

May 2020

Sustainable Investment Approach for the Emerging Market Debt SRI Fund

Approach applies to

- Standard Life Investments Global SICAV II Emerging Market Debt Sustainable and Responsible Investment Fund

Aberdeen Standard Investments recognises that the world faces a number of significant environmental and social challenges. Clients may wish to explicitly reduce exposure:

- to the long-term risks associated with ESG factors; and
- to countries which fail to meet recognised sustainability standards.

At the same time, they may wish to seek improvement in business practices through targeted engagement. For these clients, we provide a Fund which falls under our Sustainable and Responsible Investor approach.

Environmental, Social, Governance and Political Factors

As part of the research on this fund, we examine a number of environmental, social, governance and political (ESGP) factors within our research. These are enablers of economic development and elements of a country's willingness and ability to repay its debt which are core parts of the investment process. Institutional weaknesses and social issues can amplify macroeconomic fragilities and act as either catalysts or impediments to economic development. Socio-economic factors are often intertwined and mutually reinforcing. Poor education and health systems can increase inequality and hamper economic growth, which in time can threaten political stability. An unwillingness to, or difficulty, in addressing environmental and social challenges can constitute a major impediment to long-term growth.

By contrast, countries with good ESGP performance should be more resilient to exogenous shocks, such as natural disasters, financial crises or geopolitical instability. Our ESGP framework rates countries on 18 indicators across the four pillars – environment, social, governance and political. The ESGP scores provide useful information in identifying long-term factors and tendencies that might not be fully factored into sovereign bond spreads.

Environmental, Social, Governance and Political (ESGP) filter

The ESGP filtering stage of our EMD SRI strategy relies on excluding from the investment universe a subset of countries falling below a threshold for a number of indicators that are part of our ESGP framework. The exclusion criteria focus on the indicators under the Governance and Political pillars. This method is preferred to a potentially broader approach based on the overall ESGP score as the latter would tend to unfairly exclude the poorest countries that have low Social scores and/or low Environmental scores due to industrialisation or geographic vulnerability to disasters. We however have some leeway to qualitatively exclude issuers which do not meet certain Environmental or Social standards.

Our solution builds successive filters that countries would need to go through in order to be included in the investable universe whilst also incorporating a qualitative assessment in our "Direction of Travel" analysis. The rationale for using exclusive filters is to avoid including countries that score very poorly on one important factor, for example corruption, but where the average score might be pulled up by other indicators. Concentrating on the indicators under the Governance and Political pillars, the filters are applied in the manner illustrated in the chart below:

Governance and Political Filter Example



Source: Aberdeen Standard Investments. For illustrative purposes only.

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Exclusions

The process results in the exclusion of a number of countries from the investment universe. In addition, countries that should have been filtered out due to a poor showing on one or several of the indicators but were exempted thanks to a positive Direction of Travel are instead recorded on a Watch List.

Watch lists and engagement

The Watch List also includes a number of countries that would be excluded if a higher threshold for exclusion were used (20%) and the process rerun. We commit to engage with countries excluded from the investment universe, as well as those on the Watch List, to communicate our concerns on specific issues. Engagement with sovereign issuers also helps us understand plans to address those issues, which is accounted for in our Direction of Travel assessment. Through regular road shows or meetings with senior government officials across those countries, the team is often able to gather unique insights into the ability and willingness of such Governments to tackle key ESGP issues.

Framework and process

The framework is updated twice per year, which could lead to some changes in the group of countries being excluded. If a country is removed from the exclusion list, it is transferred to the Watch List in order to make sure that the improvement is sustained. Our assessment of Direction of Travel should help identify those countries on the Watch List that are at risk of falling back and of being excluded, which should avoid the portfolio being forced to sell positions after updates to the framework.

Any changes to our ESGP framework or the exclusion list would require sign-off from our Head of ESG Fixed Income and the central ESG team. All prohibited issuers are thereafter communicated to our Investment Control team to ensure they are appropriately identified and removed from the investment perimeter of the EMD SRI strategy.

Our responsible investing capabilities

As a leading global asset manager, we believe that investing responsibly can help generate long-term value for our clients. We offer an extensive and growing range of investment solutions, as well as the very highest levels of service and support.

When investing our clients' capital, environmental, social and governance (ESG) considerations are an integral part of our decision-making. By understanding how ESG factors affect our investments, we believe we can generate better outcomes for our clients, society and the wider world.

To help us achieve this, our dedicated, 20-strong ESG Investment team works closely with colleagues across all asset classes to support this work. A further 30 dedicated ESG asset-class analysts provide an additional layer of expertise.

Important Information

Investment involves risk. The value of investments, and the income from them, can go down as well as up and an investor may get back less than the amount invested.

The information herein should not be considered an offer, investment recommendation, or solicitation to deal in any financial instruments or engage in any investment service or activity. The information is provided on a general basis for information purposes only, and is not to be relied on as advice, as it does not take into account the investment objectives, financial situation or particular needs of any specific investor.

Please consider these risk factors:

- Investing in China A shares involves special considerations and risks, including without limitation greater price volatility, less developed regulatory and legal framework, exchange rate risk/controls, settlement, tax, quota, liquidity and regulatory risks.
- The use of derivatives carries the risk of reduced liquidity, substantial loss and increased volatility in adverse market conditions, such as a failure amongst market participants. The use of derivatives may result in the fund being leveraged (where market exposure and thus the potential for loss by the fund exceeds the amount it has invested) and in these market conditions the effect of leverage will be to magnify losses.
- The fund invests in emerging market equities and / or bonds. Investing in emerging markets involves a greater risk of loss than investing in more developed markets due to, among other factors, greater political, tax, economic, foreign exchange, liquidity and regulatory risks.
- The fund invests in equity and equity related securities. These are sensitive to variations in the stock markets which can be volatile and change substantially in short periods of time.
- The fund may invest in companies with Variable Interest Entity (VIE) structures in order to gain exposure to industries with foreign ownership restrictions. There is a risk that investments in these structures may be adversely affected by changes in the legal and regulatory framework.

For professional investors (in Switzerland qualified investors) only – not for use by retail investors.

Standard Life Investments Global SICAV I is an umbrella type investment company with variable capital registered in Luxembourg (no.B 204.798) at 2-4, rue Eugène Ruppert, L-2453 Luxembourg, Grand Duchy of Luxembourg.

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