip Ripman, Tulia Machado Helland, Sunniva Bratt Slette, Matthew Smith, Karin Gjerde-Meyer, Emine Isciel and Andreas Bjørbak Alnæs.

Storebrand has utilized three main approaches within sustainable investments:

A. Risk reduction through exclusions
B. Picking the best performers through a sustainability rating
C. Exerting influence through active ownership

In recent years there has been a huge debate regarding exclusions, with many prominent investment institutions advocating a focus on active ownership as the world tries to achieve the goals set out in the 2015 Paris Agreement. Our experience shows that the two methods are complementary.

Dialogue will always be key to good portfolio management. The issues we discuss with companies, whether they relate to governance, social issues or the environment are important in determining if a company's business is sustainable. Research linking strong ESG performance to better returns is growing. A good recent example that has received a lot of industry attention is "From the Stockholder to the Stakeholder: How Sustainability Can Drive Financial Outperformance" by Oxford University and Arabesque Partners. This study concludes that "prudent sustainability practices have a positive influence on investment performance".

However, if dialogue is unsuccessful and a company continues to break international norms and conventions, there has to be a consequence. Both in the Nordic markets, where Storebrand has a strong foothold, as well as international markets, where our brand is less known, exclusions (or the threat of) can lead to media attention and public debate, which in turn can generate a rethinking by the companies in question.

No asset manager wants to reduce its investable universe. Exclusions, although they can seem simple on the surface, are quite complex as it involves the assessment of a company's business practices in

> At the Storebrand Group we are dedicated to using our position to influence companies in a direction we believe is sustainable.

an unbiased way. Data providers often have different ways of covering company activities and therefore produce different exclusion lists. This can confuse managers who do not have a considered ”house view” on exclusions. Exclusion resistance from fund managers is often stronger when it comes to passive equities, where excluding companies can lead to tracking error/risk. However, one has to keep the following points in mind:

- Passive equities usually represent the largest allocations in client equity portfolios. This means they can quickly align large portions of client assets to their sustainability requirements, at a low cost.
- Although engagement is key also for passive investments, the threat of exclusions is a much more powerful tool for these types of strategies to bring about change, as the investment sums involved are much larger.
- Exclusions do not have to mean weaker performance. Storebrand has managed passive funds vs MSCI Global (developed) benchmarks for 15 years and our exclusions, applied since 2005, have not cost our clients money. Our global developed index tracking funds have delivered in line with expectations, and their respective benchmarks.

At the Storebrand Group we are dedicated to using our position to influence companies in a direction we believe is sustainable. In some cases, where we suspect violation of our policies, it may be beneficial to follow a company over time in order to apply ”positive pressure” and increase the information available. Likewise, there may also be cases where we see a company is working on corrective action, but such measures have yet to be fully implemented or are not yet verifiable. In such cases, we will place the company on an observation list, associated with specific restrictions, to allow for more time to gather the necessary information and influence company direction. Our observation list is a good example of how active ownership, and the possibility to exclude, can be used together to increase the pressure on a company.

As in most areas of financial decision-making, the issue of whether to exclude or engage boils down to context. We believe it is essential to have in-house ESG competency, both to evaluate the data coming from different ESG providers, and to choose the method that works best for each individual company. In the end the goal is the same. We want to generate strong returns for our clients. Often that can mean applying maximum pressure on portfolio companies to manage sustainability risks well and to take advantage of the opportunities rapid sustainable development represents.

For more information on Storebrand’s exclusion process, visit storebrandfunds.com

Why Invest in Water?

6 CLEAN WATER AND SANITATION

Access to clean water is one of the biggest challenges facing our society today. Flooding, drought, stricter water management laws, increasing water tariffs and angry consumers protesting and boycotting products are all reasons the companies we invest in need to worry about water stewardship.

Water shortage of 40 percent predicted by 2030
Existing water use is already higher than the total renewable supply and the gap between global supply and demand for freshwater is predicted to be 40 percent by 2030. Risk drivers are: changing climate, water pollution and aging infrastructure on the supply side and higher water consumption per capita coupled with population growth on the demand side. For the past seven years, the World Economic Forum has ranked water issues among their top five risks. The many water risks are cause for concern due to their severe impact on human life, peace between nations and the economy as a whole. As an investor, we need to know what risks the companies we invest in face and what they do to mitigate those risks.

Bottom Line impact
Physical, regulatory and reputational water risks can severely affect a company's bottom line. The Kellogg Company, for example, reported to the CDP (formerly Carbon Disclosure Project) that several of its manufacturing facilities in Mexico had experienced an increase in water prices of up to 300 percent in five years. In California, US tech company HP reported that its sites were subject to a mandatory 20 percent reduction in water consumption due to local droughts, and Volkswagen had to close its operations near to the river Rhine in Germany due to flooding from heavy rainfall.

The World Bank newly released a report "Quality Unknown, the invisible water crisis", focusing on water quality

Photo by Tong Zhao on Unsplash

Three relevant water risks for companies and investors:

1. Physical water risk – The threat of too much (floods), too little (droughts) and poor quality (pollution). These can cause production to stop, require costly improvements and increasingly pose regulatory and reputational risks.
2. Regulatory water risk – the threat of unsustainable water management by authorities, unexpected regulatory changes or increased water tariffs. May come as a result of water pollution, scarcity or conflict among users.
3. Reputational water risk – Threats stemming from how the community, employees and other stakeholders perceive a company's impact on local water resources. Mismanagement can lead to negative media coverage, decreased consumer loyalty and threaten a company's social license to operate.

> An estimated 80 percent of all wastewater is released into the environment without any prior treatment. Companies contributing to pollution, through their products or manufacturing processes are at risk of negative reactions from stake-holders.
>
> Karin Gjerde Meyer
> Senior Sustainability Analyst

challenges. This water risk topic is much less debated than droughts and floods but should be given urgent attention. An estimated 80 percent of all waste-water is released into the environment without any prior treatment, and the World Bank warns that water pollution is negatively affecting the world's economic growth, increasing poverty and jeopardizing food production.[1] Rich and poor countries alike suffer from high levels of water pollution and new pollutants including nutrients, plastics and pharmaceuticals present significant challenges. Already more than two billion people lack clean on-demand drinking water. Companies contributing to pollution, through their products or manufacturing processes are at risk of negative reactions from stakeholders.

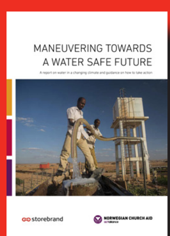
Risk Assessment

Storebrand's ESG risk assessment of companies include the following indicators: Physical Climate Risk Management, Water Risk Management, Water Management Programmes and Water Intensity. Decreasing the amount of water usage during the production process should be an important focus for water-intensive companies. Industries such as textiles, food and beverage, paper and forestry, automo-biles and mining are heavily reliant on water. If dependency on water is not met with the proper responses to ensu-re accessibility, the company's profit is at risk. As an investor, we depend on in-formation. Reporting on water metrics, even as basic as water intensity, is still not good enough. A survey by CDP, AP7 and Sustainalytics looking into the food and beverage, clothing and mining sectors shows that water disclosure remains limited. In addition, corporate water management does not appear to have improved over the last couple of years. Efforts on water intensity have taken a clear turn for the worse, with notably deteriorating levels of disclosure, performance or both. 75 percent of the companies in their study do not disclose information about water intensity or have consistently increased their water use intensity over the last three years.[2] We appeal to all companies to improve their disclosure on water-related metrics, and set clear improvement goals.

Market Opportunities

Global population growth, aging infra-structure, increased water pollution, climate change and over-exploitation of resources are not just risk factors. They also provide market opportun-ities for companies that produce products and services that help other businesses to reduce water use and secure a stable supply. New technologies and products rely on innovation and development, and companies that are first movers or well-positioned in the delivery of key products and solutions could experience significant growth. In total, market opportunities related to the water sector are expected to reach USD 1 trillion by 2025.[3] Companies that are quick to respond are more likely to gain competitive advantages and achieve commercial success.

Agriculture is by far the biggest user of the world's freshwater resources, as it accounts for 70 percent of all freshwater consumption. Photo by Markus Spiske on Unsplash.



Want to learn more about water risks and opportunities?
Download the report "Maneuvering towards a water safe future", published by Storebrand and Norwegian Church Aid in 2018 at **storebrandfunds.com**.

[1] *"Quality Unknown, the invisible water crisis" by the World Bank*
[2] *"Water Management and Stewardship: Benchmarking corporate practices" by Sustainalytics, AP7 and CDP*
[3] *"Water: the market of the future" by RobecoSAM*

Water Solutions:

Xylem Inc

Sunniva Bratt Slette
Sustainability Analyst

Since the first aqueducts were built almost 2,500 years ago in Rome[1], innovative solutions have been created to provide access to clean water. With increasing pressure on water resources, the focus going forward is on water preservation and circular water use. Storebrand seeks to increase investments in companies that provide products and services that respond to the challenge.

About Xylem

Xylem is a leading global water technology provider that makes smart solutions to meet worldwide needs for energy-efficient treatment of water and wastewater. From advanced filtration to chemical-free disinfection, the technology enables optimization of water management. Xylem products are distributed in 400 locations across more than 150 countries,. From collection and distribution to water reuse and return to nature, Xylem's efficient water technologies and industrial pumps use less energy and reduce life-cycle costs. Xylem won the Global Water Technology Award in 2018 from Global Water Intelligence (GWI) and was included in Fortune's 2019 "Change the World" list which ranks 50 companies that have made a significant social impact through their core business strategy.
Source: https://www.xylem.com/en-us/

Water Solutions

Growth opportunities in water-related markets pave the way for companies that sell disruptive technologies and new water solutions. Xylem is a company that has built its business around solving the major water challenges worldwide. Today, Xylem provides safe water and sanitation solutions to more than 3.5 million people globally.

As a response to physical climate change, Xylem has provided clean water infrastructure during more than 40 water-related disasters. Given the increasing amount of extreme precipitation in a short period of time, smart wastewater treatment is vital to prevent surface water from entering local waterways. Xylem contributes to counteracting flash floods and aims to prevent over 7 billion cubic meters, equivalent to 2.8 million Olympic swimming pools,[2] of polluted water from flooding communities annually. This improves climate resilience in cities and communities.

Xylem also addresses climate change mitigation through its goal to save more than 16.5 billion cubic meters (or 6.6 million Olympic swimming pools) of water by 2025 through technologies that avert water loss and enable water reuse[3]. Saved water reduces energy consumption that would otherwise be spent on water treatment and pumping.

Investment Portfolios

Storebrand's Solutions Whitelist keeps track of investable solution companies. Xylem is on the Solutions Whitelist based on its water purification systems and holistic approach to solving major water-related challenges. Its techno-logy contributes positively to several

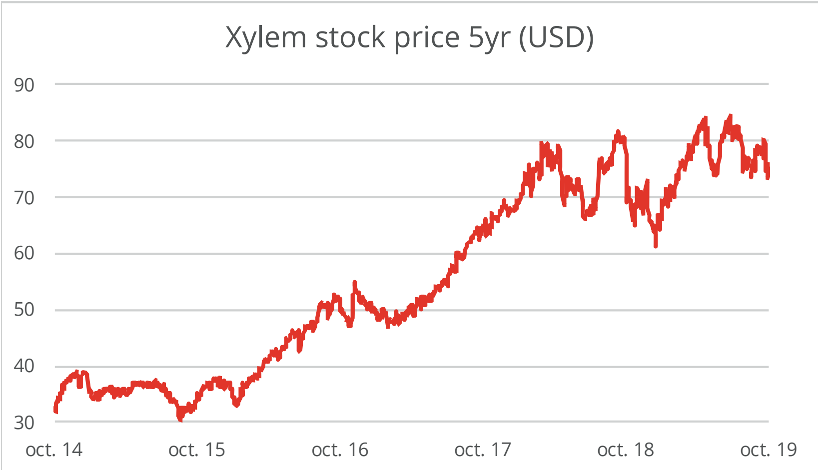
Photo by Kobo Agency on Unsplash

[1] *Ancient History Encyclopedia, https://www.ancient.eu/aqueduct/*
[2] *The Physics Factbook, https://hypertextbook.com/facts/2005/JeffreyGilbert.shtml, volume 2 500 000 litres*
[3] *Xylem, https://www.xylem.com/en-uk/sustainability/#strategy*

> Xylem is a company that has built its business around solving the major water challenges worldwide. Today, Xylem provides safe water and sanitation solutions to more than 3.5 million people globally.

UN Sustainable Development Goals (SDGs), saves water, energy and enables climate adaptation and mitigation. Furthermore, it provides access to clean water and sanitation for at least 20 million people in emerging markets, which helps lift people out of poverty.

Xylem has been an investee company in several Storebrand and SPP portfolios since the Solutions Whitelist was established in 2016. The investment has provided positive returns. As the graph shows, the company share price rose almost 50 percent over the past three years (as of October 2019 in USD).



Xylem is an example of a solution company that has had great success in recent years, which is also reflected in the share price. Storebrand-managed funds have held shares in the company since 2016.

Solution Company Analysis

A "Solution company" is a term used by Storebrand to describe a company with a business model that contributes to achieving the SDGs through its products and services, without causing significant harm. Solution company investments are one of several ways to help shift capital towards alignment with the Paris Agreement, in particular paragraph 2.1.c): "Making finance flows consistent with a pathway towards low greenhouse gas emissions and climate-resilient development". The Storebrand Global Solutions fund and Storebrand Plus funds have been at the forefront of solution company analysis and investments.

The global equity investment team at Storebrand Asset Management have optimized several index-near funds to have higher solution company exposure. The Storebrand Plus Funds have a climate-aware strategy, which includes both divesting from emissions intensive companies and investing more in those that provide solutions for a sustainable future.

Historical returns provide no guarantee of future returns. Future returns depend on market development, managerial skill, fund risk and costs. The return may be negative as a result of capital losses.

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