



# OP Asset Management

## Principles for Responsible Investment

May 2020

# Principles for Responsible Investment

## 1 Responsible investing at OP Asset Management

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At OP Asset Management we believe that investment activities cannot be carried out with due care without incorporating responsibility factors into investment decisions and processes. An analysis of ESG factors gives us more information on the target than the mere assessment of its present financial situation, regardless of whether we are investing in shares, fixed income instruments, real estate or investment products offered by external asset managers. At best, a more broad-based analysis reveals risks or opportunities that may emerge later and that may have a significant impact on the financial situation and the value of the investment.

Figure 1 below describes the organisation of responsible investment at OP Asset Management. The main policies of responsible investment are approved by the executive committee of OP Asset Management. ESG specialists and the Committee for Responsible Investment make their decisions in line with these policies. The actual implementation of the ESG strategies is carried out on a case-by-case basis through fixed income investments, equity investments, cross-assets investments, real estate investments or ESG specialists or, alternatively, through collaboration between the ESG specialists and said functions.

Figure 1



We have systematically expanded our knowledge of responsible investment in portfolio management since we signed the UN Principles for Responsible Investment in 2009. We have various responsible investment strategies that we follow in different asset classes in the most suitable way. Our main strategies for responsible investment are ESG integration, owner engagement, exclusionary screening as well as thematic and impact investing. In addition, we report comprehensively on all our operations relating to responsible investment.

In executing ESG strategies, we use our own analysis and solutions as well as external ESG analyses and data, which we apply to different strategies in accordance with our practices.

We set the short-term targets of responsible investment for one year at a time so that they are embedded into all our asset management targets and support the long-term performance of our investment activities. ESG specialists are responsible for the practical implementation of the strategies and related training throughout the organisation. Our ESG specialists are part of the portfolio management teams.

The performance indicators of the ESG specialists track the annual targets.

The next chapters provide a more detailed overview of OP Asset Management's key strategies and practices for responsible investment.

## 2 Integration

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ESG integration is one of the cornerstones of the UN Principles for Responsible Investment. In practice, it means integrating responsibility factors into investment analysis and decision-making. We see that the ESG angle provides additional information that complements conventional financial and market data, and believe that relevant ESG factors can in the long run affect the financial performance of investments and, thereby, the obtained return.

- ✓ Active shares
- Passive shares
- ✓ Corporate bonds
- ✓ Government bonds
- ✓ External asset managers \*
- ✓ Real estate

Accordingly, we aim to recognise the relevant ESG factors for our investments.

### 2.1 Active direct shares and corporate bonds

OP Asset Management's portfolio managers take into account relevant factors relating to the environment, social issues and corporate governance in their active investment decisions and portfolio construction in a manner that supports the investment activity's return and risk targets. In this, they make use of high-quality external ESG research and OP Asset Management's own analysis and conclusions.

Analysts and portfolio managers making the investment decisions are responsible for incorporating responsibility factors into their activities with the support of our ESG specialists, who specialise in these issues. When portfolio management is based on qualitative analysis, meetings with company representatives play an important role in our in-house analysis. They provide our portfolio managers with the opportunity to discuss and ask questions about the ESG factors that they believe are the most relevant. We have also prepared a handbook that details ESG risks and opportunities by sector and assists portfolio managers in the meetings and in the portfolio management based on qualitative analysis. When the meeting is over, the portfolio managers enter the discussed ESG topics into a database. OP Asset Management's portfolio managers cannot make the investment decision before checking the target company's past compliance with international norms and business ethics from the up-to-date database. If a company is on a watchlist due to possible violations, portfolio managers may invest in that company, but the violations on the watchlist must be taken into account both in the company analysis and the investment decision. The ESG integration process is the same for active direct share and active direct corporate bond investments. Credit ratings also contain ESG information so they are used in the assessment of corporate bonds.

In index-tracking investments, the selection of investments and the construction of the portfolio are, as the name implies, entirely based on the chosen index, and ESG or other types of analysis do not affect investment decisions. OP's own fund-of-funds may invest a part of their assets in passive equity funds, funds managed by external asset managers or ETF products.

## 2.2 Government bonds

Credit ratings are essential for the analysis of government bonds and the related investment decisions and portfolio construction. Issued by several service providers, credit ratings describe a country's capacity to pay interest on debt and repay the principal. Many of the factors covered in credit ratings also have a responsibility angle, such as the stability of institutions and the likelihood that civil peace will be disturbed. The country's education system and its quality, for example, affect productivity growth and, through this, the credit rating.

## 2.3 External asset managers

OP Asset Management reviews the active external asset managers' responsible investment practices prior to making any investment decisions and, thereafter, monitors them regularly. We use this review, which covers factors relating to responsible investment policies and statements, resource allocation to responsible investment, ESG integration, ESG reporting, exclusionary screening and owner engagement, for assessing the quality of the external asset managers' responsible investment. We have also determined a set of minimum criteria that new active external asset managers must meet. On top of this, OP Asset Management's ESG specialists meet and organise conference calls with external asset managers. The principles and practices described above also apply to hedge funds managed by external asset managers.

Some OP funds are managed by external asset managers. They apply the same practices relating to exclusionary screening, engagement and voting at shareholders' meetings as the funds managed by OP Asset Management. In addition, the investees of these funds must comply with international norms. OP funds managed by external asset managers also follow our thematic engagement policies. Otherwise, the practices of external asset managers may vary.

In real estate investing through funds, we review the responsible investment practices of external asset managers prior to making any investment decisions and, thereafter, monitor them regularly. We use this review, which covers factors such as responsible investment policies and statements, resources allocated to responsible investment, ESG integration and ESG reporting, for assessing the quality of the external asset managers' responsible investment. We have established minimum criteria for real estate funds. We use our influence to ensure that the boards and investment committees of underlying investee funds and companies pay attention to ESG factors and report on them.

## 2.4 Direct real estate investments

Prior to making a decision to invest directly in real estate, we assess the target's energy efficiency and evaluate factors such as public transportation. We also measure the direct real estate investment's electricity, heating energy and water consumption together with the amount of waste produced, with the objective of reducing the use of these resources. In new build and renovations, we estimate the probability of obtaining an environmental certificate for the building and for potential renewable energy production. We require the constructors of our buildings to provide us with a waste management plan and a report on waste produced.

## 3 Thematic and impact investment

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At OP Asset Management, thematic investment and positive screening mean placing the focus on megatrends and responsibility themes. In responsible thematic investment, we focus especially on environmental themes. The companies involved build their business on the development of ways to fight climate change and solutions for ensuring the availability and cleanness of water.

- ✓ Active shares
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- Real estate

We use positive screening especially in our four thematic responsible investment funds: OP-Low-carbon World, OP-Climate, OP-Clean Water and OP-Sustainable World. The portfolio managers of these funds must ensure that the selected companies have a positive impact on the theme in question. Companies positively exposed to megatrends and responsibility themes are interesting investments also outside the thematic products.

## 4 Owner engagement

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Responsibility factors affect our decisions on which companies we invest in. After an investment decision, it is also important that, as the owner of a company's securities, we play a role in the development of that company regarding both responsibility and financial matters. Public owner policies that take responsibility factors into account lay a solid foundation for responsible investment. They can be exercised alone or jointly with other investors at shareholders' meetings, by engaging directly with companies or through thematic engagement.

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### 4.1 General meetings of shareholders

OP funds participate actively in the AGMs and EGMs of listed Finnish companies. The criteria for participating in these meetings are the size of the stake in the companies in question, their portion of the fund's investments and the general significance of the meetings.

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OP funds also participate extensively in the shareholders' meetings of foreign companies. Here, our criteria for participation include the size of the investment within the fund and the suitability of local practices on shareholders' meetings.

The ownership policy of funds managed by OP Fund Management Company contains a more detailed description of our policy lines for shareholders' meetings.

### 4.2 Violations of international norms and thematic engagement

The scope of engagement primarily covers international norms, such as OECD guidelines and the UN Global Compact principles, but we may also influence other topical and significant ESG themes. We use a service provider to identify any suspected cases of violation and to verify violations of international norms. Our primary mode of action is to influence a company's action, preceding the sale of our holding.

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In thematic engagement, we seek to identify similar significant risks associated with the environment, social aspects and corporate governance for a larger number of companies. We engage in simultaneous dialogue with various companies exposed to similar risks with a view of fuelling a change in several companies at the same time while identifying best practices. Thematic engagement may relate to themes such as climate change, and we can also use service providers for thematic engagement.

In addition, we exercise our influence by taking part in joint shareholder initiatives. The objective of these initiatives may be, for example, to push companies to report on climate change issues and water risks. We may also exercise above-mentioned thematic engagement through joint initiatives. OP Asset Management's Engagement Policy describes these practices in greater detail.

## 5 Exclusionary screening

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We also use the exclusionary screening strategy for other than index-tracking products and indirect investments. Exclusion may be based on the violation of international norms, manufacturing of weapons prohibited under conventions or financial factors relating to climate change. Our list of exclusions is public and is updated whenever necessary. The list applies to all types of active direct discretionary investment, such as OP funds engaging in active direct investment. It also covers derivative contracts relating to the excluded companies, with the exception of sector and index-tracking derivative contracts. In addition, our fund selection includes an alternative that excludes a larger number of companies.

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### 5.1 Violations of norms

We do not make active direct investments in companies that have violated international norms and where engagement has been unsuccessful. We monitor our investments on an ongoing basis, in addition to which we screen and review the investments quarterly for compliance with international norms and business ethics. If a company we have invested in is considered to have violated international norms, or business ethics at a severe level, we will either sell the investment or start to engage with the company. However, we exercise our discretion in cases where a company has been excluded due to a norm violation but the actions which led to the violation are considered to have expired, or if the company has already proven that it has taken a sufficient amount of corrective measures.

When OP Asset Management's portfolio managers make a new active direct investment in a company, they verify its history for compliance with international norms. If the review uncovers a confirmed violation, they cannot invest in the company without the consent of the Committee for Responsible Investment. The portfolio manager may ask for approval for the investment, and the Committee normally grants it but always on condition that ESG specialists will start the engagement process with the company.

## 5.2 Controversial weapons

We have excluded from our active direct investments any companies that engage in the manufacture of weapons prohibited under international conventions. OP Asset Management's portfolio managers do not make active direct investments in companies that market, develop or produce anti-personnel landmines, cluster munitions, chemical or biological weapons or nuclear weapons that are prohibited under international conventions. Also companies that manufacture components that may only be used exclusively in the production of said weapons are excluded. Regarding nuclear weapons, we exclude companies that produce or manufacture nuclear weapons for countries other than the five "accepted" nuclear-weapon states, or that violate UN sanctions or the rules of the IAEA.

## 5.3 Coal producers and users

We have excluded coal-dependent mining and power companies from our list of active direct investments. The reason for the exclusion is financial, as measures to curb climate change, legislation together with various coal taxes or emissions trading are likely to turn coal usage economically less attractive.

Regarding coal producers and users, in other words mining and power companies, OP Asset Management excludes companies that are in the large global equity index MSCI ACWI IMI and that meet the following criteria:

- companies that make more than 25 per cent of their sales by producing coal for energy generation
- companies that make more than 25 per cent of their sales with coal-fired energy or power companies that base over 25 per cent of their production capacity on coal.

Exclusion can be avoided if the company has a high ranking among its peer group in terms of actions against climate change.

## 5.4 Government bonds

In government bonds, we do not invest in bonds issued by governments that do not meet the FATF criteria for anti-money laundering and terrorist financing. We also take into account domestic and EU sanctions and their restrictions on activities in government bond markets.

## 5.5 Permitted domiciles of funds managed by external fund managers

The Banking Corporate and Institutional Customers Management Board has listed, after hearing OP's Corporate Responsibility Committee, the domiciles permitted for investment solutions, i.e. funds. We permit the following domiciles for funds: the EU, the USA, the UK, Switzerland, Bermuda, British Virgin Islands, Cayman Islands, Guernsey, Isle of Man, Jersey, EEA excl. the EU, Canada, Liechtenstein,



Singapore and Hong Kong. We will review and, where necessary, update the list of permitted domiciles on an annual basis. In the review, we pay attention to the following public listings:

- Global Forum standard of exchange of information on request for tax purposes
- EU list of non-cooperative jurisdictions for tax purposes
- Financial Action Task Force identified jurisdictions with strategic AML/CFT deficiencies
- Financial Stability Board: Global adherence to regulatory and supervisory standards on international cooperation and information exchange

## 6 Reporting

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All our responsible investment reports are available on our responsible investing website. The site includes Principles for Responsible Investment, OP Asset Management's semi-annual RI Transparency Report, semi-annually calculated carbon footprints of mutual funds, an updated list of excluded companies as well as a link to fund-specific ESG reports. For our direct real estate investments, we annually report the environmental impacts of the properties, including the consumption of energy, heating energy and water together with the amount of waste produced.

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OP Asset Management's semi-annual RI Transparency Report describes topical events in investment operations from the responsibility perspective and summarises OP funds' activities in shareholders' meetings. Furthermore, we report annually on the basis of the UN Principles for Responsible Investment.

## 7 Summary

Like these principles for responsible investment demonstrate, OP Asset Management's responsible investment activities are broad-based and well integrated into our processes. These principles for responsible investment are updated whenever necessary. We also aim to report our activities as extensively and openly as possible. The table below summarises our responsible investment strategies and their execution in different asset classes.

	Active shares	Passive shares	Corporate bonds	Government bonds	External asset managers	Real estate
Integration	✓		✓	✓	✓*	✓
Thematic investment and engagement	✓		✓			
Owner engagement: shareholders' meetings	✓	✓			✓**	
Owner engagement: international norms and thematic engagement	✓		✓		✓**	
Exclusionary screening	✓		✓	✓	✓**	
Reporting	✓	✓	✓		✓**	✓

\*) Responsibility aspect is taken into account in the selection of external asset managers

\*\*\*) OP funds managed by external asset managers follow OP Asset Management's policies for voting at shareholders' meetings, engagement, exclusionary screening and reporting