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June 2020

Sustainable and Responsible Investment (SRI) Corporate Bond Approach

Aberdeen Standard Investments' SRI Credit strategies seek to deliver long-term performance by allocating capital to companies which demonstrate strong management of their environmental, social and governance (ESG) risks and opportunities.

Their goal is to make a positive difference – for our clients, society and the wider world. It's about investing in companies doing the right things to create portfolios that will help our clients achieve their long-term financial goals.

Our SRI credit portfolios are underpinned by our well established active management approach of security selection tailored to the overall environment, which combines fundamental and ESG considerations into our individual name, sector and top down portfolio construction decisions. An assessment of a company's sustainability is supported by a deeply embedded ESG framework utilising on-desk credit and integrated central ESG resources.

Our SRI credit strategies will:

- Exclude companies identified as not having sustainable business practices. This is achieved through a set of 'Binary' exclusions, which identify controversial business activities and 'Active' exclusions which identify companies rated poorly based on their management of ESG risks within their business.
- Engage with companies to gather a forward looking insight into management of ESG risks, opportunities and actively influence the management of these factors in line with best practice standards.
- Target a carbon footprint that is lower than their benchmarks.

The outcome is a portfolio that integrates ESG into every step of the investment decision-making process, thereby avoiding companies with weak ESG performance or exposure to controversial activities, in order to generate attractive long-term financial returns in a sustainable way.

Assessment criteria

The investment universe is screened to target sustainable business practices. This is achieved by applying exclusionary Binary and Active ESG criteria.

Binary exclusion

Screening companies based on controversial business activities. These are defined as companies that:

- Have failed to uphold one or more principles of the **UN Global Compact**[1]
- Are involved in **Controversial Weapons** (any tie)
- Are involved in **Conventional Weapons** (revenue of 10% or more)
- Are a producer of **Tobacco** (revenue of 10% or more)
- Are involved in **Thermal Coal Extraction** (revenue of 5% or more)
- Are involved in **Unconventional Oil and Gas** (revenue of 10% or more)

[1] The UN's Global Compact is the world's largest corporate sustainability initiative. It is a call to companies to align strategies and operations with universal principles on human rights, labour, environment and anti-corruption, and take actions that advance societal goals.

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Active exclusion

Excluding companies rated poorly - based on their management of ESG risks within their business. This is drawn from the insights of our credit analysts and central ESG investment team. In this regard, there are a number of inputs available to screen the investment universe:

ESG House Score

Our SRI credit strategies use our proprietary ESG House Score, developed by our central ESG investment team, to identify companies with potentially high or poorly managed ESG risks. The score is calculated by combining a variety of data inputs within a proprietary framework in which different ESG factors are weighted according to how material they are for each sector and region. This allows us to see how companies rank in a global context. Our SRI Credit strategies exclude companies with the highest ESG risks, as identified by the ESG House Score, in sectors identified as medium or high risk by our central ESG investment team.

Risk sector classification

Sectors are classified using industry data and internal analysis of quantified risks relating to climate change, human rights, environment, labour issues and business ethics. The overall rating is determined by the central ESG Investment team and in consultation with relevant sector analysts in credit and equity teams. The objective is to assign a risk classification for each sector: high, medium or low.

High-Risk Sector

Examples
- Construction materials
- Mining
- Oil and gas
- Gas and electricity utilities
- Autos

Medium-Risk Sector

Examples
- Real Estate
- Food distributors
- Healthcare services
- Industrial machinery
- Banks

Low-Risk Sector

Examples
- IT consulting
- Advertising
- Leisure products
- Renewable electricity

Credit ESG Risk Rating

Owned and defined by credit analysts. This indicator is used to assess how impactful we believe ESG risks are likely to be to the CREDIT QUALITY of the issuer now and in the future. Key drivers of an analyst's assessment include:

- Inherent ESG risks of the sector of operation
- Materiality of these risks
- Judgement on the timeframe over which ESG risks may have an impact
- How well management controls and plans around these risks and treats their various stakeholders

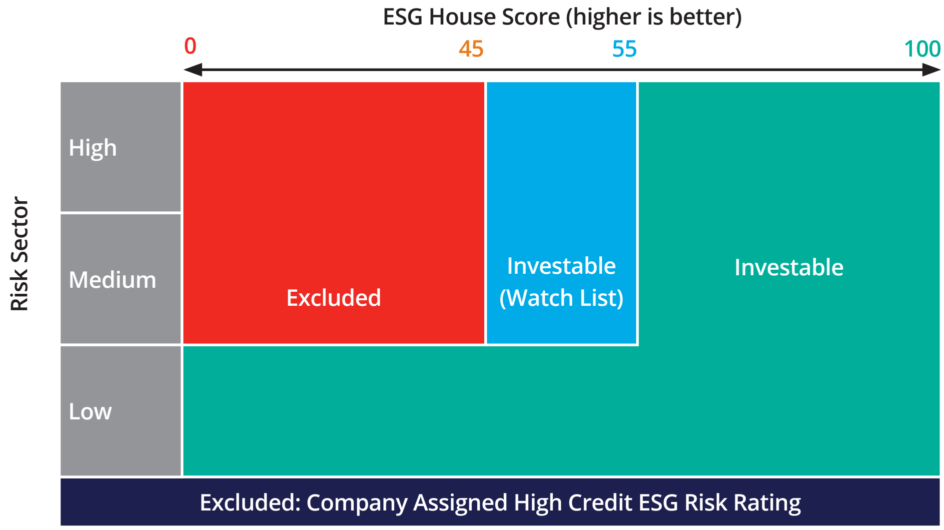
Companies are rated Low, Medium or High. A Credit ESG Risk Rating of 'High' indicates that there are potentially significant risks whose impact and timeliness could negatively impact the credit profile. Combining these factors, the active exclusions are then applied.

Universe filtered through robust proprietary ESG House Score and Credit ESG Risk Rating

Key factors

- Companies receive an ESG House score between 0 and 100 (higher is better)
- Sectors classified by risk: Low Medium, High
- Companies receive a Credit ESG Risk Rating: Low, Medium, High

Exclusions
- Companies with a rating of 45 and less and operate in High or Medium risk sectors
- Companies assigned a High Credit ESG Risk rating (regardless of sector)



[2] Scope 1 emissions are direct emissions from owned or controlled sources. Scope 2 emissions are indirect emissions from the generation of purchased energy.

Engagement

Engagement with company management teams is a key part of our research and investment process and a key facet of our overall stewardship programme. It provides us with a more holistic view of companies, including current and future ESG risks that need to be managed, as well as potential beneficial opportunities. This stage also provides the opportunity for us to discuss any areas of concern, share best practice knowledge and drive positive changes. The priorities for engagement are established based on:

- Materiality of holdings (i.e. size)
- ESG issues that are considered a key driver of the credit profile of a company.
- An ASI Watch List which includes:
  - Companies with ESG House Scores between between **45 and 55** and operating in 'High' and 'Medium' risk sectors.
  - Negative ESG house score rating movements.
  - Hot topics – reactive engagements relating to any negative news events.

Carbon Footprint

When building the portfolio we will target a lower carbon footprint compared to the benchmark. This is measured by having a lower combined 'scope 1' + 'scope 2' emissions[2].

Summary of our Sustainable and Responsible Investment approach:

- **ESG research integration** – ESG credit assessment supported by analyst ESG tool kit.
- **Company engagement** – cross-asset class engagement to gather forward looking insights and drive positive change.s
- **ESG exclusion criteria** – companies identified as having the poorest management of ESG risks are excluded based on binary and active ESG criteria.
- **Portfolio construction** – targeting a lower carbon footprint compared to the benchmark and factoring thematic ESG themes into portfolio positioning.

Our capabilities

We have a market-leading, 50-strong Responsible Investment team. This highly experienced and well-resourced group undertakes sector and thematic research, engagement and voting activity. ESG specialists are also embedded in each team.
We believe our success lies in our ability to connect across teams, geographies, public and private markets to generate superior investment solutions for our clients.

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Important Information

Past performance is not a guide to future results. The value of investments, and the income from them, can go down as well as up and clients may get back less than the amount invested.

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