arabesque

Our Approach to Sustainable Investing

For professional investors only

Content:

Purpose and Scope

Sustainability, according to the Brundtland definition, entails meeting present needs without compromising the ability of future generations to meet their own needs. It encompasses a forward-thinking approach that seeks to harmonize economic, social, and environmental objectives for a ensuring a lasting and harmonious coexistence between humanity and the environment.

We firmly believe that as a financial institution, we play part in tackling the critical social, economic, and environmental challenges that our societies are currently confronting. In this rapidly evolving world, sustainability is at the core of our values and practices. By proactively integrating sustainability considerations into our investment decisions, we strive for long-term value creation for both investors and society as a whole.

Our Approach to Sustainable Investing is intended to provide a comprehensive framework that describes how Arabesque Asset Management incorporates sustainability considerations across our investment strategies and solutions. Our approach to sustainable investing, and the practices described herein, equip us to design and provide products that reflect our investment philosophy and enable clients to align their investment objectives with their core values.

About Arabesque

The Arabesque Group established out of a desire to tackle key challenges faced by the asset management industry. It was founded in 2013 as a management buy-out from Barclays, bringing together leaders in finance, mathematics, and sustainability. Their collaborative efforts aimed to develop the next generation of sustainable data and technology for the industry.

Since its inception, Arabesque has grown organically and established the following businesses:

- ESG Book: a dedicated data business, focused on providing the market with corporate sustainability data.
- Arabesque AI: a dedicated technology business, focused on providing customised and impact-driven portfolios at scale.
- Arabesque Asset Management harnesses the technological and ESG expertise developed within the Arabesque Group to provide investment products and services designed to meet the long-term financial objectives of investors.

The name 'Arabesque' represents geometric colours and patterns drawn with mathematical equations. It reflects what we believe is a pioneering approach to finance — leveraging technology and ESG information with our quantitative investment strategies.

Investment Philosophy

Our investment philosophy focuses around recognizing investors' growing awareness of externalities associated with their investee companies (i.e., ESG risk and opportunities), and their desire to align their values with their investments. The emergence of innovative technologies such as Artificial Intelligence, Machine Learning, and Natural Language Processing allows us to improve the effectiveness of our investment strategies by examining vast datasets and reducing human biases. As such Arabesque's investment philosophy combines the integration of ESG considerations and cutting-edge technologies, driving a systematic investment process and personalized customization.

Since our foundation in 2012, sustainability factors are embedded within every investment strategy to enhance our information environment, to mitigate risks and allocate capital to companies that are fit for future. Consequently, 100% of Arabesque's strategies integrate sustainability considerations. The specific sustainability methodology utilized within our product range is dependent upon multiple factors, including the objectives of a specific investment strategy, portfolio construction, and client preferences.

Oversight

At Arabesque, sustainability lies at the very core of our firm's foundation, driving us to integrate ESG considerations across all levels of the organization and within every product we offer. We firmly believe that a robust Board of Directors plays a pivotal role in setting the right tone at the top, reinforcing our commitment to responsible practices and guiding our strategic sustainability initiatives.

Arabesque benefits from a Board comprised of global leaders in the areas of corporate responsibility, sustainable investing, environmental activism, human rights, and gender equality. The Board is chaired by Georg Kell, the founding Executive Director of the UN Global Compact, who plays an active role in globally promoting sustainable finance.

The overall responsibility for implementing our ESG approaches in investment strategies lies with Arabesque's Investment Committee. The Investment Committee's responsibilities with regards to sustainable investment include, but are not limited to:

- Monitoring the integration of ESG across all investment strategies and products
- Authorizing the development and enhancement of ESG research and methodologies in investment strategies and products
- Overseeing external reporting, such as the UN PRI, as well as proxy voting and engagement activities

Research and data

ESG Book, formerly Arabesque S-Ray®, was designed as a proprietary tool to analyze ESG data as a part of Arabesque Asset Management's investment strategies. ESG Book spun out from Arabesque Group as a specialized data and technology provider in the field of sustainability. The asset management arm integrates ESG Book data in the investment process until today.

ESG Book combines cutting edge technology and proprietary research to produce a series of sustainability metrics and analytics. Launched in 2018, the company offers a range of ESG and climate solutions that are used by many of the world's leading investors and companies. Covering over 50,000 companies, ESG Book's product offering includes ESG raw data, company-level and portfolio-level scores and ratings, analytics tools, and a SaaS data management and disclosure platform. ESG Book's solutions cover the full spectrum of sustainable investing including ESG, climate, net-zero, regulatory, and impact products.

The metrics obtained from ESG Book are strategically employed across all our strategies. We firmly believe in the value of incorporating material environmental, social, and governance information, commonly referred to as extra-financial factors, into our investment decisions. By doing so, we aim to minimize risk exposure and enhance returns for our clients. The comprehensive insights provided by ESG Book enable us to evaluate companies' adherence to responsible practices, identify potential risks related to environmental impact and social issues, and assess the effectiveness of corporate governance structures. This holistic approach not only aligns with our commitment to sustainable investing but also reinforces our belief in the ability of ESG integration to drive long-term value creation in portfolios.

Arabesque investment strategies integrate the following ESG and sustainability metrics provided by ESG Book:

- ESG Score: This score is based on the principal of financial materiality, using data that significantly helps explain company's future risk-adjusted financial performance.
- United Nations Global Compact Score: This score assesses a company's performance against the four principles of the United Nations Global Compact, human rights, labour rights, environment, and anti-corruption.
- Preference Filter: This filter is based on revenue segmentation data and provides a flag for a set of business involvements deemed as controversial. Flagged industries include alcohol,arms, fossil fuel, gambling, or tobacco.
- Temperature Score: This score assesses the extent to which corporations across the world are contributing to the rise in global temperature based on their current emissions. It assigns companies a score in degrees Celsius based on 2030- and 2050-time frames.

Integration of Sustainability Considerations in Investments

All companies in Arabesque investment strategies must meet the pre-determined sustainability criteria to be considered for investment portfolios. These criteria are based on sets of screens and analysis using ESG Book data and tools.

We apply these tools throughout our investment strategies in the following approaches:

Screening

All our investment strategies have a sustainable universe, which is created by leveraging ESG Book data, analysing the different aspects of sustainability. While maintaining an ESG-agnostic stance, we embrace fundamental guidelines to ensure responsible investment practices. By grounding our strategies in these basic principles, we ensure a consistent and well-informed approach to sustainable investing. We believe this screening approach can be used to reduce portfolio risks, supports performance and promote sustainable practices.

- Normative Screen: By excluding companies that violate the norms-based principles of the UN Global Compact, we can minimize reputational risks. This approach ensures that our investments align with globally accepted ethical standards and socially responsible principles. By actively supporting sustainable and responsible businesses, we demonstrate our commitment to widely caring about sustainability and upholding the values of the UN Global Compact.
- ESG Screen: By identifying firms with reduced ESG risk and a potential to perform well over the medium- to long-term. Performance can be generated through growth related to sustainable products, cost savings with regards to sustainability-related innovation, and reduced operational, regulatory and reputational risks.
- Preference Screen: By employing threshold-based exclusion of companies based on their corporate activities, investors can align their investment strategies with their values. If a company's revenue is found to be 5% or more affiliated with any selected filter (e.g., tobacco), it can be removed from the client's investment universe.
- Temperature Score Screen: By screening of companies in high GHG emitting sectors linked to fossil fuels unless the companies are aligned with the emission reduction targets set out by Paris Agreement.

Faith-Based Screening

Faith-based investment solutions leverage our sustainability screening capabilities by complying with standards, such as Catholic and Shariah-compliance standards. Arabesque's Shariah-compliant investment products comply with the AAOIFI Shariah Standard No 21 and Malaysia Securities Commission guidelines. Furthermore, in line with Shariah requirements, we do not invest in any preference shares, warrants, derivatives, or interest-based investments. In screening a Catholic-compliant portfolio, ESG Book uses the United States Conference of Catholic Bishops' (USCCB)

2003 Investment Policies as its rulebook. The rulebook covers topics such as protection of human life, promoting human dignity, or protecting the environment, amongst others.

ESG Integration

ESG integration involves explicitly and systematically integrating ESG related considerations in our investment analysis and portfolio construction. Our material ESG Scores are assessed alongside other traditional financial factors when forming an investment decision. While our screening approach is targeted at the investment universe phase, Arabesque's ESG integration approach goes further in the way we select securities and weight them during portfolio optimization. As a result, investors' capital allocation is focused towards companies that explicitly and consistently perform well both in financial and extra-financial terms.

In addition to ESG screening, applying ESG integration within selected investment solutions also aims to:

- Explicitly weight ESG risks and opportunities, alongside traditional financial analysis in our target functions
- Strengthen the exposure of companies that perform best on ESG-related characteristics.

Thematic Investments

Embracing innovation in sustainable investing, our approach extends to thematic strategies. These strategies target specific global challenges, allowing investors to align their portfolios with themes such as renewable energy, clean technology, and healthcare advancements, driving both financial growth and positive impact.

At Arabesque, we see climate change as a key theme with far-reaching implications for societies, economies and markets across sectors. The transition to a low-carbon economy presents both risks and opportunities, shaping the investment landscape and underscoring the value of sustainable, future-focused portfolios. As such, Arabesque launched a climate pathway strategy. In addition to performance objectives, the strategy aims to:

1. Align with the goals set out by the 2015 Paris Agreement: by investing into companies whose behaviour and operations would keep global temperature rise this century well below 2 degrees Celsius above pre-industrial levels and pursue efforts to limit the temperature increase even further 1.5 degrees Celsius.
2. Mitigate transition risks and report in line with TCFD metrics: by investing in companies that either a) provide products or services that aid the low-carbon transition or b) are environmental leaders in their respective industry.

The strategy combines specific E metrics, with Temperature score and UN Global compact screen to create a portfolio of attractive environmental companies (Solution Providers, Environmental Leaders, Strong Paris-Aligned companies), while distributing risk equally amongst all holdings.

Thematic – Bespoke

Arabesque is uniquely positioned to create tailor-made investment thematic strategies utilizing technology build by its sister company Arabesque AI. Arabesque AI, spun out from the quantitative research team, created Aether a technology platform empowers portfolio managers to construct hyper- customised portfolios at speed – integrating any number of financial and non-financial constraints and preferences.

Active Ownership

Arabesque views active ownership as an integral part of its business and fiduciary duty as a responsible investor. As such, we engage on and promote ESG matters within the wider market and across companies we invest in. Being a Principles for Responsible Investment (PRI) signatory and advocate, our approach to stewardship is in line with the second principle stating that "*We will be active owners and incorporate ESG issues into our ownership policies and practice.*"

As a quantitative asset manager, we leverage advancements in technology for attaining increased transparency into corporate behaviour and use this data to inform our investment decisions. With a foundation in technology and sustainability, these two pillars also inform our engagement activities.

We seek to engage with corporations on issues that are aligned with the company's critical concerns around sustainable investing. These are the guiding principles:

1. Information Transparency: Businesses should support increasing information transparency and enhanced disclosures. We believe this leads to improved data quality, data availability, and transparency.
2. Sound Governance: Businesses should have a sound governance and capital structures, with accountability at the top, with strong risk management and anti-corruption
3. Social Responsibility: Businesses should uphold human and labour rights, promoting sound employee rights, diversity, customer care and eliminating discrimination, child or force labour, or any harmful practices.
4. Environmental Matters: Businesses should support a precautionary approach to environmental challenges and undertake initiatives to greater responsibility around climate change, biodiversity, energy efficiency, water efficiency, amongst others

The above principles are being applied equally, meaning neither is prioritized in our engagement activities.

Proxy Voting

We believe that companies with strong governance practices, who consider stakeholders interests are better to positioned to perform well in the long run. Through proxy voting, shareholders can influence a company's corporate governance practices, management, and operations. As part of the transition to a more resilient economy, we see proxy voting as vital shareholder responsibility.

Arabesque has partnered with Glass Lewis to carry out proxy voting activities. We follow the Glass Lewis ESG Thematic Policy. Voting in line with this policy and maintaining key stances on best practices upholds our belief that material ESG factors can affect companies' risk profiles and long-term financial performance.

We utilize the Glass Lewis platform Viewpoint to produce annual reports on the fund's voting, which are available on our website.

Direct Engagement

By engaging in direct dialogue, we are able to voice our concerns, provide guidance and collaborate with companies towards achieving long-term sustainable outcomes.

Arabesque has engaged in a dialogue by approaching companies directly and has launched an engagement campaign. However, direct engagement is not Arabesque's primary engagement type due to the quantitative nature of the investment process.

Collaborative Action

Given the rules-based, quantitative investment process, we acknowledge the limited holding period for securities in our funds' respective portfolios. As such, we focus on collaborative engagement with other investors and asset owners because we believe that working with like-minded investors on engagement matters is likely to enhance its outcomes. Indeed, due to the collective reputation, size and weight of participating investors, collaboration will be more likely to influence change. This approach is in line with the fifth principle of PRI, which encourages signatories to work together collaboratively to enhance their effectiveness in implementing the principles.

In terms of collaborative actions, Arabesque:

- Leverages relationships with non-profit(s) organizations to co-sign engagement efforts and opportunities with other asset managers (e.g., ShareAction)
- Identifies pooled engagement opportunities via collaboration platforms, email or other channels

Since 2014, Arabesque subscribes to the Principles for Responsible Investment, the world's leading platform for sustainable investment. Guided by these principles, Arabesque reports annually on its progress of incorporating PRI within its investment process.

Arabesque is a proud affiliate and partner of the following organizations and thought leaders:

PRI Principles for Responsible Investment

United Nations Global Compact

UKSIF
UK Sustainable Investment and Finance Association

Climate Action 100+

ShareAction»

Escalation and Conflict of Interest

As the majority of our engagement is conducted via collaborative efforts, where we do not have a direct ownership in the companies, we do not have a formal escalation procedure in place. If the opportunity arose, we would follow the escalation process of a given engagement, having a dialogue with the campaign lead about the next steps and taking part on follow-up calls with the issuers. A further challenge regarding escalation, is presented by our systematic investment process, resulting in holding periods of less than a year on average. This limited holding period restricts our collaboration in filing shareholder resolutions as we may not hold the security at the time of the Annual General Meeting. However, if there was a collaborative engagement campaign prior to the resolution, we would participate.

Similarly, given the collaborative nature of our engagement activates, the risk of conflict of interest related to stewardship is considered to be low.

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