Sustainable Asset Management: Key Messages and Recommendations of SFAMA and SSF

16 June 2020

SFAMA Swiss Funds & Asset Management Association

Swiss Sustainable Finance

Contents

A. Introduction

1 Background

1. The financial sector is part of the economic system and acts in the wider context of civil society and the natural environment. The developments in society and the environment (e.g. poverty alleviation, climate change, loss of biodiversity) hence influence the financial sector and its activities, while at the same time the financial sector, through its activities, has an influence on society and the environment (see Appendix 1). The financial industry is expected to play an active role in both integrating environmental, social and governance (ESG) risks into financial decision-making and aiming for a positive contribution towards greater sustainability of the economy, society and the natural environment.

2. Switzerland is one of the largest centres for institutional asset management and is a global leader in wealth management. As a member of the UN, Switzerland has committed itself to implementing the UN 2030 Agenda for Sustainable Development, with the 17 Sustainable Development Goals (SDGs). Switzerland also ratified the Paris Climate Agreement in October 2017. The implementation of sustainability in various sectors, including the financial sector, is an important factor for the achievement of these agreements, but also for international competitiveness.

3. In a globalised economy, the success of corporate strategies is becoming increasingly influenced by ESG factors. Integrating such factors into financial analysis and risk management can lead to higher profitability, lower tail-risk and lower systematic risk. Asset managers have recognised the importance of integrating sustainability factors into the decision-making process. At the same time, the asset management industry is aware of its responsibility in addressing global challenges and contributing to the necessary change. Considering sustainability aspects in the investment process hence offers the opportunity to achieve financial objectives while contributing to achieving broader goals such as the Paris Agreement or the UN Sustainable Development Goals.

4. Against this background, the Swiss Funds & Asset Management Association SFAMA and Swiss Sustainable Finance (SSF) decided to team up to develop high-level key messages (chapter B) as well as detailed recommendations on sustainable asset management (chapter C) that help asset managers aiming to integrate sustainability into their products and services. The key messages reflect the associations' high-level views on Sustainable Finance in the area of Swiss asset management. The recommendations are of a more technical nature. They focus on the investment process and contain more detailed recommendations on the elements an asset manager should consider in order to successfully implement a sustainable investment process.

5. This document is a joint publication of SFAMA and SSF. We hope that it will help further promote sustainable asset management in Switzerland and support the asset management industry in meeting the expectations of the government and relevant stakeholders.

2 Objectives and scope of application

Generally, SFAMA and SSF see a clear need for recommendations for the broad integration of ESG factors into all investment processes. This helps the Swiss asset management sector to remain competitive and adapt its services to changing requirements. The key messages and recommendations are applicable for the Swiss asset management industry[1]. **6.**

Therefore, the objective of this paper is to give an overview about the main beliefs of the Swiss asset management industry and to provide asset managers with an effective guide for the implementation of a sustainable asset management process including governance, risk management, investment policy and strategy. **7.**

The recommendations describe the most important elements that are crucial for the successful implementation of a sustainable asset management process. They provide a general overview of how ESG factors should be implemented into the different elements of an investment process for it to be considered sustainable. **8.**

This paper does not take the form of binding SFAMA Guidelines. The key messages and recommendations are applicable on a voluntary basis and are supposed to educate asset managers intending to strengthen their sustainable investment management with a set of recommendations. They specifically address organisations that are in an early phase of integrating ESG factors into their asset management. **9.**

This paper focuses on the implementation of sustainability factors in the investment process from a financial / economic perspective. The key messages and recommendations do not cover regulatory obligations on a national or international level that asset managers must comply with vis-à-vis their clients and the supervisory authority, or due to product regulations (e.g. FinSA[2] conduct rules, CISA[3] product regulations, other binding obligations / regulations, cross-border services), as this would go beyond the scope of such recommendations. The same applies to the fulfilment of obligations under civil law such as client preferences that the asset manager must comply with (e.g. contract with the client, client instructions). This paper does not contradict these obligations, nor does it discharge the asset managers from these obligations. **10.**

[1] Asset management is the production and management of investment solutions in the form of collective investment schemes or individual, institutional mandates. A key feature of this definition is the clear focus on institutional clients such as pension funds, insurance companies, sovereign wealth funds or corporations. It also includes the management of funds that are pooled in collective investments schemes (CIS), especially investment funds and investment foundations. See p. 5 IFZ/AMP Asset Management Study 2019; https://sfama-cms.cdn.prismic.io/sfama-cms%2Fc02845c9-8c18-4f8c-9e1f-c6e32de7c935_ifz+amp+studie+2019_final_hohe+aufl%C3%B6sung.pdf

[2] Federal Act on Financial Services of 15 June 2018, Classified compilation 950.1.

[3] Federal Act on Collective Investment Schemes of 23 June 2006, Classified compilation 951.31.

B. Key Messages on Sustainable Asset Management

11. The following key messages reflect the views of the Swiss asset management industry, represented by SFAMA and SSF, on the role of Sustainable Finance for the Swiss asset management Industry.

1. Fiduciary Duty

Consistent with the fiduciary duty to clients, superior long-term risk-adjusted returns can be generated by considering sustainability criteria. Sustainability should therefore be at the heart of the investment philosophy.

2. Corporate Sustainability

Asset managers should consider social, economic and environmental impacts in all aspects of their business and anchor their values in a corporate sustainability policy.

3. Comprehensiveness

The Swiss asset management industry is committed to addressing the topic of sustainability in a comprehensive way in its asset management services. In doing so, it aims to integrate sustainability aspects in all elements of the investment process. Furthermore, and as a general rule, the internal sustainability policies should be binding and the relevant processes measurable and transparent.

4. Stewardship

It is good practice to be an active owner and integrate active ownership mechanisms into the asset management process.

5. Transparency

In implementing sustainability criteria, transparency is key, and they should be reported in an explainable, standardised and measurable way.

6. Data Quality

In implementing sustainability criteria, it is crucial to obtain comprehensive data from sources considered reliable and to encourage the continual improvement of data quality.

7. Climate risks

It is essential to assess climate risks along the decision-making process (e.g. investment analysis, investment decisions) and to address them through stewardship (active ownership). Each asset manager is responsible to implement such processes.

8. International Developments

There should be an ongoing commitment to observing international developments on sustainability and aligning business activities with them.

C. Recommendations for Sustainable Asset Management

1.1 General information 12.

A sustainable investment process (used in these recommendations as a synonym for responsible investment and ESG investing) contains similar elements to a normal investment process. The following chart provides an overview of the different elements of a sustainable investment process. The subsequent chapters are essentially organised along this order:

Figure 1: Integration of Sustainability into different elements of the investment process

Source: Swiss Sustainable Finance

1.2 Fiduciary duty

According to the concept of fiduciary duty, an asset manager takes all necessary measures to achieve 13. the best possible risk-adjusted return on investment, taking due care and protection of the client's interests and requests into account[4].

Risk assessment is not limited to traditional risk categories but also covers emerging risks resulting from 14. ESG factors. This means, for example, that factors such as climate change should be integrated into the investment strategy if they could result in material financial risks or are expected to have an impact on performance. This helps the asset manager to avoid risks and identify opportunities linked to sustainability topics that materialise in the medium to long term.

The consideration of such financially relevant sustainability factors is therefore consistent with the asset 15. manager's obligation to achieve the best possible risk-adjusted return on investment, taking due care and protection of the customer's interests into account.

[4] For due care and protection of the client's interests, see Art. 398 para. 2 Federal Act on the Amendment of the Swiss Civil Code (Part Five: Code of Obligations; Classified compilation 210); Art. 51b para. 2, Art. 71 para 1 Swiss Federal Act on Occupational Retirement, Survivors' and Disability Pension Plans (BVG; Classified compilation 831.40), and Art. 50 et seq Ordinance on Occupational Retirement, Survivors' and Disability Pension Plans (BVV 2; Classified compilation 831.441.1).

1.3 Credibility of the sustainable investment process and consistency with the overall policy of asset managers

16. An asset manager integrating ESG factors into the investment process may wish to integrate sustainability into their vision and mission, in order to assure alignment between the overall company strategy and the investment strategy. Integrating sustainability into the overall strategy by actively managing ESG topics that are considered relevant for the whole company (e.g. energy and resource consumption, diversity, good governance) contributes to the overall credibility of the sustainable investment strategy. Furthermore, a company expresses conviction, if the assets under its control (e.g. reserves, pension fund assets) are managed in line with the sustainable investment policy, but always subject to the asset manager's mandate given to him by the asset owner.

1.4 Governance

1.4.1 General information

17. The question of how sustainability factors are incorporated into the organisation's investment management system is essential. Generally, a distinction can be made between human resources with oversight roles and those with implementation roles.

18. Individuals with *oversight roles* are those with management or governance responsibility for ensuring that the organisation implements its policies and achieves its objectives and targets in relation to sustainable investment performance. Assigning oversight to a person, team or committee should not be seen as a way to compartmentalise ESG responsibility. Instead, the purpose is to ensure accountability for embedding ESG considerations within the organisation and investment processes[5].

19. Individuals with *implementation roles* are those charged with implementing specific aspects of the organisation's sustainable investment practices. For example, conducting ESG-related research, incorporating ESG issues into investment strategies, voting on shareholdings, or engaging with companies. Implementation of ESG analysis in investment decision-making does not only apply to dedicated sustainability staff but could be a part of any role or activities[6].

1.4.2 The role of the board and management[7]

20. As this is relevant to the manner in which an asset manager oversees its sustainable investment activities, this should include a description of the following items[8]:

- The board's oversight of ESG risks and opportunities, and
- The management's role in assessing and managing ESG risks and opportunities.

21. In describing the board's oversight of ESG issues, the asset manager should define and implement the following aspects[9]:

- Processes and frequency by which the board and / or board committees (e.g. audit, risk, or other committees) are informed about ESG issues.

[5] PRI Reporting Framework 2019, Strategy and Governance, p. 19.
[6] PRI Reporting Framework 2019, Strategy and Governance, p. 19.
[7] For simplicity, these recommendations use the singular version of these terms. For asset managers with multiple board bodies or management bodies, the comments apply to the board and management body/bodies responsible for this topic.
[8] See also TCFD, Implementing the Recommendations of the Task Force on Climate-related Financial Disclosures, p. 38.
[9] See also TCFD, Implementing the Recommendations of the Task Force on Climate-related Financial Disclosures, p. 38.

- Define the organisation's objectives with regards to ESG and formulate an investment policy that includes its approach with regard to the consideration of ESG risks and opportunities in the investment process.
- How the board monitors and oversees progress against goals and targets for addressing ESG issues.
- The board's risk tolerance and policy for overseeing ESG risks and opportunities as well as the role of management in implementing the decisions made by the board concerning the setting up, maintenance and regular review of the internal control system (ICS), including the related controls for overseeing ESG risks.
- Keep track of international developments in sustainable finance and in alignment with the business model of the asset manager – adapt to these developments where necessary and useful (e.g. EU regulations in case of providing cross-border services).

In describing executive management's role related to assessment and management of ESG issues, the asset manager should address the following items[10]: **22.**

- Assign executive management responsibility for the sustainable investment process (e.g. to a member of the executive management or committee) and define reporting lines.
- Description of the associated organisational structure(s) and required resources.
- Define appropriate tools to monitor ESG issues.

1.4.3 Appropriate training

Once responsibilities are defined, an organisation should make sure relevant employees receive appropriate training to enable them to integrate sustainability factors into the investment process[11]. **23.**

1.5 Investment policy[12]

Generally, the investment policy contains an overall statement describing the approach of an asset manager to achieve its identified mission. It describes the investment strategy, defines the investment objectives and informs about the investment process, as well as applied standards for performance measurement. The investment policy should also cover the approach to sustainable investments or the way ESG factors are integrated into the investment activities[13]. **24.**

Integrating ESG topics into the investment policy demonstrates an asset manager's recognition of the materiality of ESG factors and the commitment to integrate such factors into the investment process in order to come to informed investment decisions. These factors play a central role when it comes to putting a sustainable investment policy into practice. As part of the investment process, it should be ensured that material ESG risks and opportunities form part of the investment analysis and hence could influence the investment decision. This can be done in many different ways as different ESG factors may be relevant, depending on the context. **25.**

The sourcing of reliable and high-quality data is crucial for the successful implementation of ESG factors into an investment process. **26.**

[10] See also TCFD, Implementing the Recommendations of the Task Force on Climate-related Financial Disclosures, p. 38.
[11] SSF provides an overview of different training in the field of sustainable investment. Furthermore, SSF has developed an e-learning course on sustainable investments that is available for free for SSF members. See http://www.sustainablefinance.ch/en/training-_content---1--1081.html.
[12] For simplicity, these recommendations use the singular of this term. In practice, an asset manager may have several policies that take an ESG approach and to which these recommendations may apply.
[13] PRI Reporting Framework 2019, Strategy and Governance, p. 7.

27. An asset manager should define the following:

- Objectives: The asset manager's objectives with regard to the consideration of ESG risks and opportunities and measures taken to achieve these objectives. For example, climate risks being one of the key sustainability topics should be covered by the asset manager's objectives. In order to contribute to achieving the Paris Climate Agreement, the asset manager should assess climate risks along the decision-making process (e.g. investment analysis, investment decisions) and address them through active engagement.
- Data quality and sourcing: The asset manager should define the process to source reliable ESG data and regularly monitor their quality and encourage a continual improvement.
- Responsibilities: Who is formally in charge of applying sustainable investment practices.
- Process: How ESG information is handled (e.g. from where it is obtained), how it is processed, how controversial ESG issues and ESG risks are addressed and handled (e.g. climate relevance in policy).
- External fund managers: How the due diligence process for the ESG approach of external fund managers is designed.
- Reporting: How to ensure regular reporting on sustainable investment activities and where to report on them.
- Monitoring: How is a regular review of the process and its implementation ensured.
- The approach to active ownership:
  - Description of how / if voting rights are exercised (e.g. regular basis or not) and if they are based on a dedicated policy.
  - Description of how / if the asset manager actively engages with companies.

28. The description should form part of the asset manager's investment policy. The investment policy should reflect the investment beliefs and convictions of the organisations.

29. The investment policy or a summary thereof should be published (e.g. via the website).

1.6 Investment strategy

30. The investment strategy is a high-level plan which defines how the investment is performed and embeds comprehensive consideration of all long-term trends affecting the portfolio of the asset manager. Through the integration of material sustainability factors into the investment strategy, an asset manager aims to actively manage and monitor material risks and therewith operate as efficiently as possible for the benefit of his clients and other stakeholders.

31. An asset manager should inform about how it deals with ESG risks and opportunities in its investment process. It informs clients about the factors considered relevant and how they influence respective decision-making. The investment strategy should clarify the company's general approach(es) applied to its different products and services, and also describe the tools and data used in the organisation.

32. Chapter 1.6.2 lists a variety of sustainability approaches currently observed in the industry. The list is not intended to be exhaustive. An asset manager should define different methods or combine aspects from the approaches listed below to an individual approach that fits the objectives of its investment policy.

33. While the investment strategy should be reasonably generic, the individual product presentations should give a more detailed view of the application of ESG in the respective investment process. The asset manager is expected to apply one of the approaches mentioned below, a combination thereof, or a new approach with similar effects. The objectives of the sustainable investment strategy can vary and usually envisage an improved risk / return profile, an alignment to values and norms and / or a positive contribution to the achievement of a sustainable economy.

If an asset manager claims to have a sustainable investment process in place, it should describe which approach or combination of approaches the process is based on (referring to the different forms of sustainable investing described above) and how the respective approaches are implemented. **34.**

The asset manager shall ensure that sufficient internal or external resources are committed to achieve the objectives stated in the investment policy and investment strategy in a meaningful way. An overstatement of measures ("greenwashing") has to be avoided, while clients should be given a fair and realistic picture of the asset manager's chosen approach towards ESG. **35.**

1.6.1 Strategic and tactical asset allocation

Sustainability factors should be integrated into the different levels of strategic and tactical asset allocation. On a strategic level, an asset manager might consider taking material sustainability factors into account when defining its target allocation for the various asset classes (e.g. leave aside certain sectors or countries). On a tactical level, sustainability information might influence top-down decisions regarding the attribution to different sectors or markets at a given point in time. **36.**

Asset managers might also decide to apply ESG factors purely in the bottom-up process, integrating such factors in the assessment of individual portfolio holdings. **37.**

1.6.2 Different sustainability approaches

There are many different ways of integrating sustainability factors into an investment process. The following approaches are prevalent in the market and serve different needs or motives of different investors (see point 30-35). They are not mutually exclusive, and investors usually choose to combine different forms, depending on their motivation. The application of these approaches also varies across different asset classes (e.g. equities, fixed income, alternative investments) or investment styles (e.g. fundamental / quantitative investing, active / passive investing). **38.**

1.6.2.1 Exclusions (negative screening)

The exclusion approach (or negative screening) refers to the deliberate exclusion of issuers from an investment portfolio due to activities or business practices that violate given norms or values – based on client's preferences – or due to anticipated risks. **39.**

There are two main types of exclusions: *unconditional exclusions* of products or business activities incompatible with the investor's values (often referred to as values-based exclusions, e.g. exclusions of weapon manufacturers) or leading to excessive risks (e.g. coal mining) and *conditional exclusions* of companies based on negative business practices, such as breaches of certain norms, regulations or global ESG standards (often referred to as norms-based exclusions, e.g. systematic violation of human rights). The application of exclusion criteria can help to align an investment portfolio with the overall cultural values and norms of an investor and can reduce specific risks. **40.**

The Federal Act on War Material (WMA) of 13 December 1996[14] forms the basis for norms-based exclusions practised by many Swiss investors. It was amended in February 2013 to include provisions on financing in the context of war materials prohibited in Switzerland, e.g. nuclear, biological and chemical weapons, anti-personnel mines and cluster munitions. **41.**

It prohibits the direct financing of the development, manufacture or acquisition of prohibited war materials (Article 8*b* WMA). The indirect financing of prohibited war materials is banned only if intended to circumvent the ban on direct financing (Article 8*c* WMA). It refers to participation in companies that **42.**

[14] Classified Compilation 514.51.

develop, manufacture or acquire prohibited war materials, or the acquisition of debt securities or other investment products issued by such companies.

43. Based on this regulation – and taking current investment practice into account – excluding companies that produce such war materials prohibited in Switzerland is considered a minimum requirement for sustainably managed assets.

1.6.2.2 Best-in-class approach

44. This approach prioritises investments in companies with high sustainability standards across different sectors. A company's or issuer's ESG performance is compared with the ESG performance of its peers (e.g. of the same sector or industry) based on sustainability research / data. All companies or issuers with a rating above a pre-defined threshold are considered investable. The threshold can be set at different levels (e.g. 30 % best performing companies or all companies that reach a minimum ESG rating). The level of the pre-defined threshold defines the size of the remaining investment universe. Some best-in-class approaches focus on a small share of the total investment universe, while others still define bigger shares of the total universe as investable.

45. The best-in-class approach can support the focus on companies that have a reduced financial risk due to higher sustainability standards. Asset managers can rely on external sustainability ratings when applying a best-in-class approach, as the preparation of ESG ratings for a large universe is quite resource-intense. Using ESG benchmarks that are based on a best-in-class approach can also help an asset manager to implement such a strategy.

1.6.2.3 ESG integration approach

46. ESG integration refers to the inclusion of ESG risks and opportunities in the traditional financial analysis and investment decision based on a systematic process and on appropriate research sources. The idea is to get a holistic view of a specific issuer of securities. There are different forms of how ESG factors can be integrated into the financial analysis or the investment decision. Sustainability information can be used to adapt estimates of future cash-flows or it can lead to adjusted discount rates, to name just two examples[15]. Usually, ESG factors are only integrated into the investment decision if they are expected to be financially material. Hence, a company with a low sustainability performance in some areas might still be considered an interesting investment, as long as the expected financial risk / return of an investment remains attractive. This is a major difference to the best-in-class approach, where a minimum sustainability standard is defined for each investment.

1.6.2.4 Stewardship (active ownership)

47. The terms stewardship or active ownership are often used to refer to a combination of engagement and voting. In practice, asset managers either combine the two approaches or focus on one of them.

1.6.2.4.1 Voting

48. This term refers to investors addressing concerns about ESG issues by actively exercising their voting rights based on ESG principles or an ESG policy. Investors might choose to reject a certain proposal at the Annual General Meeting (AGM) based on the fact that it is not in line with their overall ESG policy. Many of the AGM agenda points do not directly refer to environmental or social topics, but rather to governance aspects. In some cases, investors therefore chose to indirectly express their discontent with a sustainability strategy by voting against other agenda items (e.g. blocking the re-election of certain board members who do not support the company's progressive ESG strategy).

[15] For further examples of ESG integration see also: ESG integration in Europe, the Middle East, and Africa: markets, practices, and data, CFA and PRI, March 2019.

An asset manager can establish their own voting policy covering the aspects perceived as relevant for the organisation (e.g. renumeration standards, governance structures, diversity) or act on the advice of external, specialised providers. **49.**

1.6.2.4.2 Engagement

Engagement refers to an active dialogue between shareholders and management teams of investee companies or other relevant stakeholders with the goal of convincing them to take account of environmental, social and governance criteria within their sphere of influence. A structured engagement process defines clear engagement targets with a clear timeframe and reports on outcomes such as changes in a company's strategy and processes so as to improve ESG performance and reduce financial risks. Engagement can complement voting, as it offers the opportunity to discuss issues with the management that are not on the AGM agenda. **50.**

There are different forms and levels of engagement: **51.**

- In the case of direct company engagement, each investor holds an individual dialogue on ESG aspects with companies. Such engagements are often carried out by analysts or portfolio managers that hold a dialogue with senior management and / or boards of the companies they invest in.
- In a collaborative engagement process, different investors team up to bundle their forces and investor power in the dialogue with companies or when co-filing shareholder proposals. The PRI (Principles for Responsible Investment) offers a “Collaborative Platform” on which investors can post initiatives and look for allies for their engagement processes. Some collaborative engagement processes are formalised into separate organisations (e.g. Climate Action 100+, The Institutional Investors Group on Climate Change IIGCC).
- A third form of engagement is public policy engagement, where investors lobby politicians for improved frameworks for a sustainable economy (e.g. calling for a carbon tax).

Investors might choose to outsource the engagement process to a service provider that pools the interests of different investors and thereby carries more weight in the dialogue with the companies. An asset manager can establish their own engagement policy covering the aspects perceived as relevant for the organisation or rely on an engagement policy of a respective service provider. The engagement policy should also address the escalation process foreseen in case an engagement is not successful. **52.**

1.6.2.5 Sustainable thematic investments

This approach refers to investment in businesses contributing to sustainable solutions both in the environmental and / or social dimension. In the environmental segment, this could include investments in renewable energy, energy efficiency, clean technology, low-carbon transportation infrastructure, water treatment and / or resource efficiency. In the social segment, this includes investments in education, health systems, poverty reduction and / or solutions for an ageing society. **53.**

1.6.2.6 Impact investing

Impact investments intend to generate a measurable, beneficial social and / or environmental impact alongside a financial return. Important differentiating factors to other forms of sustainable investments (namely thematic investing) are the *intentionality* of an investment in a sector or activity that has such a positive impact, the *management* process that allows for a direct impact, and the *measurability* of the impact through relevant Key Performance Indicators (KPIs). Impact investments can be made in both emerging and developed markets and target a range of returns from below-market to above-market rates, depending upon the circumstances. **54.**

55. If an asset manager claims to provide impact investment products, regular reporting is crucial for the intention, the respective management processes and the achieved impact, based on relevant KPIs.

1.6.3 Suitability of different approaches for different purposes

56. The different approaches described in chapter 1.6.2 have different effects and serve different motivations. It is important for an asset manager to choose approaches or combinations thereof that best match the main needs of their clients and the types of assets managed.

57. The table in Appendix 3 shows which approaches are particularly suitable for which asset classes, depending on the primary motivation of the target clients. It illustrates that not all approaches are equally suitable for all asset classes. Many investors choose to combine different approaches to best achieve their targets.

1.6.4 Monitoring

58. An effective implementation of a sustainable investment policy requires continuous monitoring of the process. Specific sustainability KPIs are the basis for such monitoring. Usually, such KPIs – e.g. sustainability ratings provided by an external provider or internally prepared KPIs – are integrated into the portfolio management and reporting system. This allows for tracking specific sustainability indicators (e.g. average sustainability rating of a portfolio) or the violation of a defined policy (e.g. black-listed company appears in a portfolio).

59. The evolution of the sustainability KPIs can be made a mandatory agenda item at portfolio management or risk management meetings. Furthermore, such KPIs can be integrated into personal objectives of relevant staff.

60. The asset manager should describe how the process of ESG implementation (chapter 1.6.2) is managed, ensured and monitored. He also defines management responsibilities for the monitoring process.

61. The asset manager ensures that it has allocated sufficient resources that allow for proper monitoring of the investment process.

62. The portfolio should be tested against the pre-defined sustainability KPIs regularly, e.g. once a year.

1.7 Risk management

63. Based on the SFAMA Specialist Recommendation on Risk Management[16], asset managers should integrate sustainability risks and opportunities into their existing risk management processes for identifying such risks and opportunities. They should also define how they identify, assess and manage sustainability risks and opportunities for each product or investment strategy. This might include a description of the resources and tools used in the process.

64. Based on SFAMA's Specialist Recommendation on Risk Management regarding the creation of a risk profile for a collective investment scheme or an asset management mandate[17], ESG risks and the approach to manage them at product level should be documented in the risk profile.

1.8 Transparency and reporting

65. Both institutional and private clients increasingly expect to be informed on a regular basis about the implementation of the sustainable investment policy including the data used. There are different forms for asset managers to provide this transparency and keep their clients informed. Building on existing

[16] SFAMA Specialist Recommendation on Risk Management, 7 September 2018.
[17] SFAMA Specialist Recommendation on Risk Management, 7 September 2018, point 47.

frameworks that make recommendations for sustainable investment reporting may help to increase comparability for clients[18].

1.8.1 Information on the product level

Asset managers should inform their clients about the sustainability performance of a given product by integrating relevant ESG Key Performance Indicators and / or additional information on relevant developments (e.g. ESG reasons behind major investments / divestments) into their client communication (e.g. in the product factsheet and / or through separate communications tools). **66.**

The asset manager has to ensure that he has access to data and has the right tools in place that allow for appropriate reporting on the sustainability performance of its portfolios[19]. It should be possible to provide clients with the necessary information to make an objective assessment of the asset manager's goals and outcomes. **67.**

The asset manager should report in a transparent way on how ESG is integrated into a product (e.g. which approaches are applied, scope of the sustainable investment policy, list of exclusions of products, applied metrics, results of the engagement process, voting records, etc). This gives clients the opportunity to compare products and to assess the sustainability performance of a product more easily. **68.**

1.8.2 Information on the company level

Preparing a sustainable investment report helps provide further insights into relevant developments across different portfolios. In such a report, asset managers can discuss concrete challenges and opportunities resulting from sustainability developments and provide illustrative examples of companies that profit or suffer from such developments. Furthermore, such a report could provide an overview of exercised voting rights and the results of engagement activities. **69.**

An asset manager should include a section on ESG in its annual reporting. This can for example include reporting on any recent activities (e.g. exercised voting rights) or describe any specific items that are / were subject to consideration in the organisation. **70.**

In cases where an asset manager actively participates in engagement programmes with companies, such activities should be reported as well. **71.**

1.8.3 Publication of the sustainability policy

On top of periodical information on sustainability activities, asset managers should inform on their website about the sustainability policy and strategy of their different products. Such documents can have an individual format or be based on an industry guideline. The Eurosif SRI Transparency Code[20], followed by many sustainability funds in Europe, defines different elements for which a sustainability fund should provide information. Usually such information is available on the website of the respective asset managers. **72.**

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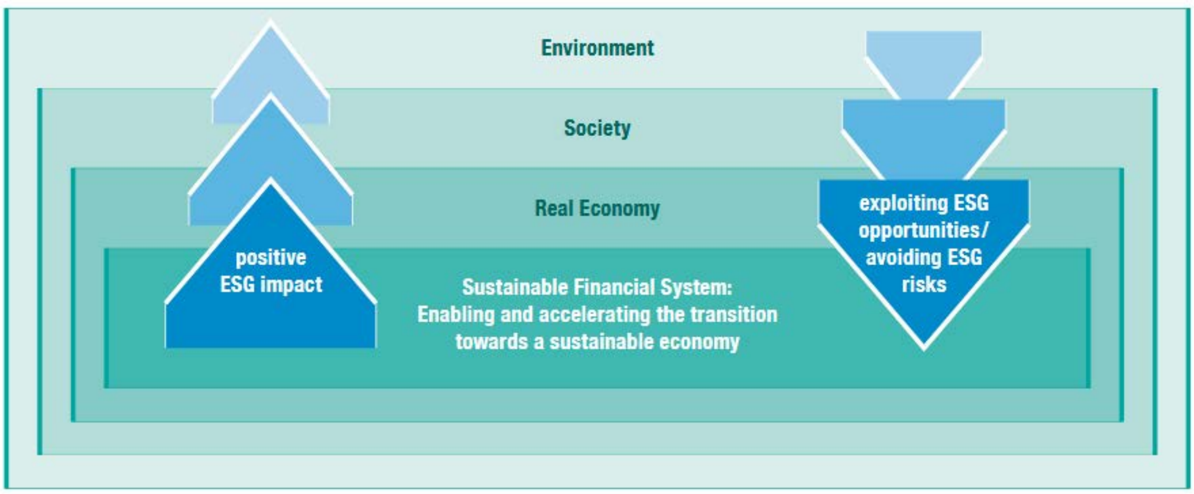
[18] Asset managers who have signed the Principles for Responsible Investments (PRI) are obliged to publish an annual PRI report. Large parts of this report are public by default. Asset managers with ambitious transparency goals often choose to make the whole PRI report publicly available. The Taskforce on Climate-related Financial Disclosure (TCFD) has published guidelines for financial service companies on how to report on climate risks of their portfolios.

[19] Data can be purchased from external providers or sourced directly from companies. There is a growing number of companies reporting ESG data, although reported KPIs are not always comparable. Initiatives such as Global Reporting Initiative (GRI), Sustainability Accounting Standards Board (SASB) and TCFD contribute to increasing data availability and standardisation of KPIs.

[20] European Sustainable and Responsible Investment Forum, Eurosif European Sustainable and Responsible Investment (SRI) Code, February 2018.

Appendix 1: The role of the financial system in the transition to a sustainable economy

The financial sector is part of the economic system and acts in the wider context of civil society and the natural environment. The developments in society and the environment (e.g. poverty alleviation, climate change, loss of biodiversity) hence influence the financial sector and its activities, while at the same time the financial sector, through its activities, has an influence on society and the environment:



Source: Proposals for a Roadmap towards a Sustainable Financial System in Switzerland, Federal Office for the Environment, 2016

Appendix 2: Terms and definitions

The following table contains definitions of various terms relating to sustainable finance and sustainable investments that are used in these recommendations[21].

(1/2)

Term	Definition
Best-in-class	Approach in which a company's or issuer's environmental, social and governance (ESG) performance is compared with that of its peers (e.g. in the same sector or category) based on a sustainability rating. All companies or issuers with a rating above a defined threshold are considered investable. The threshold can be set at different levels (e.g. 30% best performing companies or all companies that reach a minimum ESG score).
ESG - Environment, Social and Governance	ESG stands for Environmental (e.g. energy consumption, water usage), Social (e.g. talent attraction, supply chain management) and Governance (e.g. remuneration policies, board oversight). ESG factors form the basis for the different SI approaches.
ESG Analysis	Such an analysis includes collecting information on how an investment target manages and performs on environmental, social and governance factors. When an investment institution wishes to track to what extent potential investments (e.g. companies, countries and issuers) are exposed to ESG risks and opportunities and how they actively manage them, they carry out an ESG Analysis.
Engagement	Engagement is an activity performed by investors (typically shareholders or bondholders) with the goal of convincing management to take account of environmental, social and governance criteria. This dialogue includes communicating with senior management and / or boards of companies and filing or co-filing shareholder proposals. Successful engagement can lead to changes in a company's strategy and processes so as to improve ESG performance and reduce risks. Such engagement can be performed as direct interaction between an investor and an investee company or in the form of collaborative engagement, where a number of investors team up to hold a joint dialogue (often carried out by a respective service provider).
ESG Integration	The explicit inclusion by investors of ESG risks and opportunities in traditional financial analysis and investment decisions based on a systematic process and appropriate research sources.
Voting	This refers to investors addressing concerns about environmental, social and governance (ESG) issues by actively exercising their voting rights based on ESG principles.

[21] A broad overview of further definitions of various terms relating to sustainable finance and sustainable investments is available in the Swiss Sustainable Finance glossary (http://www.sustainablefinance.ch/en/glossary-_content---1--3077.html).

Appendix 2: Terms and definitions

(2/2)

Exclusions	An approach excluding companies, countries or other issuers based on activities considered not investable. Exclusion criteria (based on norms and values) can refer to product categories (e.g. weapons, tobacco), activities (e.g. animal testing), or business practices (e.g. severe violation of human rights, corruption).
Impact Investing	Investments intended to generate a measurable, beneficial real-world social and environmental impact alongside a financial return. Impact investments can be made in both emerging and developed markets and target a range of returns from below-market to above-market rates, depending upon the circumstances.
Responsible Investment / Sustainable Investment / ESG investment	Responsible investment (analogous to sustainable investment) refers to any investment approach integrating environmental, social and governance factors (ESG) into the selection and management of investments. There are many different forms of responsible investing, such as best-in-class investments, ESG integration, exclusionary screening, thematic investing and impact investing. They are all components of responsible investments and have played a part in its history and evolution.
Sustainability Ratings	Ratings reflecting how a company / country / fund manages and / or performs with regards to environmental, social and governance (ESG) factors. Sustainability ratings give investors a snapshot of the sustainability performance of a company / country / fund and are the basis for many sustainable investment approaches.
Sustainable Development Goals (SDGs)	The SDGs are 17 goals set by the UN in 2015 to be achieved by 2030, aiming to catalyse sustainable development. They include goals such as no poverty, gender equality, decent work, sustainable consumption, climate action and reduced inequalities. The goals were developed to replace the Millennium Development Goals (MDGs) which ended in 2015. Unlike the MDGs, the SDG framework does not distinguish between "developed" and "developing" nations.
Sustainable Finance	Sustainable finance refers to any form of financial service integrating environmental, social and governance (ESG) criteria into the business or investment decisions for the lasting benefit of both clients and society at large. Activities that fall under the heading of sustainable finance include (but are not limited to) the integration of ESG criteria into asset management, sustainable thematic investments, active ownership, impact investing, green bonds, lending with ESG risk assessment and the development of the whole financial system in a more sustainable way.
Thematic Investing / Sustainable Thematic Investing	Investment in businesses contributing to sustainable solutions both in an environmental or social dimension. In the environmental segment this includes investments in renewable energy, energy efficiency, clean technology, low-carbon transportation infrastructure, water treatment and resource efficiency. In the social segment this includes investments in education, health systems, poverty reduction and solutions for an ageing society.

Appendix 3: Suitability of different approaches for different asset classes, depending on the primary motivation (examples)

(1/3)

		Relevance / suitability	Asset class: Equities active	Equities passive	Corporate bonds active	Corporate bonds passive	Sovereign bonds	Real estate (direct)	Private Equity	Other alternatives**: microfinance (private debt)	Other alternatives**: commodities and precious metals
Motivation	**Complying with generally recognised standards and / or specific criteria imposed by their own organisation**	High relevance / good suitability	• Exclusion criteria • Best-in-Class	• Exclusion criteria	• Exclusion criteria • Best-in-Class	• Exclusion criteria	• Exclusion criteria	• Sustainable real estate	• Exclusion criteria • Sustainable thematic investments • Impact investing / Investments for development	• Impact investing / Investments for development	• Exclusion criteria
		Medium relevance / moderate suitability	• Active voting / Shareholder engagement • Sustainable thematic investments	• Best-in-Class • Active voting / Shareholder engagement • Sustainable thematic investments	• Sustainable thematic investments	• Best-in-Class	• Best-in-Class		• Active voting / Shareholder engagement *		
		Low relevance / moderate suitability	• ESG integration		• ESG integration			• ESG integration • Best-in-Class	• ESG integration		

* integral part of private equity investments

**Only those other alternatives are listed for which sustainable solutions already exist. Mortgages were not taken into consideration.

Source: Handbook on Sustainable Investments, Swiss Sustainable Finance, 2017.

Appendix 3: Suitability of different approaches for different asset classes, depending on the primary motivation (examples) (2/3)

		Relevance / suitability	Asset Class: Equities active	Equities passive	Corporate bonds active	Corporate bonds passive	Sovereign bonds	Real estate (direct)	Private Equity	Other alternatives**: microfinance (private debt)	Other alternatives**: commodities and precious metals
Motivation	**Improving the risk / return profile**	High relevance / good suitability	• ESG integration • Active voting / Shareholder engagement		• ESG integration			• ESG integration • Best-in-Class • Sustainable real estate	• ESG integration • Active voting / Shareholder engagement*		
		Medium relevance / moderate suitability	• Best-in-Class • Sustainable thematic investments	• Best-in-Class • Active voting / Shareholder engagement • Sustainable thematic investments	• Best-in-Class	• Best-in-Class	• Best-in-Class		• Impact investing / Investments for development • Sustainable thematic investments	• Impact investing / Investments for development	
		Low relevance / moderate suitability	• Exclusion criteria	• Exclusion criteria	• Exclusion criteria • Sustainable thematic investments	• Exclusion criteria	• Exclusion criteria		• Exclusion criteria		• Exclusion criteria

* integral part of private equity investments

**Only those other alternatives are listed for which sustainable solutions already exist. Mortgages were not taken into consideration.

Source: Handbook on Sustainable Investments, Swiss Sustainable Finance, 2017

Appendix 3: Suitability of different approaches for different asset classes, depending on the primary motivation (examples) (3/3)

		Relevance / suitability	Asset Class **Equities active**	**Equities passive**	**Corporate bonds active**	**Corporate bonds passive**	**Sovereign bonds**	**Real estate (direct)**	**Private Equity**	**Other alternatives**: microfinance (private debt)**	**Other alternatives**: commodities and precious metals**
Motivation	**Promoting sustainable development**	High relevance / good suitability	• Best-in-Class • Active voting / Shareholder engagement • Sustainable thematic investments	• Sustainable thematic investments	• Sustainable thematic investments			• Sustainable real estate	• Active voting / Shareholder engagement* • Sustainable thematic investments • Impact investing / Investments for development	• Impact investing / Investments for development	
		Medium relevance / moderate suitability	• Exclusion criteria • ESG integration	• Exclusion criteria • Best-in-Class • Active voting / Shareholder engagement	• Best-in-Class	• Best-in-Class		• ESG integration • Best-in-Class	• Exclusion criteria • ESG integration		
		Low relevance / moderate suitability			• Exclusion criteria • ESG integration	• Exclusion criteria	• Exclusion criteria • Best-in-Class				• Exclusion criteria

* integral part of private equity investments

**Only those other alternatives are listed for which sustainable solutions already exist. Mortgages were not taken into consideration.

Source: Handbook on Sustainable Investments, Swiss Sustainable Finance, 2017

Appendix 4: Literature and further information

- Principles for Responsible Investment, PRI Reporting Framework 2019, Strategy and Governance.
- Task Force on Climate-related Financial Disclosures, TCFD Implementing the Recommendations of the Task Force on Climate-related Financial Disclosures, June 2017.
- European Sustainable and Responsible Investment Forum, Eurosif European Sustainable and Responsible Investment (SRI) Code, February 2018.
- Swiss Sustainable Finance, Handbook on Sustainable Investments, December 2017.
- SFAMA, Specialist Recommendation on Risk Management, 7 September 2018.
- Swiss Sustainable Finance, SSF E-learning tool on sustainable investments, 2018.