Willis Towers Watson

Sustainable Investment Policy

Delegated Investment Services

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Contents

1. Introduction and scope

Sustainable investment ("SI"), we believe, is central to successful long-term investment outcomes and a key part of Willis Towers Watson's beliefs and investment approach.

SI describes long-term, finance-driven strategies that integrate environmental, social and corporate governance ("ESG") factors, effective stewardship and real-world impact in investment arrangements. This reflects, in our view, good risk management and supports a robust investment industry. We believe that the principles underlying SI form the cornerstone of a successful long-term investment strategy and that SI considerations can materially improve risk and/or return for our portfolios. In addition, this topic is subject to significant regulatory and public scrutiny, as well as material reputational risk.

Our delegated solutions are in many ways complete reflections of our investment expertise – building portfolios that are designed to contain our best ideas in return generation and risk management. Therefore, delegated portfolios look to fully embed the best of our SI research, risk management and idea generation. This policy documents the way in which the Delegated Investment Services team currently does this in its portfolios, and is intended to cover our delegated offerings globally. This policy accompanies the overall investment business approach to sustainability and the firm-wide activities undertaken in this area.

Related content:

- Willis Towers Watson Sustainable Investment
- Wills Towers Watson ESG
- Willis Towers Watson Climate Risk and Resilience

2. Willis Towers Watson's purpose

Willis Towers Watson's overarching purpose is 'creating clarity and confidence today for a more sustainable tomorrow' so sustainability is at the heart of what we do as a firm.

Within the investment practice, we exist to deliver better outcomes for savers.

Better outcomes mean better, long-term returns with well-managed risk along the way. To achieve this we must continue to innovate and focus on the forward-looking risks and opportunities. This includes the risks and opportunities associated with sustainability.

Sometimes achieving better outcomes will also mean improving the quality of the savings system so that savers' confidence in that system increases and they are willing to save more. It may also mean investing in a way that has a positive impact on the world that savers live in and will retire into.

We recognise our duty to multiple current and future stakeholders – clients, employees, shareholders, wider society and the planet – as these are all interconnected. Better outcomes require changes – from us as individuals, as a firm and as an industry. We therefore take our role in changing investment for the better very seriously.

We summarise this purpose as 'investing today for a more sustainable tomorrow'.

Note: Although this policy document reflects Willis Towers Watson's current approach and understanding, it is subject to change at any time.

3. Beliefs

As a fiduciary manager we have a responsibility to act in the best interest of our clients. Fundamentally this means seeking the best risk-adjusted returns as applied to their individual investment contexts, which includes considering all material risks (current and future), many of which we see as sustainability related.

In order to fulfil this responsibility, we attempt to think and act like a leading asset owner and responsible market participant. One of our core investment beliefs (copied below) is specifically focused to SI.

Sustainable investment is central to successful long-term investor outcomes

- Sustainable investing is about employing long-term strategies that integrate ESG factors and effective stewardship, with regard for the impact on society and the planet now and in the future, recognising that this influences both risk and return
- Sustainability risks tend to be inaccurately appreciated by the market. Investors should look to use informational and implementation advantages to improve long-term outcomes by avoiding unrewarded risk, seeking opportunities, undertaking effective stewardship and managing impact
- Collaborative engagement and advocacy are important to give the investment industry a stronger voice and improve investment outcomes for all participants
- Climate change, and a just transition to net zero carbon emissions, is a systemic and urgent global challenge which necessitates specific risk management, opportunity identification and collective action

As highlighted above, within the broad remit of sustainable investment, we have identified climate change as a critical and systemic priority, given the risk it presents to our clients' investments, the ongoing resilience of the savings universe, and the planet as a whole.

4. Structure

SI is embedded throughout our investment process, from setting a mission and belief framework, through risk management, portfolio construction and manager selection, to implementation and monitoring. We view SI as an integral input to the decisions we make, not a separate or disconnected consideration.

In order to best achieve this integration, SI is the ultimate responsibility of the Global Chief Investment Officer who is responsible for and oversees all our investment content and portfolio management. The Head of Sustainable Investment, who reports to our Global Chief Investment Officer, is tasked and empowered to ensure teams and individuals are applying best practice SI principles, as well as providing advice and training to associates as necessary. Each associate applies SI as tailored to their particular role, further supported by a network of over 50 SI champions across the business. These SI champions are key in applying our beliefs and framework to their particular team and area of expertise, and the network has representation across all our teams and geographies.

[redacted]

5. Integration

We believe that integrating SI into the entire investment process is the best way to realise the full value available from SI. We describe below how we attempt to embed SI from a top-down and bottom-up perspective across both research and portfolio management.

a. Asset research

Identifying investment opportunities and risks

Sustainability and ESG are key factors in identifying themes and asset classes we wish to pursue, avoid, overweight or underweight in our clients' portfolios. Determining these views is an exercise of ongoing collaboration across all of our research teams, the Thinking Ahead Institute and portfolio management.

Long-term themes

Our asset research team analyse long-term global trends and have developed detailed long-term themes in conjunction with the Principles for Responsible Investment (PRI). These themes are outlined in the appendix along with the United Nations Sustainable Development Goals (UN SDGs). We consider the exposure of our portfolios to these themes, and believe that assets that align well with them not only stand to benefit and profit from the shift in global capital as the trends accelerate and are more widely adopted, but also create positive change for society. The long-term nature of these moves makes illiquid assets a great way to express these views, although we do target exposure in more liquid assets too.

b. Manager research

We have a formal process for integrating SI into our manager research decisions, which is tailored to be most relevant and appropriate for the asset class and strategy in question.

Our assessment of an asset manager's SI practices and implementation, in the context of individual strategies and products, feeds into our overall view of their ability to sustain a competitive advantage and the suitability of those products for our clients' portfolios. Consequently, the overall rating we place on a strategy will reflect our view of the SI credentials and capabilities of the strategy under review.

In order to better assess the quality of sustainable investment approaches, our focus varies by asset class. For example, in listed equities we particularly emphasise voting and engagement activity. In real estate, we often focus more on specific and detailed environmental, social and governance practices that are applied to the assets.

In addition, we recognise that long-term themes may create return opportunities and we explore these through our manager research process too, where we look for positive alignment, particularly in private markets.

Finally, a large part of our manager research process is based on assessing the culture in place at the asset manager. Our Thinking Ahead Institute has written multiple papers on how to assess culture, focusing on leadership, the client value proposition and the employee value proposition. SI plays a significant part in this culture assessment, including inclusion and diversity principles.

Related content:

- Willis Towers Watson PRI megatrends research
- Thinking Ahead Institute Culture and Leadership Study
- Measuring culture in asset managers

Figure 1. **For strategies we recommend our clients invest in, we expect asset managers to:**

Have a demonstrable process in place that identifies and deals with material SI issues	Avoid or seek to remedy any unrewarded ESG risks	Assign clear responsibility for maintaining and developing SI standards and implementation	Be a responsible market participant, for example supporting and contributing to key relevant SI bodies and initiatives

c. Portfolio management

Our portfolio construction process focusses on maximising portfolio quality, as evaluated through a number of 'lenses', including sustainability. This helps us build robust, diversified portfolios to meet our clients' risk and return requirements, as well as help to ensure our portfolios are resilient to a range of sustainability-related issues and/or able to take advantage of sustainability-related opportunities.

We recognise that while many SI considerations have clear risk and return consequences, embedding this 'lens' into portfolios also requires us to consider issues that are subject to greater uncertainty, less measurement and are heavily context-dependent. This can include, for example, issues with potential reputational risks for us and our clients. Therefore, the roles of judgement and qualitative overlays are crucial.

SI is incorporated into our portfolio management process through a number of avenues. An important part of our framework for doing this is to assess sustainability through two dimensions (see *Figure 2*).

Figure 2. **A framework for assessing sustainability**

Portfolio resilience

Exposure of the portfolio to sustainability-related risks and opportunities

Manager SI integration

The extent to which, and success with which, sustainability is incorporated into the decisions made by managers in the portfolio

Given the prioritisation of climate change noted earlier, this is a key focus of our portfolio construction process – understanding our risk exposures and reducing them through time, as well as identifying and investing effectively in the opportunities. This occurs both through top-down identification and analysis of climate-impacted sectors for investment, as well as the bottom-up contribution of each manager investment.

The portfolio management team has the job of bringing together all of the research, risk management and idea generation done by different specialist teams in the business in a consistent manner for all our clients and funds. Our clients have many different constraints and types of mandate with us, meaning a 'one size fits all' approach is not possible. Each portfolio management team must make different trade-offs to create the best quality portfolio possible through our lenses, guided by our Portfolio Management Group (PMG), which is responsible for setting model portfolios for delegated clients globally. PMG are the ultimate owners of this SI policy and our Global Chief Investment Officer and Delegated Chief Investment Officer are responsible for ensuring our teams around the world implement the policy effectively.

Portfolio tools

In order to assist our portfolio construction and management processes, we draw on a number of portfolio tools, the majority of which have been developed and tailored in-house to best align with our approach to building portfolios and our investment beliefs. Examples of some of these tools are outlined below in *Figure 3,* and illustrated in more detail in *Figures 4 to 8*.

We currently use a variety of third party data sources as input to some of these tools. For example, in our equity, corporate credit, and sovereign bonds exposures (including exposure through hedge funds), we make use of MSCI ESG research which allows analysis of holdings-level ESG scores, their component E, S and G aspects, key climate change related metrics, and controversy data. At both a security and portfolio level, this allows us to challenge bottom-up security selection decisions with managers and apply top-down portfolio management, on absolute and relative bases.

These tools are combined within our overall portfolio construction tool which assesses all the lenses of portfolio quality that we consider, and allows us to build portfolios that weigh these lenses according to our investment beliefs, market conditions and client contexts.

Figure 3. **Example portfolio construction and management tools**

Portfolio resilience scoring

Aggregating security-level ESG data to indicate the total exposure of a portfolio (or parts of a portfolio) to a wide range of sustainability issues

Scenario analysis

Used to stress-test our portfolios, including for example on realistic global emissions pathways to assess portfolio quality in the face of various climate change scenarios

Physical risk mapping

Using location data to assess assets' exposure to a range of physical risks and perils under a variety of climate change scenarios

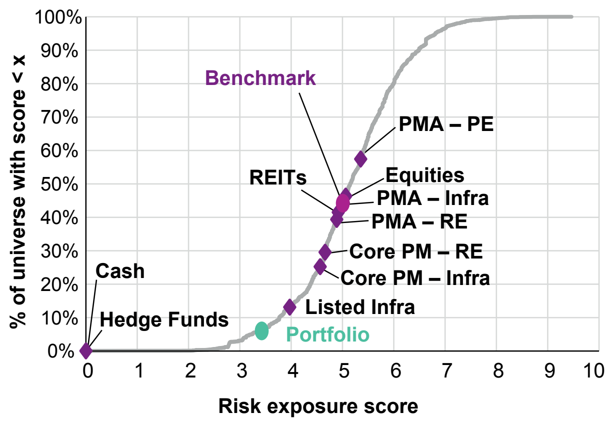
Thematic risk and opportunity exposure

Identifying key trends and sub-trends with outsized risks and opportunities, and mapping portfolios to minimise exposure to the former and maximise exposure to the latter

Note: As our SI policy and approach develop, so do our tools and, as a result, the examples shown here can change at any time or be replaced or discontinued.

Examples of our portfolio construction and management tools

Figure 4. **Portfolio sustainability risk exposure vs. security universe**



Source: Willis Towers Watson and MSCI

Figure 5. **Example manager sustainable investment report summary**

Manager	Product	ESG integration	Voting	Engagement	Change comments
Manager A	Equity Indexation				
Manager B	Global Equity			▲	Appointment of third party to provide corporate engagement overlay
Manager C	Developed Market Sovereign Credit				
Manager D	Private Market Fund				
Manager E	Real Estate Fund				

Each asset manager's strategy is generally assessed against the following three key areas:

- Integration of ESG risks and opportunities within investment research and decision-making, including resources available
- Proxy vote decision-making and execution process (where applicable), including disclosure of voting policy and results
- Process for proactive corporate/asset engagement (where applicable), including disclosure of engagement activity

Key

Strength: the asset manager largely adheres to and may exceed recognised best practice standards

Neutral: the asset manager's approach is satisfactory but may not be wholly consistent with recognised best practice

Weakness: the asset manager's approach is not satisfactory in our opinion and would benefit from improvement

▲ Positive change

▼ Negative change

Figure 6. **Example product sustainable investment report**

Global Equity – Strategy XYZ

Executive summary

Manager A is a medium-sized manager that runs concentrated long-only portfolios of around 30 to 40 stocks. Its concentrated portfolio naturally lends itself to active ownership and the integration of environmental, social and corporate governance (ESG) considerations. It aims to vote all its proxies, and will engage with a company on an issue of concern. Overall the approach followed currently has limitations with potential areas for improvement, such as more systematic consideration of consideration of ESG risks, a more expansive voting policy and also reporting of engagement activity.

Success factors	Strengths	Weaknesses or issues
ESG integration	Manager publicly supports sustainable investment initiatives There is a firm-level policy in place covering how ESG risks are assessed and integrated into the broader investment process. This is not publicly available, but is disclosed to clients Research analysts undertake ESG analysis and document these risks within company analysis ESG risks are considered as part of the valuation and portfolio construction process, as well as the process to identify the investable universe	There are no internal resources dedicated solely to ESG analysis There is only occasional consideration of ESG risks when it is considered relevant within this strategy The strategy's formal policy on ESG analysis and integration is not publicly available but is disclosed to clients on request Analysts are not provided dedicated training to help identify and understand the importance of ESG issues
Voting	The firm's voting policy is disclosed to clients, but not publicly Summary firm-level voting activity and complete voting history is disclosed publicly, including rationale for contentious votes As part of the investment process, all votes are exercised where appropriate to do so Contentious voting decisions are made by the investment team	There is a voting policy in place, but this does not include how conflicts of interests are addressed or beliefs on voting in respect of ESG-related issues, such as remuneration and corporate governance structures Summary firm-level voting activity is disclosed to clients, but lacks details on rationale for contentious votes or voting history
Engagement	The firm's engagement approach is globally consistent, subject to regulatory restrictions The firm participates in and occasionally lead collaborative engagement efforts Engagement activity is undertaken by the investment team and with senior-level executives such as chief-level executives and the board of directors	There is no firm-level engagement policy in place Engagement undertaken by the firm is not generally reported

Key: Strength Neutral Weakness Positive change Negative change

Global Equity – Strategy XYZ

Executive summary cont.

Manager position statement: "ESG considerations are important and a fundamental part of the analysis of a company where relevant. We invest in typically 30/35 stocks which we believe are good quality highly visible businesses. Our valuations depend on predictability of management and dependability of cash flows. As such anything that could jeopardise the company in any way must be examined and considered. If we believe there is a potential issue we will engage with management and use independent expert networks to obtain an unbiased opinion. This is likely to be more focussed on governance issues but where relevant social and environmental would be considered. We focus on three main areas – accountability, alignment and transparency."

Annual update: ESG integration – Voting – Engagement .

Firm background	
Firm assets	US$ xx m
ESG/sustainability lead	Fund Manager /Head of Global
ESG team size	0
# stocks >3% owned	13
Supported initiatives	PRI, UK Stewardship Code, multiple others

Firm voting activity	
# eligible votes	1,353
% votes exercised	95%
% against | abstained	2% | 2%
% against remuneration	1%
Top two topics voted against or abstained	1. Remuneration 2. Board structure

Firm engagement activity	
# of engagements	6
Top two engagement topics:	1. Capital structure 2. Remuneration, Social or ethical and Board structure
Most intensive company engagement	Li and Fung – Social and governance

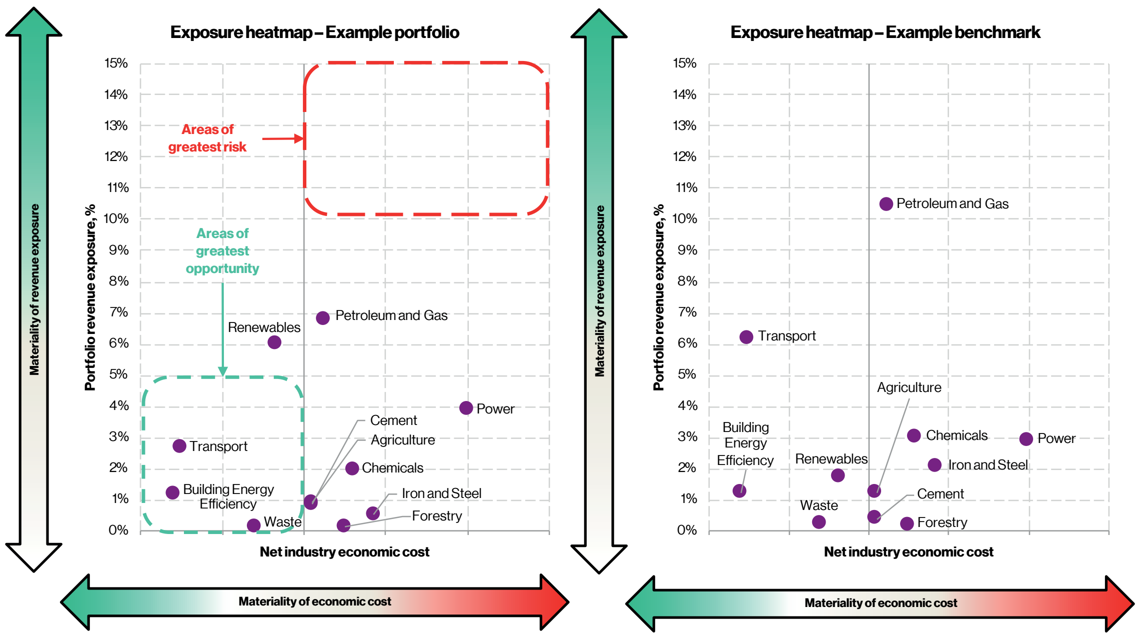
Product background	
Product assets	US$ 13,700 m
Product type	Active – Fundamental
Typical # of holdings	34
Turnover	41%
# stocks >3% owned	12
Exclusions applied	None as standard
Exclusions available	If requested by a client

Product voting activity	
# eligible votes	476
% votes exercised	95%
% against | abstained	2% | 2%
% against remuneration	1%
Top two topics voted against or abstained	1. Remuneration 2. Board structure

Product engagement activity	
# of engagements	6
Top engagement topics:	1. Capital structure 2. Remuneration, Social or ethical and Board structure
Most intensive company engagement	Li and Fung – Social and governance

Source: based on information provided by the asset manager

Figure 7. **Example exposure to climate risks and opportunities**



Source: McKinsey Global Institute, Factset, Willis Towers Watson

Figure 8. **Example physical risk peril mapping**

XYZ Real Assets Portfolio (sample)

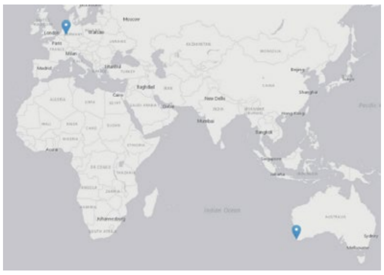
	Valuation ($m)	Country
Asset A	282.5	Australia
Asset B	43.4	Netherlands

Understanding Exposure to Natural Perils

- We provide a concise view of natural peril exposure for the two assets in the XYZ Real Assets Portfolio.
- It provides the foundation for understanding and managing physical (catastrophe) risk.
- Natural Catastrophe is comprised of twelve natural perils, with more weight given to more damaging perils.
- The assessment of your exposure to 12 natural peril risks is condensed into one overall figure – the Aggregate Risk Score. The risk score is from 1 (low risk) to 5 (high risk).

Aggregate Risk Score for the sample portfolio

Aggregate Score	
Natural Catastrophe	**3.1**



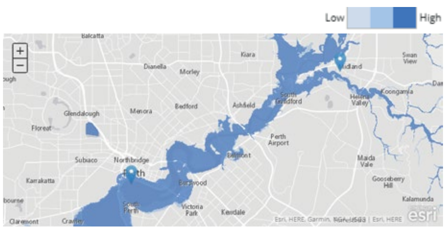
Breakdown by Peril

	Winter storm	Flash Flood	River Flood	Tornado	Coastal Flood
Peril Score	3.13	2.87	2.73	2.13	0.67
% Locations	100%	50%	50%	50%	50%
% Asset Valuation	100%	86.7%	86.7%	13.3%	13.3%

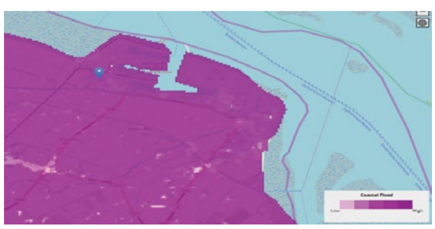
Peril score is an average of each location's score, weighted by total insured value. Percent exposed indicates the proportion of locations by count or by total insured value with a high risk score for each (3 or higher)

Source: Willis Towers Watson

Asset A



Asset B



6. Stewardship

We believe that effective stewardship is a critical aspect of sustainable investment and important to a well-functioning investment industry. We recognise our role as an influential industry participant, and seek to exercise our stewardship responsibilities, either directly or via third parties, across a range of activities:

- Asset manager engagement
- Security-level engagement
- Voting
- Public policy, advocacy and collaboration

We also engage extensively with our clients, and with asset owners in general. This is partly to ensure that we provide the best possible services and outcomes now and into the future with a close understanding of their needs. However this engagement is also important to help them shape and contribute to a sustainable investment industry where they themselves can be influential and advocate for and support positive change.

a. Asset manager engagement

The main goals of our manager research process are: a) finding the best asset management organisations capable of delivering superior outcomes to our clients; and b) working together with these organisations to explore ways to better meet our clients' evolving needs. Each of our asset manager appointments is seen as a long-term partnership with an institution we rate highly. Our manager research team practises asset manager engagement in the same manner that we ourselves expect asset managers to engage in a constructive dialogue with the businesses, issuers and assets they own.

The three main priorities that have recently defined and will continue to define our asset manager engagement in the foreseeable future are as follows:

- Sustainable investment
- Culture
- Inclusion and diversity

What constitutes best practice in these three areas has been rapidly evolving, and as a result, we engage with asset managers not only to evaluate their current capabilities but also their plans and desired outcomes in the future plus activities to achieve them.

We encourage our preferred asset managers to articulate their purpose beyond narrowly defined financial returns and include benefits for clients, employees, society and planet.

We want to engage with those firms that recognise their responsibility in actively creating a sustainable future and expect an industry mindset shift in the way leading groups make their investment and business decisions towards more direct consideration of externalities. One important example is encouraging our preferred managers to carefully consider the coming global climate transition in their investment decisions.

While different firms vary in their approaches, their leadership usually plays the critical role in defining the purpose, motivating their employees and creating the ability to continuously improve. Hence, our asset manager engagement process involves interaction with the most senior leaders of the firms with which we partner.

We highlight stewardship as an area where the industry needs to improve. Engaging with underlying businesses, issuers and operating assets, not on quarterly results, financial models and valuations but on their strategy, culture, leadership, innovation, and sustainability is an opportunity for the asset management community to demonstrate actual value creation to society. We have engaged with numerous managers in detail on this, shared best practices and have published research to call for greater efforts.

With closed-end funds, we often have significant representation on investor advisory committees which allows us a clear mechanism for ongoing engagement, oversight and influence. We currently have seats on over 50 investor advisory committees.

In those rare instances where our engagement process does not lead to sufficient progress, we often will look to allocate capital to other opportunities.

In addition, our manager research team engages with our preferred asset managers and other third parties to design and provide seed capital for new solutions where existing offerings do not meet our clients' needs. We have created more than 130 such new solutions in the last 15 years. An example of this is the MSCI Adaptive Capped ESG Universal Index which can be used for core equity exposure for both DB and DC clients, and explicitly incorporates ESG ratings, ESG momentum and minimum standard exclusions within the index design.

Related content:

- Manager Ideas Exchange
- Investor Stewardship: One hand on the wheel

b. Corporate engagement

We endeavour to effect positive change in our industry and the market more widely, and therefore promote corporate engagement as a tool to help achieve this. In the vast majority of cases, corporate engagement is the responsibility of the underlying managers who hold the securities and are best-positioned to engage. It is therefore a key part of our research and engagement with managers (as above) to assess the engagement capabilities and practices of managers, share and encourage best practices, and advocate for greater and more effective stewardship at an industry level.

To supplement corporate engagement carried out by individual managers, we have partnered with EOS at Federated Hermes ("EOS") – a leading stewardship provider. For several of our funds, EOS provide additional corporate engagement to that of the asset managers, applying their expertise, scale and market standing to effect positive change. We have worked closely with EOS for many years, input into their engagement planning and prioritisation, and currently have representation within their Client Advisory Board as vice-chair.

c. Voting

Voting on equity shares is an important and visible engagement tool. In our portfolios, there are two ways in which we exercise our voting rights and responsibilities:

i. Third party funds

This is the most common method of ownership we encounter given that we delegate stock selection to third party managers. In doing so, we also delegate voting rights and the execution of those rights. Therefore, assessing the voting practices of our agents is an important part of our process. Our manager research team looks at this across both active and passive mandates; it is also specifically assessed and monitored via our Sustainable Investment reports (see sections 5b and 8, as well as *Figures 5* and *6*). This report tracks and summarises various voting processes, resources and metrics, ultimately assigning a positive, neutral, or negative score on a manager's voting practices.

[redacted]

[redacted]

[redacted]

[redacted]

ii. Directly held equities

Although less common, we do own stocks directly in some instances through managed accounts. It is important to note that Willis Towers Watson still make no underlying stock selection decisions, which continue to be outsourced to third party, best-in-class, specialists. However, as the stocks are under our control, we are able to influence voting more easily than for third party funds above. To ensure managers are voting in the best way possible at every opportunity, we use EOS to provide voting advice to the asset managers. We then regularly monitor the voting decisions each manager makes against what they were advised by EOS, engaging or challenging where necessary.

Related content:

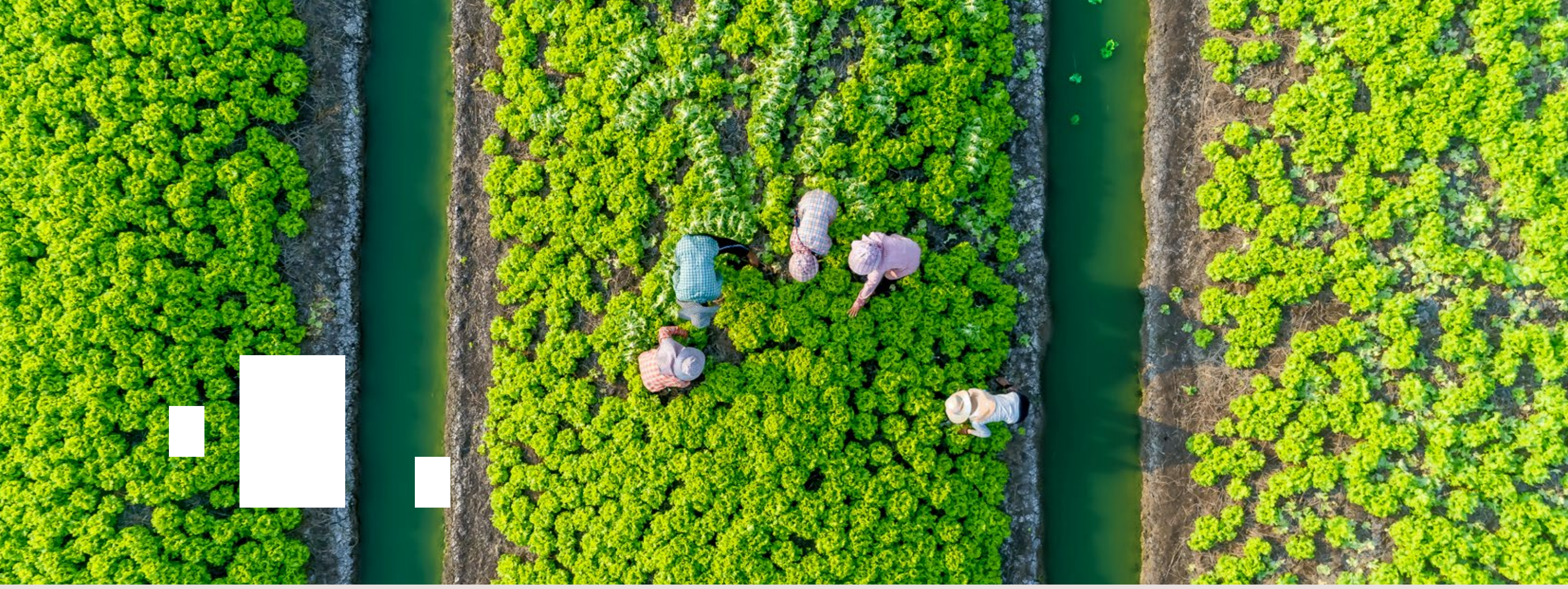
- More information on EOS at Federated Hermes and their voting policies can be found here: www.hermes-investment.com/uki/stewardship/

Where our clients hold managed accounts with direct equities, we review (in addition to reviewing the manager's policies and procedures in the manager research team) the voting procedures mandated under the agreement between the manager and the client on a regular, ongoing basis.

d. Public policy, advocacy and collaboration

We have strong conviction that collaborative engagement and advocacy are important to give the investment industry a stronger voice and improve investment outcomes for all participants. Long-term value creation relies on robust economic and investment markets. As a trusted adviser, we recognise the role we play in the investment chain, believing that undertaking activities to promote resilient and well-functioning economic and investment markets is consistent with our fiduciary duty and with our aim of changing investment for the better. We do this in a number of ways, including engaging in a dialogue with regulators and policymakers and participating in the work of industry bodies and collaborative investor initiatives, to promote high industry standards and effective investment markets.

We also partner with EOS to undertake public engagement and advocacy on our and our clients' behalves. EOS work with policy makers and institutions around the world to better ensure policies and standards are aligned with the interests of investors and best meet the needs of end savers. Some examples of our collaborative initiatives and engagements are shown on page 12, with further details in the appendix.



Examples of our collaborative initiatives and engagements

Thinking Ahead Institute (TAI)

A global not-for-profit innovation hub, which aims to mobilise capital for a sustainable future. Its membership includes over 40 engaged institutional asset owners and service providers committed to changing and improving the investment industry for the benefit of the end saver. More information can be found at: www.thinkingaheadinstitute.org

Willis Research Network (WRN)

A collaboration between academia and our insurance and reinsurance experts, currently working on programs and projects with over 50 science partners worldwide. WRN seeks to integrate public science with the risk management community to enhance our collective ability to understand, evaluate and manage climate risk (including extreme natural catastrophes, climate variability and emerging risks) and to provide credible scientific expertise to improve decision-making across the industry.

Principles for Responsible Investment (PRI)

We are a signatory to the PRI, and further information as well as our annual Transparency Report can be found at www.unpri.org.

UK Stewardship Code

We are a Tier 1 signatory, and we encourage and help our clients to adhere to its guidelines; further information can be found at www.frc.org.uk

The Diversity Project

We are founder members of this investment industry initiative which aims to attract and retain diverse talent in the industry.

Transition Pathway Initiative (TPI)

We are official supporters of this global investor initiative that assesses companies' preparedness for transition to a low-carbon economy. Led by asset owners and academic research from the Grantham Research Institute and London School of Economics, TPI is supported by more than 50 investors globally with combined assets over $16 trillion (as at October 2019).

Institutional Investors Group on Climate Change (IIGCC)

We are members of this investor collaboration with a mission mobilise capital for the low carbon transition, which has more than 190 members, across 15 countries, with over €28 trillion in assets under management (as at October 2019).

Find out more here:

- Tackling sustainability challenges through collaborative initiatives

Thinking Ahead Institute
Willis Towers Watson

Willis Research Network
Willis Towers Watson

Signatory of:
PRI Principles for Responsible Investment

DIVERSITY PROJECT

Transition Pathway Initiative

IIGCC
The Institutional Investors Group on Climate Change

Note: Our relationships with these and other partners can change at any time and certain partner relationships may be replaced or discontinued.

7. Exclusions

We start with the view that having active managers that fully integrate best-in-class sustainability thinking into their process and undertake effective stewardship (voting and engagement) is a better approach than blunt exclusions. However, we also recognise that in mandate design we have sustainability-related responsibilities as decisions in this regard have a significant influence on the real-world impact of the investments we make.

There are instances where we believe that exclusions make sense including the following:

- The mandate is passive or smart beta in nature so there is no active manager applying judgment to increasing risks that were not envisaged at the outset of the mandate
- We believe that the active managers employed are good but not best-in-class on sustainability, potentially due to them having a shorter time horizon than we or our clients have
- For risk management, we want to moderate exposures in one part of our portfolio in order to offset an over-exposure in another part of the portfolio

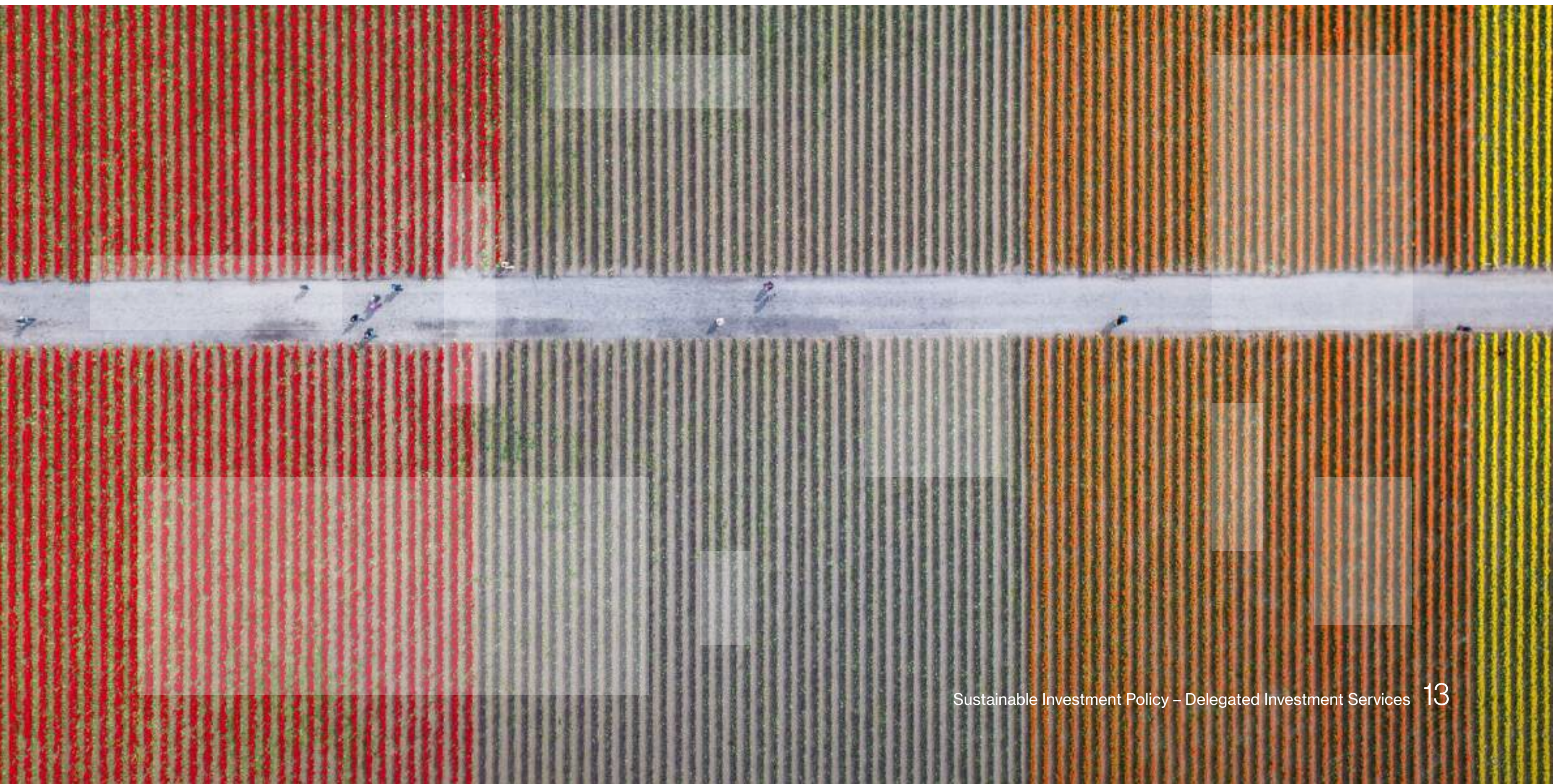
However, we are of the view that exclusions should not be included into a mandate lightly for the following reasons among others:

- They may constrain the ability to engage for positive change, particularly at a security level
- They may have limited positive real-world impact, particularly in secondary markets
- They can only deal with first order effects and often second and third order effects are at least as material, if not more influential in many cases
- It is possible that an exclusion that improves the sustainability/resilience of a portfolio in one aspect reduces the sustainability/resilience of the portfolio in another
- Measuring ESG exposure and risk is inherently difficult and dynamic in nature (for example the extent to which sustainability risks are reflected in market prices, or not)

Exclusions generally fall into three groups:

- Those that represent a licence to operate and do not change materially over time (e.g. where it is illegal to invest in some jurisdictions, where it is common practice in a particular market, or where it has become global best practice)
- Those that we believe would improve the return per unit of risk when risk is considered holistically (generally by mitigating exposure to issues/externalities that may not yet be fully priced in)
- Those that are primarily introduced on moral grounds

We are comfortable, subject to the appropriate analysis, with introducing exclusions in the first two groups (particularly where we believe engagement will have limited impact), but the third group will typically be a client-by-client decision.



8. Monitoring and reporting

Figure 9. **Sustainability monitoring scorecard**

Dimension	Metric	Portfolio score	Benchmark score	Portfolio assessment
Portfolio resilience	Sustainability Risk Exposure Score (absolute)	4.7	4.2	
	Sustainability Risk Exposure Score (relative)	41.9	37.5	
Carbon footprint	Weighted Average Carbon Intensity	136.4	201.1	
Climate impact	Impact on portfolio return of 2°C scenario	-0.1% pa	-0.2% pa	
	Impact on portfolio return of "business as usual" scenario	-0.2% pa	-0.4% pa	
Bottom-up industry exposures	% revenue exposed to top 5 industry climate opportunities	9.1%	8.9%	
	% revenue exposed to top 5 industry climate risks	11.5%	19.9%	
Manager sustainability integration	Areas of strength (% of total)	65%	n/a	
	Areas of weaknesses (% of total)	8%	n/a	

Source: Factset, McKinsey Global Institute, MSCI, Sustainability Accounting Standards Board, Willis Towers Watson

a. Sustainability scorecard

The monitoring undertaken by portfolio managers and researchers forms the basis for our client reporting, noting that reports will often be bespoke to client context.

Key sustainability data for the portfolio is captured and summarised on our sustainability scorecard – an example is shown above. This draws on underlying tools and data sources to give an overall view of a portfolio's sustainability exposures and positioning, which can then feed into our portfolio construction tool to be considered alongside other portfolio quality lenses.

b. Sustainable investment reports

As described in section 5b, we undertake detailed assessments of the sustainability practices of managers in the context of each highly-rated strategy we use in our delegated portfolios. These assessments are summarised in our sustainable investment reports, which are tailored to the asset class and strategy in question, covering ESG integration, engagement and voting (where applicable).

An example report for an equity manager is shown in *Figure 6*. Our research team complete, update and review these reports as appropriate, mindful of both changes to the manager or strategy, as well as evolutions in industry best practices. PMG is responsible for reviewing new manager products before they are available for delegated portfolios, and as part of this, PMG review the sustainable investment reports. On an annual basis, PMG consolidate all the manager sustainable investment reports to review them in their entirety and in a portfolio context.

Manager and portfolio scores are tracked over time looking to see improvement. Any laggards or managers with worsening scores are frequently investigated so the manager can be improved or, if necessary, a replacement sought. As described in sections 5 and 6, engagement with the asset management community is a critical part of what we do to raise standards, help shape the industry for the better, and deliver material benefits for our clients.

c. Sustainable investment product review

Given the oversight PMG has of our investment solutions and portfolios, it naturally sits with this group to monitor products with ESG or SI tilts or screens in them. PMG review a summary of each product annually to ensure each remains fit for purpose and are performing in line with expectations.

d. Review of and interaction with third party providers

Any sustainability-focused advisors or specialist providers for Willis Towers Watson will be formally reviewed at least annually by the team responsible for their appointment, overseen by the Head of Sustainable Investment. When appointing these providers, we conduct market reviews to consider who best fits our requirements. This process is run by the Head of Sustainable Investment, in consultation with (among others) the delegated team and PMG.

e. Policy review

All SI policies will be reviewed and updated at least annually. This policy is owned by the Global CIO, Delegated CIO and PMG, who are responsible for its implementation in delegated portfolios globally.

Appendix

Collaborative initiatives and partnerships

We believe that collaborative initiatives are important to address the critical and underserved sustainability challenges in investment markets, economies, society and the environment.

We are proud to have real expertise on these topics across our company and we use those skills to collaborate with others with the aim of improving long-term outcomes for our clients, and the world they live in. Some highlights of our recent activities and partnerships are listed below:

- **Chartered Financial Analyst (CFA) Institute**
- **EOS at Federated Hermes (EOS)**
- **International Integrated Reporting Council (IIRC)**
- **Principles for Responsible Investment (PRI)**
- **Transition Pathway Initiative (TPI)**
- **UK Stewardship Code**
- **Association of Member Nominated Trustees (AMNT)**
- **1-in-100 initiative**
- **Centre for Risk Studies, Judge Business School**
- **ClimateWise**
- **Global Adaption and Resilience Investment Working Group**
- **Global Assessment Report (GAR)**
- **Global Ecosystem Resilience Facility (GERF)**
- **Global Innovation Lab for Climate Finance**
- **Insurance Development Forum (IDF)**
- **Natural Resource Risk Index**
- **Task Force on Climate-related Financial Disclosures (TCFD)**
- **United Nations Environment Programme Finance Initiative Principles for Sustainable Insurance Initiative (PSI Initiative)**
- **Wharton's Initiatives for Global Environmental Leadership (IGEL)**

Find out more here:

- Tackling sustainability challenges through collaborative initiatives

Signatory of:

Note: Our relationships with these and other partners can change at any time and certain partner relationships may be replaced or discontinued.

Long-term themes

We are long-term investors and we need to consider what may influence the flow of capital over this investment horizon, which we expect to positively skew our return profile (less downside, more upside). We have codified a number of long-term themes which aim to capture the way our world and economies will change. In particular, we partnered with the Principles for Responsible Investment (PRI) to produce the PRI and Willis Towers Watson Investment Institutions Trend Index 2017. The themes and sub-themes identified in this work are shown in *Figure 10*.

The evolution of these themes is expected to affect how the revenue of companies and industries will move. For example, the transition to a low carbon economy will likely cause revenues from oil and coal producers to move towards renewable energy, something we have taken advantage of in a number of our portfolios. Our manager research, asset research and portfolio management teams all use these themes when researching and including new managers and strategies.

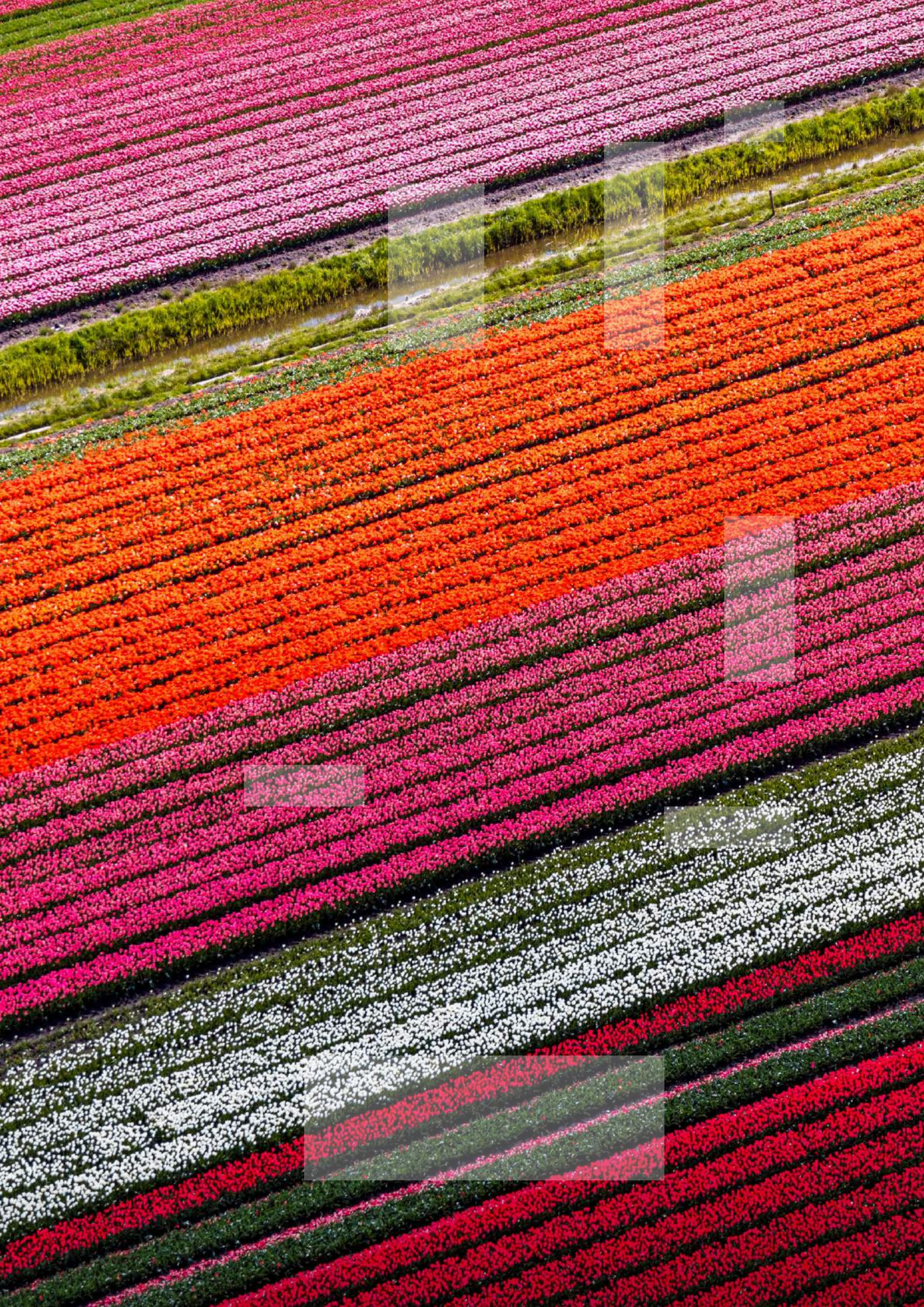
The UN sustainable development goals (UN SDGs) were adopted by 193 countries at the UN Sustainable Development Summit in September 2015, as part of the 2030 Agenda for Sustainable Development. The UN SDGs have become a popular method of assessing a portfolio's impact on the world through the lens of sustainability. The 17 goals are shown in *Figure 11*. The themes identified above are designed to align with and progress many of the SDGs. Delegated portfolios are, where reasonable, mapped to the SDGs, which feed into our thematic thinking and framework when selecting managers, identifying opportunities, and building portfolios.

Figure 10. **Themes and sub-themes that capture future changes in world and economies**

Main themes	Sub-themes
Environmental challenges	Transition to a low carbon economy
	Acute environmental impacts
	Chronic climatic shifts
Societal challenges	Human capital
	Inequality
	Savings
	Public sector finances
	Consumption
Emerging economy growth and dynamism	Urbanisation
	'One Belt One Road' initiative
	EM competitors
	EM consumers
	EM institutions
Technological advances	Cybersecurity
	Digitisation
	Automation
	Fintech
	Biotech

Figure 11. **The United Nations Sustainable Development Goals**

Source: www.globalgoals.org



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