ESG INSIDE
Processes
Advisory
Products

# Our Sustainable Investment Journey 2020

Danske Bank

*"Sustainable investment is an integral part of our ambition to grow and protect our customers' assets. Our journey to bring environmental, social and corporate governance (ESG) inside our investment processes is key to meet our customers' demand for investing sustainably. Integrating ESG helps us make better-informed investment decisions and provide our customers with solutions aimed at delivering competitive, long-term performance."*

Berit Behring
Head of Wealth Management and member of the Executive Leadership Team

# *Content*

# *Welcome to ESG Inside®*

Sustainable investment in Danske Bank is a cornerstone of our fiduciary duty to create value for our clients. When we coined our strategy ESG Inside® two years ago, we started a journey to integrate ESG into our investment processes and products. We have progressed well, and we are still on a journey, as our ambition is sincere and integrating ESG into the core of our business is not a quick fix.

In this second annual report 'Our Sustainable Investment Journey', we share our progress over the past year, and efforts made by our investment teams across the Nordic countries.

Our approach to ESG integration focuses on materiality, which requires access to high quality and reliable ESG data from companies. While companies' ESG disclosures have progressed, and the volumes of ESG data have grown, there are also several white spaces in companies' disclosures. Since we believe that better data will give us better insights and help us to make better investments, we want to support and contribute to how companies can further improve their ESG disclosures to investors. Therefore, in 2019, we analyzed the 100 largest listed Nordic companies' sustainability disclosures and its usability in our investment processes. You can read about our findings and how our portfolio managers contribute to improved disclosure through direct dialogue with companies.

Over the past year, we have strengthened our ESG data platform significantly to cater for different needs in our different portfolios with different philosophies and asset classes. We developed our materiality dashboard mDASH®, which is based on the SASB materiality framework, and provides our investment teams with a tool to assess individual companies.

Our active ownership efforts in 2019, covered dialogue with more than 500 companies in which we addressed more than 100 different ESG topics. It should come as no surprise that issues related to climate change continued to be top of the agenda for companies across sectors and countries, making it a top-priority matter for us from an investment perspective. Indeed, our most discussed topics last year were Green House Gas Emissions and Energy Transformation.

In all we do, we seek to be transparent and clear in our reporting and disclosure. Apart from this annual report, we have launched publications such as our 'Active Ownership Report' and 'Active Ownership Stories, which provide not only the facts and the figures from our dialogue and voting activities but also the more in-depth stories of dialogue carried out by our portfolio managers. In addition, we report $CO_2$ data, carbon footprint, restriction criteria, etc. on individual funds and portfolios.

ESG Inside® our products across our investment strategies have been mapped during the year, in order to provide our clients with a clear description of a fund's specific ESG characteristics, such as ESG Integrated, Restricted, or Thematic. You can read more about this in the report.

Danske Bank's ambition is to embed sustainability in all we do. In 'Our Sustainable Investment Journey' report, I welcome you to learn how we do this in our investment business through ESG Inside® our processes, products, and advisory.

Ulrika Hasselgren
Global Head of Sustainability & Impact Investment
Danske Bank Wealth Management

*"Danske Bank's sustainable investment strategy is called 'ESG Inside®' and is all about bringing sustainability inside our investments. We integrate environmental, social and governance (ESG) factors into our investment processes across strategies and asset classes. "*

Ulrika Hasselgren
Global Head of Sustainability & Impact Investment
Danske Bank Wealth Management

## Introduction:

# *ESG Integration*

Integrating ESG into the investment process is part of our fiduciary duty to achieve the highest and most stable investment return. Therefore, it is essential to identify those environmental, social and governance factors in investment research, security selection, portfolio construction and the decision process that may pose a risk or an opportunity and thereby affect financial performance.

There is no one "best way" or "silver bullet" to integrate ESG. Rather, several approaches are needed in order to be relevant and applicable for each asset class and strategy. To us, ESG Integration means each investment team appropriately identify material financial and ESG factors, assessing the potential impact of these material factors on performance and making investment decisions that consider all material factors, including ESG factors.

A definitive list of ESG issues does not exist, and there is no agreed-upon standard market taxonomy or set of definitions that can be used as a 'true' benchmark. Our investment teams therefore have access to ESG information from multiple data sources. Having access to multiple data sources has for many years been natural when it comes to financial information but is yet to become a market standard for ESG information. During the last year, we have expanded our data platform by including more ESG data and making sure that ESG data is sufficiently integrated into the systems used by our portfolio managers. Today, 76% of our portfolio managers state they have sufficient access to ESG data. However, the development of our ESG data platform is a never-ending process and is expected to continue and intensify over the next few years due to new EU regulations on sustainable investments.

The financial sector has so far failed to achieve consensus on just what constitutes material ESG issues for each sector and company. This complicates the picture for investors, as it makes it difficult to assess our holdings. To address this, we have partnered with the Sustainability Accounting Standards Board (SASB) to leverage their research knowledge on financial materiality. SASB focuses on identifying the nonfinancial issues and metrics that are most likely to impact financial performance – which is central to our ESG Integration process. This framework has also been leveraged in the development of our Materiality Dashboard, mDASH®, a tool that 50% of our portfolio managers (PMs) use.

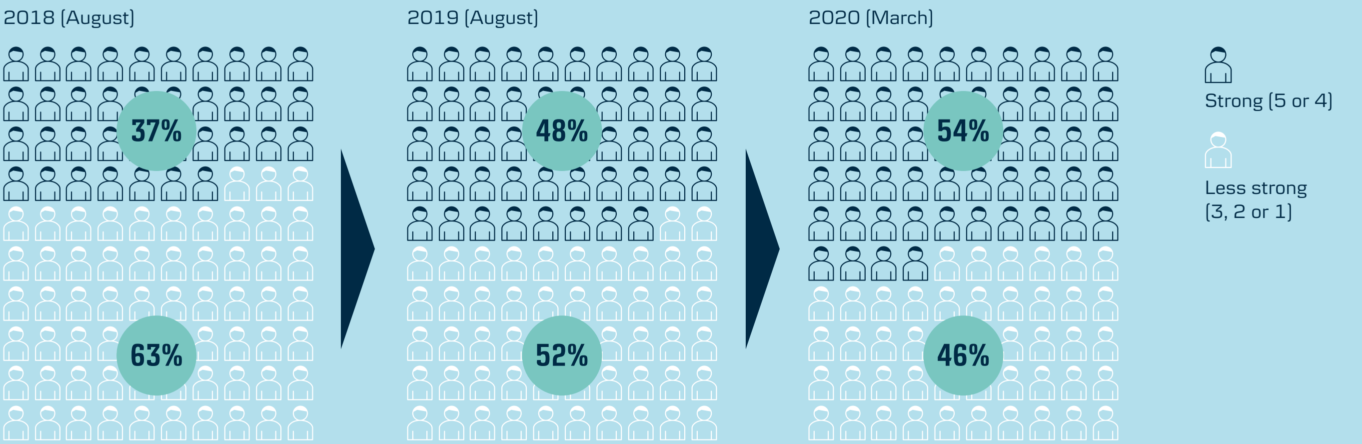
The strength of this bottom-up approach is that our solid foundation of data, tools and resources enables the investment teams to integrate ESG in a meaningful way.

# KPIs and self-assessments

Sharing details on progress and activities means we receive continual feedback for making improvements and peer-benchmarking our approach as well as strengthening internal processes and capacity building. Our portfolio managers (PMs) therefore conduct a self-assessment survey twice a year.

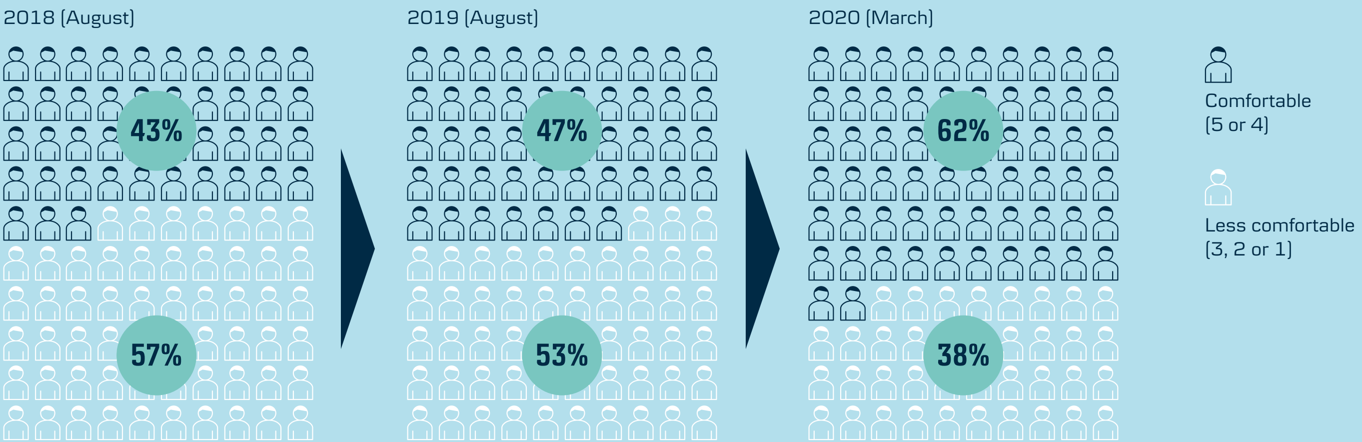
We have set the ambitious goal that 100% of our PMs should be able to tell their ESG integration story by the end of 2020. The latest survey conducted in March 2020 concluded that 96% of our PMs integrate ESG into their investment process, indicating that ESG integration is part of the everyday work of our investment organisation. The perceived strength of the ESG approach has also increased among the investment teams from 37% in 2018, to 48% in 2019 and 54% in March 2020.

## Strength of ESG intergration approach




Portfolio managers' comfort in describing their ESG approach has improved from 43% in 2018 to 62% now.

## PMs level of comfort in describing their ESG approch




Continuing to track these numbers is important, as work is being done to strengthen the ESG data platform, provide better day-to-day support on ESG issues and ramp up education and training as well as make internal and external expertise and support more readily available.

Another goal is to make a long-term contribution to improving the quality of ESG data and corporate disclosure of material sustainability/ESG information for Nordic companies. We firmly believe that better data will provide better insight, which in turn will facilitate better-informed investment decisions. We are therefore establishing initiatives and KPIs to address this topic.


# *In search of quality ESG data*

We believe that incorporating ESG matters into our investment processes is and should always be about investing. We say that ESG issues should be considered as factors along with financial factors, that our investment teams should treat them holistically, and manage them from a risk and-return perspective to support better-informed investment decisions.

Whether your preferred method of ESG integration is more quantitatively or qualitatively oriented, integration of ESG matters is heavily data dependent and requires access to high quality and reliable ESG data. The market for ESG data has grown exponentially over the past 10 years, underling the growing demand but also the non-standardized and chaotic nature characterizing this data.

Today the sources of ESG data are more diversified than ever and one area of particular interest is data reported directly by companies. Investors are increasingly paying attention to companies' sustainability disclosures both to figure out if companies are running their business with the future in mind and to assess how environmental, social, and corporate governance (ESG) issues could affect financial performance.

Companies have undoubtedly noted the attention as well. While communication of ESG risks to key stakeholders is not new, efforts have become more ambitious, driven not only by investor demand but also by regulation and the growing societal expectations.

To get a better understanding and support the furthering of standardized ESG disclosure from companies, Danske Bank decided to analyse the usability of companies' sustainability disclosures in our investment processes. We looked in-depth at the 100 largest listed Nordic companies' reported ESG data in 2018, and our research showed several white spaces in the companies' disclosures.

These findings have been presented and discussed in the whitepaper "In search of quality ESG data – An investment view on corporate sustainability disclosures". We bring here the most important conclusions from this study in a condensed version and refer to the white paper for more details in terms of data and numbers.

Exhibit 1 gives the overview in terms of number of data points and

## Top 100 Nordic listed companies

| | Total | Denmark | Finland | Norway | Sweden |
|---|---|---|---|---|---|
| Reports analyed | 100 | 22 | 17 | 14 | 46 |
| Data points | 20,790 | 2368 | 5501 | 3434 | 9487 |
| Average data points | 207,9 | 10,7,64 | 323,59 | 228,93 | 206,24 |
| Enviromental data points | 36% | 35% | 33% | 29% | 40% |
| Social data points | 47% | 48% | 49% | 55% | 43% |
| Governance data points | 17% | 17% | 18% | 16% | 17% |

*Source: Top 100 Nordic listed companies' sustainability reports, annual reposts, integrated reports, ect.*

focus area for the four Nordic markets covered in the study.

The main challenge with sustainability disclosures is that companies have significant leeway in terms of what they report on and how to calculate it. Sustainability disclosures are still largely voluntary, and companies can align themselves with any number of reporting initiatives, depending on their appetite and which stakeholders they prioritize.

This can be contrasted by companies' reporting of financial data, where history, regulations and international standards all have played their part in creating an ecosystem that allows for direct comparisons of data across companies, sectors, and geographic areas.

Nordic companies have been early adopters of reporting frameworks, and have established a good reporting structure. 80% of our research sample is aligned with at least one reporting initiative. While the ambition is good, it has created a legacy of focusing on environmental and social materiality rather than financial materiality. The choice of reporting initiative has thus had a large effect on what is being disclosed. This, combined with the use of many different reporting practices, leaves us as investors with the task of wading through troves of irreconcilable data.

Based on our research we have identified four criteria in support of investment-relevant sustainability disclosure. We will start by looking at the following three criteria:

1. **Comparability:**
   Data that is comparable across companies and industries.
2. **Accessibility:**
   Data that is accessible to investors in different formats.
3. **Reliability:**
   Data that has high quality assurance.

Comparability:

# *Data that is comparable across companies and industries*

While both depth and breadth of available sustainability data have increased over the years, intercompany comparability remains elusive. Our analysis shows that comparability of data is impeded due to three main reasons. First, specific disclosure items are to a large extent company specific. In practice, this means that we are not able to compare companies simply because other companies do not report on the same topics – even for companies within the same sector and industry. Across our research sample, this is the most pressing issue and reduces our comparable dataset by half on average.

Secondly, even when companies report on the same sustainability topics, comparisons are not possible as data is fraught with scope mismatches. This reduced our comparable dataset by 37% on average, as data is either too generic or too specific, to lend itself to comparison.

Thirdly, our research shows a lack of methodological transparency and alignment between companies. There is a large variation between how companies measure variables.

Ultimately, it is an issue of complexity. With so many different reporting initiatives, most of which are largely unaligned on both scope and purpose of reporting, the complexity of the reporting landscape compounds the comparability issue. Hence, it is not surprising that companies produce sustainability disclosures that do not add up. In order to integrate sustainability data into our investment processes and decision-making, we need reliable data for broad comparisons. One minor consolation is that comparability can increase, partly facilitated by third-party data providers.

This comes, however, at the expense of accuracy as third-party data usually rely on subjective methodologies and extensive estimation to cover missing data fields. Moreover, third-party data providers can actually compound the focus on the wrong issues, as their focus historically have not been on financial materiality. Companies, seeking good scores from rating agencies, have been driven towards excessive reporting simply not to become penalized in the scoring process.

Accessibility:

# *Data that is accessible to investors in different formats*

While many questions can be raised about the quality of sustainability data, one main challenge with deploying it concerns its accessibility. In order to integrate companies' sustainability data, the actual data sourcing needs to be instantaneous. Currently, companies' self-disclosed data is only accessible  if investors go to search for and collect it.

This is partly due to the multi-purpose of disclosures. Companies tend to use sustainability disclosures as a marketing platform, and to provide a narrative targeting several audiences and stakeholders. Instead, companies should clarify the purpose of its sustainability disclosure and distinguish between financially material disclosure and society material disclosure.

This has implications for us, as it drives the need to use third-party data providers, who play an important role in plugging the accessibility gap, while at the same time it comes with the caveat that data points are based on estimates. The validity of this data is thus contingent on the estimation methodology, something that several data service providers have been reluctant to show. This means that while they can help solve the accessibility issues, they also help confound the intrinsic quality issue.


### Reliability:

# *Data that has high quality assurance*

Ultimately, for data to be usable in an investment context it needs to be reliable. Our investment decisions needs to be firmly anchored in a conviction that the reported sustainability numbers actually reflect what is going on in a company.

Our research shows that few companies use third-party assurance as a means to provide investors with signals of credibility. Looking outside of the Nordic region, this is certainly the case. Only 3% of U.S. companies had full assurance of sustainability reports and 36% had partial assurance[1]. Applying the same lens to a Nordic context, it is evident that companies go further in terms of providing transparency through assurance: 31% of Nordic companies offered full-assurance of their sustainability reports and 34% had partial assurance. While this represents significant steps in the right direction, we encourage companies to go further in bolstering the reliability of their disclosures. Out of the 31 companies that offer "full assurance", 23 companies lacked quality of the assurance statement, e.g., no statement of competency and responsibility of the assuror and no references to assurance standards.

While the question of how, and whether, companies make use of third-party assurance is relevant, it only scratches the surface of the real issue. For companies' sustainability disclosures to carry weight they need to be anchored in sound governance and management and performance measurement systems. To that end, assurance standards play a significant part in helping us gain insights. Companies with high quality assurance will often use assurance standards geared specifically at sustainability disclosures and their underlying processes and management systems."[2]

*[1] Si2 and IRRC Institute: State of Sustainability and Integrated Reporting 2018*
*[2] Assurance based both on a combination of AA1000 and ISAE 3000 are likely to deliver enhanced results and are technically complementary*

# *Incorporating carbon footprint data to make better investment decisions*

Lars Erik Moen,
Portfolio Manager and Head of Norwegian Equities, Oslo

Assessing climate-related risk is an important part of the investment process, says portfolio manager Lars Erik Moen. By tracking a company's carbon footprint, he can mitigate the risk of a company not being priced correctly according to the climate challenges it faces. However, lack of carbon data poses a huge challenge.

"We expect there will be stricter sustainability demands on companies in the future. This will likely have a significant impact on the companies' business models and financial performance," says Lars Erik Moen, Head of Norwegian Equities. Together with his team, he spends a great deal of time evaluating and analysing the carbon footprint of the companies they invest in. Lars Erik believes the national and international focus on reducing the impact of climate change is creating new types of risk for companies that they need to address and manage. Identifying these risks is important as they can influence a company's return potential and licence to operate.

"The transition to a low-carbon economy brings with it numerous new challenges for companies, including complying with stricter sustainability requirements from governments and a growing consumer demand for green solutions. Simply put, if companies do not transform their businesses and embrace the green agenda, they will probably not be attractive investment cases for us in the long run," explains Lars Erik Moen.

He stresses that the extensive focus on climate issues is part of his efforts to safeguard and future-proof the investments and returns of Danske Bank's customers.

**Holistic understanding of risks and opportunities**

In his view, the market focuses too narrowly on companies' direct emissions from the burning of fossil fuels (Scope 1 emissions) and indirect emissions generated by the electricity purchased and consumed by companies (Scope 2 emissions). As a consequence of focusing only on Scope 1 and 2 emissions, aluminium company Norsk Hydro and solar energy company REC Group have higher carbon emissions than oil companies. That is why the Lars Erik Moen also includes Scope 3 emissions in his analysis. This provides him with a more complete picture of a company's associated risks and exposure to the climate agenda. Scope 3 emissions include emissions from a company's suppliers as well as the consumers of its products and services (i.e., upstream and downstream activities). These indirect emissions often represent the largest portion of a company's carbon footprint, and in some cases account for as much as 90% of a company's total emissions.

"By considering all three emission scopes, we can capture all risks and opportunities throughout the company's value chain and gain a better understanding of its climate and environmental impact. This approach enables us to conduct a holistic analysis of how companies might be subject to future regulations and changes in consumer behaviour that could influence their business models and future return potential for Danske Bank's customers," notes Lars Erik Moen.

By way of example, he points out that the carbon footprint of oil companies is much larger when including Scope 3, as this also encompasses the emissions created from using their products. Furthermore, including the Scope 3 emissions of shipping companies, for example, means their emission data are unaffected by whether the company owns or leases their vessels.

**Huge need for assessments and calculations**

Access to quality greenhouse gas emission data is limited, and far from all Norwegian companies publicly disclose such data. In fact, only about 30 percent of companies listed on the Norwegian stock exchange report carbon emissions and most of them do not include Scope 3 emissions. Hence, the Norwegian equity team has to perform its own calculations and assessments of Scope 1, 2 and 3 emissions.

"Measuring a company's carbon footprint may seem straightforward, but in practice the calculation can be tricky. Sometimes, it is easier to determine a company's earnings for next year than to calculate last year's carbon footprint. Furthermore, when you have a portfolio of companies where services or products can be interlinked, you run the risk of double counting when calculating a company's carbon footprint,' says Lars Erik Moen.

He points out that although the team has to employ a number of assumptions and estimates, he still believes detailed carbon analyses are important for understanding the consequences of expected increased carbon taxation, etc. for companies. It provides him with more objective measures for evaluating how far a company or sector has progressed in the green transition and of its efforts to address climate-related risks and opportunities.

**Constantly improving the investment process**

The ongoing shift to a green economy will likely transform whole sectors and business models and set out entirely new roadmaps for creating viable business growth. This trend underlines the importance for investors to have access to quality emission data, explains Lars Erik Moen, as robust sustainability data are needed to make the best possible investments.

"When a company pledges to cut its emissions, we have to consider what exactly is being counted and whether all scopes are included. Hopefully, we will see more and more companies increase the transparency of their climate impact across all scopes. I support initiatives like the Task Force on Climate-Related Financial Disclosures, that encourages companies to publish details and data on their climate-related risks," says Lars Erik Moen.

He emphasises that the method for utilising carbon data as a way of assessing and identifying investment risks and opportunities is constantly improving, thus supporting better-informed investment decisions for the benefit of Danske Bank's customers.

## What are Scope 1, 2 and 3 carbon emissions?

The so called Scope framework was introduced by the World Resources Institute and World Business Council for Sustainable Development as part of their Greenhouse Gas Protocol Corporate Accounting and Reporting Standard back in 2001 focusing on Scope 1 and 2, and with Scope 3 as optional. The goal was to create a universal method for companies to measure and report the emissions associated with their business. The three scopes allow companies to differentiate between what they emit directly into the air, which they have the most control over, and the emissions they contribute to indirectly.

### Scope 1

Scope 1 emissions are direct carbon emissions from sources that are owned or controlled by the company. These include manufacturing and process emissions, onsite fuel combustion and emissions from company vehicles.

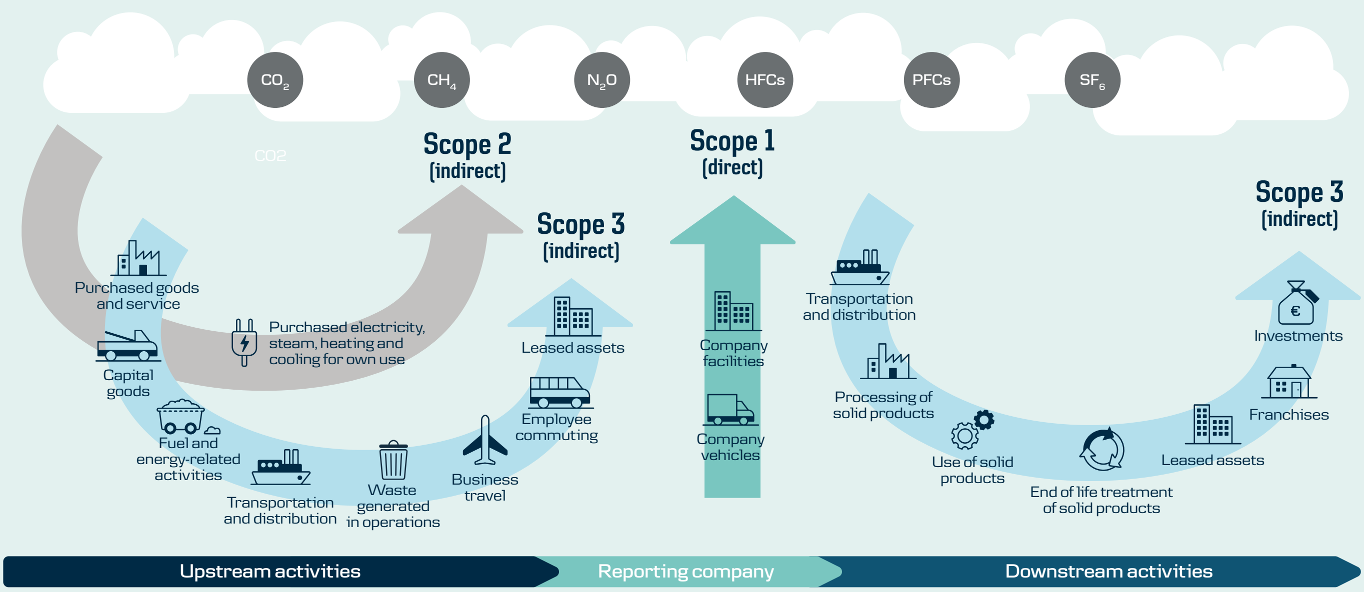
### Scope 2

Scope 2 emissions are indirect emissions from the use of energy that the company buys, such as electricity, heating or cooling, and steam.

### Scope 3

Scope 3 emissions are all the indirect greenhouse gas emissions not captured by Scope 1 and 2 reporting. Also known as value-chain emissions, they include emissions from the company's suppliers as well as the consumers of their products or services.

GHG Protocol scopes and emissions across the value chain



# *Sustainability data from across the value chain*

Emelie Aulik,
Senior Portfolio Manager, Swedish Fixed Income, Stockholm

For a long time, Senior Portfolio Manager Emelie Aulik has followed and analysed Swedish property companies, which, from the point of view of sustainability, can be said to be at the forefront in terms of energy efficiency. At the same time, however, they still have a lot of work to do when it comes to reporting.

The Swedish construction and property industries account for almost 40% of energy use in Sweden and for about 20% of the country's carbon dioxide emissions. Translating a major political focus on climate into more regulations and tougher climate-related requirements places high demands on the industry to reduce its climate impact and find ways to maintain its appeal to investors in future. As is always the case when a sector or industry undergoes rapid change, there are big profits to be made for those who act quickly and intelligently.

I note that most property companies have made great improvements in terms of energy use; most have

completely or partly switched to climate-neutral heating and electricity supply. Wallenstam is an example: it builds its own wind turbines and solar parks to supply its properties with electricity. In this context, it is important to understand that the rapid change we are seeing is largely linked to the increases in profitability it generates. Compared to other types of companies, property companies' investments in energy-efficient improvements can mean a more immediate and felt impact in the form of increased profitability and stronger cash flow. This is one of the reasons why the property industry accounts for a significant proportion of the green bonds being issued, with the proceeds being used for various types of environmental projects. This may include, for example, the expansion of wind turbines, environmentally certified new-build and rebuild projects, or other climate-related adaptations to properties.

But with these initiatives comes an increased creativity in terms of reporting. Many companies wish to excel, and new ESG data points are quickly emerging and being presented in a nice-looking and appealing way. However, the overall picture quickly becomes rather fragmented and somewhat chaotic: in an attempt to appear to be sustainability champions, companies not only lose sight of the opportunity to make relevant comparisons across the industry; other, more complicated, difficult-to-access areas, important to us as investors, are left out.

The industry's focus on sustainability is largely a focus on energy use and certification of existing properties. Energy management of the property portfolio is a real priority in itself, but it needs to be supplemented by sustainability assessments at supplier level and life-cycle analyses of buildings. An interesting fact in this context is that, in the annual surveys of different industries' sustainability insights conducted by SB Insights,[1] the property industry ends up at the bottom year after year. Here, most attention is paid to a lack of focus on sustainability in connection with purchases. Few of the property companies we have analysed have any substantial understanding of their suppliers, nor are they interested in the life-cycle perspective; instead, they exclusively focus on keeping costs down. A lot of the talk around sustainability suddenly seems empty and hollow, which is a problem,

> *Energy management of the property portfolio is a real priority in itself, but it needs to be supplemented by sustainability assessments at supplier level and life-cycle analyses of buildings.*

not least in the longer term. Building materials such as cement and concrete account for most of the industry's emissions, and so we believe that construction itself will be the biggest sustainability challenge for property companies in the future. Most emissions thus fall into what is called Scope 3, i.e. emissions resulting from companies' construction activities, with actual emissions occurring on other parties' sites. In light of the increased regulation, both today and in the future, we believe that companies exercise no control or even have a grasp of this particular area, which will grow in importance. Using more sustainable materials in construction will, we believe, increasingly pay off and we generally think that companies should start this transition process as soon as possible.

> *It is of interest to note how property companies, while reporting and, in some cases, over-reporting on their sustainability efforts, continue to overlook basic areas that we investors consider relevant.*

Looking at the situation from a broader perspective, it is of interest to note how property companies, while reporting and, in some cases, over-reporting on their sustainability efforts, continue to overlook basic areas that we investors consider relevant. For example, only Vasakronan has estimates for emissions within Scope 3. Property companies have complicated value chains, at least if you look at the rear end of the chain, where several thousand subcontractors are often found. We understand that it is generally difficult to keep track of everyone but we firmly believe that this will be required. Property companies must take the entire value chain into account – at present, it seems that they are not doing so. Any company that comes up with sound and efficient solutions in this area will soon, we believe, be able to stand out from the competition. Essentially, such companies will meet future expectations of both the market and legislation. Reporting relevant data and making it available to us as investors is an important part of this mapping exercise. Here, we will be looking for substance and relevant data points and we will highlight the need to obtain these when talking to companies.

[1] *https://www.sb-index.com/*

# *The private equity view on ESG integration*

Claus Heimann Larsen
Head of Danske Private Equity, Copenhagen

As head of Danske Private Equity, Claus Heimann Larsen has first-hand experience of working with ESG matters. Together with his team, Claus reviews and analyses hundreds of investment opportunities every year. Seen from an ESG data perspective, he actually thinks the private equity business has a golden opportunity not to repeat some of the mistakes committed by listed companies in recent years.

"We are in the business to make money for our clients and in that process we are very focused on ESG because it is a way for us to think investments. We have integrated ESG into our investment process, so that it's now a central part of what we do."

**Good business**
Claus Heimann Larsen is firmly committed to his fiduciary duty. With a long career in the world of private equity, Claus has seen many good investment opportunities that he is now able to sort under a number of ESG factors.

"ESG mapping or not, this is something that I have done for a long time. Whether done implicitly or explicitly, taking ESG considerations into account is simply good business. What we have now is an ecosystem and a taxonomy that helps investors communicate more directly and clearly about these issues – but that doesn't change the fact that it still made sense to look at ESG factors 20 years ago."

"

*Whether done implicitly or explicitly, taking ESG considerations into account is simply good business*

Claus also points to the robustness and systematic approaches to ESG as another aspect enabled by the emerging ESG ecosystem. In doing so he also quickly identifies a clear dividing line between listed and private equity:

"The private equity market is definitely different to the public market. Less regulation is an obvious difference, which means a greater diversity in terms of investment opportunities and best practices. Companies in the private space have a greater degree of freedom and can to a greater extent pursue their own interests, so to speak. Moreover, we are in a business where we take relatively few investment decisions every year. We do not make final investment decisions every hour or every day, and sometimes a month can go by without any final decisions being made. In other words, we have time to think and time to assess the opportunities from a qualitative perspective."

**Qualitative approach**
The word "qualitative" is key here, since there is generally low coverage of unlisted companies by external ESG

data vendors. Unless you get data directly from your investee or portfolio companies, investors are left with a qualitative approach.

"Our ESG approach is definitely more qualitatively anchored. We are in close dialogue with the private equity managers taking the investment decisions, methodically asking them how they think and apply ESG. We use our due diligence processes to uncover ESG aspects when committing capital to private equity funds, but also when investing directly in companies. The process consists of eight different steps, and apart from meeting the investment teams we also meet the portfolio companies, perform portfolio analysis, conduct legal and risk reviews, etc. We do not have an explicit ESG step as part of this process, rather the ESG analysis is integrated into each of the eight steps. This means that we cover a lot of ground in our fundamental analysis of a given fund or direct investment, and ESG is included throughout the process."

**Data needs to be relevant**

Claus Heimann Larsen has some specific views on ESG data reported in a private equity context.

> *Whereas I will always welcome more ESG data, I would rather not have the market flooded with irrelevant or non-material ESG data that is of little value from an investment point of view*

"Again, I see some significant differences when comparing listed and private equity companies, and this also applies to ESG data. To me, the chaotic situation with listed companies overreporting on ESG data reminds me of the less regulated world of private equity. In a way, I am glad that the private equity space has not reached that level of creativeness yet, as I know a lot of the ESG data from listed companies is quite useless for investors. Hence, these early days for ESG reporting in the private equity space actually come with a golden opportunity for privately held companies to learn the lesson: Whereas I will always welcome more ESG data, I would rather not have the market flooded with irrelevant or non-material ESG data that is of little value from an investment point of view."

Some private equity funds are further ahead when it comes to ESG reporting. The most advanced private equity funds cover their portfolio companies with dedicated ESG reports.

"We encourage this and push them to do it as best we can. With regard to maximising value on exit, academic research has shown that a strong ESG story can make a significant difference. That said, the story needs to be anchored in material ESG aspects. The private equity world is highly professional, with investors looking for facts, aspects or perspectives that can help them understand a potential investment opportunity. I see room for improvement and also see good opportunities for players that report on material ESG matters in a smart and accessible way. I definitely expect us to take more ownership in terms of pushing for the right ESG data and reporting in the future – following the impact investing approach, if you will," concludes Claus Heimann Larsen.

**Financial materiality:**

# *Data that reflects what is important for the company*

To support the furthering of standardized ESG disclosure from companies, Danske Bank decided to analyse the usability of companies' sustainability disclosures in our investment processes. Here, we look at the last and perhaps most important criteria identified in the study of 100 largest listed Nordic companies' ESG reporting: the lack of financial materiality.

While companies provide an abundance of sustainability-related information, less than one-third is financially material according to our research and the SASB (Sustainability Accounting Standards Board) Materiality-map.[1] In other words, the vast majority of reported information will not tell us much about how value is created.

While the remaining one-third that covers material data could still be enough, it is concerning that only 17% of the companies in our sample have full coverage of the topics that could affect their financial performance. This is a challenge, as the remaining 83% have white spaces, leaving us blindsided to how they may be exposed to key sustainability issues.

While companies on average underreport on financial materiality, some stand out on a sector basis. Companies in sectors such as Extractives & Minerals processing and Renewable Resources have a long-standing dialogue with investors around their material ESG risks, which is usually core to understanding the business case.

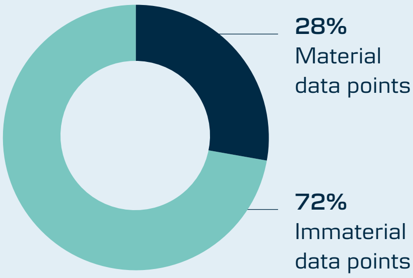
Conversely, some sectors stand out for their underreporting. These include the Financial and Health Care sectors. Particularly, these sectors have risk exposures in the social capital and governance areas where we find disclosures wanting. These areas merit consideration from both a business and social equity point of view, as they span as diverse as Data security & privacy, Competitive behaviour, and Systemic risk management practices.

Fortunately, several companies are showing signs of adopting the concept of financial materiality. 62% of companies did their own materiality assessments during 2018. While it can be challenging to understand companies' internal assessments – few companies have adopted a common taxonomy – we found evidence that companies undertaking such assessments showed signs of increasing relevance of data for investors. It is likely that companies that go through the process of interlinking financial performance and sustainability are better at reporting on topics relevant to investors. Indeed, average coverage of financial materiality was 14 percentage points higher for companies who conducted a materiality assessment than for those who did not.

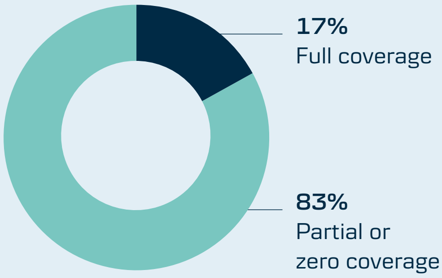
[1] *https://www.sasb.org/standards-overview/materiality-map/*

### Share and scope of financially material ESG data point

**Share of reportet material ESG data points**
Percent, 100% = 20,790 data point




**Scoe of material ESG data ponits**
Percent, 100% = 100 companies




### Financial materiality:

# *Our approach to materiality*

Danske Bank is committed to embed sustainability into the core of its business. As an investor and manager of our customers' assets and savings, we are committed to building robust investment processes and take ownership of our ESG assessments, focus on materiality, i.e., what is business-critical, engage with portfolio companies to address the data challenge, and encourage the furthering of standardized and auditable reporting. This will give us better data and insights, which will help us make better-informed investments.

We have engaged in a partnership with Sustainability Accounting Standards Board (SASB) to leverage their research knowledge on financial materiality. SASB has in our view emerged as one the most credible and promising international frameworks focusing on identifying those non-financial corporate topics and metrics that are most likely to impact financial performance.

To execute on our commitment, we have developed our own proprietary materiality dashboard called mDASH®, which is used by our investment teams to assess and evaluate companies' sustainability performance and standards in a holistic manner.

- mDASH® is based on the SASB Materiality-map, which guides our understanding of – on industry level – which ESG factors may financially impact companies we invest in.
- mDASH® makes available a large set of externally sourced data points from companies and third-party data providers, structured and categorized to help cut through the information noise by identifying financially material ESG topics against which companies can be assessed.
- mDASH® collates company dialogue data, which calibrates our evaluation and highlights progress and outstanding material issues for us to address with the companies we invest in.
- For each company covered by mDASH®, a propriety materiality score, mSCORE® is produced that combines the SASB Materiality framework with weighted average of a selected range of ESG risk score from some of the leading data providers
- The key principle of the mSCORE® methodology is hence the separation of materiality assessment and source data assessment. This allows for an agile and non-biased adjustment of methodology on a continuous basis, something we believe to be of extra value given the dynamic environment surrounding the field of sustainable investments.
- Given the fact that ESG disclosure is not standardised nor mandatory, there is certain degree of disclosure bias; companies have a tendency to focus on reporting on those ESG issues they perform well on. mSCORE® attempts to mitigate this challenge by identifying leading data sources from different angles, effectively complementing each other.

# *Cutting through the data noise with mDASH®*

Kasper Brix-Andersen
Chief Portfolio Manager and Head of Fundamental Equities, Copenhagen

Chief Portfolio Manager Kasper Brix-Andersen uses mDASH® to cut through the noise from ESG rating agencies and identify the ESG factors that are important for a company's business model. This helps him and his team produce more nuanced research and assess the quality of a company.

The team follows a strict investment process when selecting companies including a fundamental analysis of a company with a focus on quality, potential and valuation. A company's approach to ESG can be one of the factors that makes a company an even better investment case, as it can enhance quality, improve the potential and/or make the valuation more attractive. Hence, analysing ESG issues is a natural aspect of the investment process for Kasper Brix-Andersen and the rest of the European equity team.

"We are constantly on the lookout for investment cases where several important factors come together in one attractive whole. We generally look for companies of high quality that have an attractive and value-creating business model, and which are undervalued by the equity market," explains Kasper Brix-Andersen.

ESG is a natural aspect of the fundamental research process and provides Kasper Brix-Andersen with new perspectives and angles on companies that are often not covered by traditional investment analyses. This produces a fuller picture of each company and provides the team with an improved basis for decision-making. Danske Bank's proprietary ESG research tool, mDASH®, plays a vital part of the team's investment process, as it helps them to identify themes and focus on the crux of relevant ESG factors for a particular company.

**Cutting through the noise with mDASH®**

There are plenty of agencies that rate a company's ESG work. The challenge, though, is that the agencies tend to differ in their evaluations of each company and often focus on different aspects. Moreover, the agencies' ESG information is not always up-to-date, or they may lack key information, as the agencies often do not work closely with the companies.

"mDASH® creates considerable value for us as portfolio managers, as we can separate out ESG factors with investment value from non-material ESG factors and at the same time cut through the noise from the agencies' diverging analyses of the same company. With mDASH® we have defined for ourselves the key ESG factors from an investment perspective, and we can zoom in on the ESG factors that are material for each company," explains Kasper Brix-Andersen, who adds:

"Instead, we have taken ownership of the ESG analysis with our materiality dashboard also known as mDASH®. We can quite precisely identify the factors that we believe play a key role

”

*We generally look for companies of high quality that have an attractive and value-creating business model, and which are undervalued by the equity market,* for the company's financial situation and future value creation, such as data security, green transition, business ethics or work safety. We then dive into how an individual company handles these relevant factors and what they are doing to improve. Finally, we can use it in our dialogue with the company's management."

Kasper Brix-Andersen points out that he applies a materiality perspective to identify potential ESG risks where the company, for example, does not manage climate, corruption, or product quality issues satisfactorily which can comprise a business risk. He also uses the materiality to identify companies' ambition and potential to improve in the ESG area and thus perhaps become an attractive investment case.

> *We have taken ownership of the ESG analysis with our materiality dashboard also known as mDASH®*

**Dialogue with companies on material ESG issues**

After obtaining detailed knowledge on business-relevant ESG issues from mDASH®, the team can have a better and deeper dialogue with companies, says Kasper Brix-Andersen. For example, the team can discuss specific measures that could boost the company's ESG efforts and create further growth and development.

"We know the key ESG issues for each company and through dialogue with management we can dig deeper and become better acquainted with their strategy. We can cross-check whether our analysis and view of the company are accurate and, in that way, get a more nuanced picture of the company's strategic considerations. We incorporate this input into our investment analysis and consider it when selecting companies," explains Kasper Brix-Andersen.

> *We can cross-check whether our analysis and view of the company are accurate and, in that way, get a more nuanced picture of the company's strategic considerations*


# *A quantitative view on ESG integration*

Ville Kivipelto
Senior Portfolio Manager, Alpha Finland, Helsinki.

A healthy dose of scepticism and caution is necessary when you work with ESG integration in a quant portfolio – at least if you ask Senior Portfolio Manager Ville Kivipelto.

Integrating ESG into actively managed portfolios presents many challenges. An obvious one is how to navigate the chaotic landscape of company-reported ESG data, as described earlier in this publication. Another obvious challenge is the materiality focus, whereby you as a portfolio manager constantly have to separate noise from the data that matters for a company's long-term financial performance.

**Focus on value creation**
If you are a quant manager, you can add an extra dimension to your ESG integration efforts: your ESG assessment needs to end up as some kind of quantitative score that can go into your model. You can perform all kinds of qualitative assessments along the way, but in the end you need to find the score that should be included in your model. So when your overarching goal is to optimise your portfolio to maximise expected return, how do you incorporate ESG into the model when the data a) lacks history, b) arguably has some quality issues, and c) is under constant development and change?

> *Many companies that in my opinion should have low scores are scoring well – and the same is true the other way round. The scores seem to say more about the company's ESG reporting than anything about the underlying quality.*

You start and try to work your way forward while at the same time focusing on your fundamental task: to create attractive return for your clients – at least, that is Ville Kivipelto's view. Ville Kivipelto is a quant portfolio manager and part of Danske Bank Asset Management's investment team in Helsinki.

**Understand the different methodologies**

"I am generally a bit sceptical when it comes to ESG scores. Many companies that in my opinion should have low scores are scoring well – and the same is true the other way round. The scores seem to say more about the company's ESG reporting than anything about the underlying quality. I appreciate that the models calculating the scores can be more, or less, sophisticated – and in a way you get what you ask for. This is why it is absolutely necessary to have internal research capabilities that truly understand the different vendors and their methodologies."

The quality problem represents a bigger issue, according to Ville Kivipelto.

"Generally speaking, I do not yet view it as an alpha source and hence I am sceptical about whether you will find attractive risk premia in ESG data. The other data that goes into my model, e.g. high dividend yield, strong balance sheet, high quality, and attractive growth are characteristics that historically are linked to strong operative performance and attractive stock performance. Whereas I can find academic research reinforcing the link between many of these factors and outperformance on the stock market, I do not find that in the same significant and consistent way when it comes to ESG data – or to put it differently: seen from my perspective and given my quant context, there are no reliable studies showing how to use ESG to create outperformance."

Ville Kivipelto is not easily drawn to compelling story telling or nicely wrapped messages. Instead, he seeks facts and more specifically facts that can help him in his responsibility as a portfolio manager.

"I have a fantastic job with a great deal of responsibility. Whatever I do professionally needs to be fully anchored in my pursuit for attractive and competitive risk-adjusted return in the long run. I cannot afford to play around with clients' money just because there is suddenly a lot of data available and a bunch of people talking about ESG."

**mSCORE® as a quality parameter**

So how did you find your way into sustainable investments?

"It all started when I got introduced to our proprietary materiality tool mDASH®. The fact that mDASH® focuses on the material ESG aspects of any given company means that the most irrelevant aspects of sustainability have been removed. I see mDASH® as a distilled version of all available ESG data out there. Through mDASH®, someone has done the job that I could not do, but which still needed to be done."

Ville explains that he uses the mSCOREs® coming out of mDASH® as a quality parameter in his model.

"I use the mSCORE® as a quality component. Essentially, if I have two companies that look the same from a quality perspective, the one with the better mSCORE® gets a better final quality score and attracts a higher weight in the portfolio."

The obvious question is of course if he has been able to come forward with any kind of portfolio improvement, e.g. from a risk perspective?

"Well, my overall ESG score has gone up and I am quite sure I have removed some tail risk [the most severe risk] related to low scoring companies. But it is still early days. I think I have found a way to get started and I know for sure that my average ESG score has improved, but whether that will play out in terms of performance is too early to tell."

Finally, what is the next step for you in terms of optimising the model, and how can sustainability play a role here?

"I am planning to start adding country ESG scores to my model. Country allocation is an important part of my strategy, so that could be beneficial. But as always, I will approach this area with the same diligence and care as ESG data in general. I will continue to cautiously take small steps that over time will hopefully make a significant difference for my portfolio."

*I use the mSCORE® as a quality component. Essentially, if I have two companies that look the same from a quality perspective, the one with the better mSCORE® gets a better final quality score and attracts a higher weight in the portfolio.*

# *ESG integration across the investment organisation*

Christian Heiberg
CIO, Danske Bank Asset Management, Copenhagen

**Christian Heiberg, can you please describe your role as the CIO of Danske Bank Asset Management?**
I have overall responsibility for all our investment portfolios, including the asset allocation decisions that go into our solution mandates. We have a diversified set-up of portfolios investing in many different asset classes and geographies. That means we also have a diversified skill set, with a clear delegation of investment responsibility down to the individual investment team behind each strategy. We do not manage our portfolios through committees or on a house-view basis, but bottom-up, with the responsibility placed where the competence resides.

**As CIO, in what way do you regard sustainable investment to be part of this?**
Very much in the same way, actually. I think there is a tendency to think of ESG analysis and investing as a completely different ball game, something that needs to be treated more on the side by ESG analysts, supplementing the financial analyses our portfolio managers carry out. There are those who think you need to be “passionate” about sustainability to really understand

> *I lead an organisation that is extremely passionate about investments and in being so they will look into all relevant aspects of a given investment opportunity*

## ESG Integration Council

The ESG Integration Council comprises Heads of investment strategies and was created to support ESG integration into the core of our investment processes. Since ESG Inside® is about making better-informed investment decisions, addressing risk issues, problems and dilemmas, and influencing portfolio companies through active dialogue to contribute to a positive outcome, decisions must be anchored in and supported by the investment organisation.

During the last 12 months, the ESG Integration Council has been involved in the development and creation of new policies, instructions and initiatives related to Sustainable Investments. This includes the development of voting guidelines, Sustainable Investment Instructions, a commitment to Climate Action 100+ as well as a new policy to restrict tobacco investments in order to meet customer demands.

the full implications of it. I lead an organisation that is extremely passionate about investments and in being so they will look into all relevant aspects of a given investment opportunity, be they sustainability-related or not. Hence, the analyses and decisions taken from a sustainability point of view need to be placed where the competence, knowledge, and insights into the asset class and the concrete investment opportunities reside. In other words, it is integrated into all other relevant analyses at an investment team level.

**How does the ESG Integration Council fit into this picture?**
"The Council is where I as CIO can take the lead in terms of ESG-related matters. It is an important forum for me to strengthen and reinforce our view on sustainable investments, i.e. organised bottom-up and anchored in our strategy ESG Inside®. Moreover, this is the forum where the investment organisation discusses and evaluates ESG risks and dilemmas, reviews and endorses investment restrictions, decides on collaborative engagements, and decides on other topics of relevance across my organisation."

*The Council is where I as CIO can take the lead in terms of ESG-related matters. It is an important forum for me to strengthen and reinforce our view on sustainable investments, i.e. organised bottom-up and anchored in our strategy 'ESG Inside'.*

**Can you give a concrete example?**
Last year, we took the decision to restrict investments in tobacco companies. As such, it is never an easy decision to expand investment restrictions, but with the research presented and the amount of client input included the decision to restrict was not that difficult [Please find more details on the decision to restrict tobacco companies in Chapter 3].

**What else did the Council do in 2019?**
One important initiative was the new, or rather the second, Shareholders' Rights Directive. Clearly, this is something we cannot conceptually implement bottom-up and where we need firm commitment across the investment organisation. In many ways, I think our organisation was quite prepared, in the sense that we were already able to report on our engagements in a quite detailed way, for example. One concrete outcome of the work with the Shareholders' Rights Directive was the voting guidelines, which are expected to be fully implemented during the first half of 2020. Among other things, the guidelines set out some important rule-based approaches to more standardised proposals for the Annual General Meetings (AGM). This will not only save time and increase consistency across our actively managed portfolios, it will enable us to open up for voting on passive holdings in 2020, an important step to further develop and elevate our sustainable investment offering across our product range [you can read more about our voting activities for passive holdings in Chapter 2].

## Introduction:

# *Active Ownership*

Active Ownership is the use of rights and positions of ownership to influence the activities or behaviour of investee companies by taking an active interest in their circumstances, development and management, and by maintaining a long-term focus on the company.

Our approach is based on the belief that addressing challenging issues through active ownership and dialogue is the more sustainable path rather than divesting and thereby losing an opportunity to make a positive impact and act as a responsible investor.

Recent decades have seen a dramatic rise in the exercising of active ownership in markets around the world. After the introduction of a Corporate Governance Code in the UK in 1992 (the Cadbury Report), aimed at improving companies' corporate governance, increased attention has been paid to investor behaviour with regard to their ownership of companies. This has been further highlighted by the introduction of additional regulations, such as the Shareholders Rights Directive II.


## At Danske Bank, we exert active ownership in three ways:

### 1. Company dialogue:

The ultimate goal of our dialogues is to support corporate performance and long-term value creation. Our portfolio managers use their position as investors to make a difference and to have a real impact by contributing to change and improvements, which is tied to our ambition of protecting and enhancing our investors' investments. Engagements may also focus on clarification of disclosed information, discussion of voting decisions or getting a deeper insight into companies' business strategies. Our portfolio managers regularly engage with companies to address ESG matters that can impact the financial performance of companies. This approach enables our portfolio managers to manage ESG risks and unlock opportunities in their portfolios as well as support and influence companies to improving aspects that impact their business and thereby support their growth and development.

### 2. Collaborative engagement:

When appropriate, we collaborate with peers, like-minded investors and other relevant parties to exert our active ownership, engage through joint dialogue and contribute to a positive impact. This might be appropriate in instances where Single Engagement has not led to the preferred outcome. We also participate in and support a number of different investor initiatives to encourage increased transparency and sustainability standards in companies and financial markets, such as CDP, Institutional Investors Group on Climate Change, Paris Pledge for Action, TTCFD, Climate Action 100+, The Montreal Pledge, and the UN-supported Principles for Responsible Investment.

### 3. Voting:

We use our rights to voice our opinion at general meetings. Mostly, we support the company management; but we also use our shareholder rights to vote in line with our fiduciary duty to consider the best interests of our customers. We vote on a variety of management and shareholder resolutions, although the majority target corporate governance issues subject to local listing requirements, such as approval of directors, approval of reports and accounts, approval of incentive plans, capital allocation, reorganisations and mergers. Investment teams assess resolutions and apply our voting policy and market standards to each item on the agenda.

**Extended voting scope**
In the past year, considerable work has been carried out to strengthen the infrastructure that enables us to vote more extensively. We seek to vote all shares held while taking into account preconditions, resources, and the costs of exercising voting rights. This has been done through the establishment of a more consistent voting scope that enables us to allocate resources to the most important issues. This means that Danske Bank now aims to vote according to the following rules:

1. Vote the largest holdings on an aggregated level (in terms of market value), meaning the sum of the voted holdings should exceed 80% of the total equity portfolio value (excluding Voting Scope Exemptions).
2. Vote all shareholdings that have substantial ownership, meaning exceeding 0.4% of votes or capital in an investee company.
3. Vote on issues of principal importance, meaning exercise voting rights if there are matters of specific concern. Matters of specific concern could be related to, for example, shareholder proposals regarding the environmental area, board diversification, political lobbying or media attention.
4. Vote on issues related to specific present and previous engagements.

Another important development within voting is the creation of Danske Bank voting guidelines. The purpose of this initiative is to provider better guidance for voting decisions. These voting guidelines are also instrumental to being able to vote on passively managed assets – something that Danske Bank has been doing since the start of 2020. Voting Guidelines is an extensive document covering a diverse range of topics such as board compensation, capital structure and director overboarding. These guidelines can be summarized in eight general principles:

1. The board should act in the best long-term interests of the company for the benefit of shareholders and take into account relevant stakeholders. The board should have a sufficient mix of directors with adequate competence and independence appropriate to the company's operations. The Chair of the board and CEO should not be the same person.
2. Remuneration for executive management should align with company and shareholder interests, with the aim of achieving long-term performance and sustainable value creation. Remuneration for non-executive directors (NED) should reflect company size and complexity as well as the NEDs' expertise and board position requirements.
3. The board should strive to achieve an effective and well-balanced capital structure. Capital exceeding the company's needs in relation to its long-term strategies should be distributed to the company's shareholders.
4. Audits should be carried out by external auditors independent of the company and its management.
5. Rights of all shareholders should be equal and protected. The principle of one-share-one-vote is recommended. Minority shareholders should have voting rights on key decisions or transactions that can affect their interest in the company.
6. All shares in a company carrying the same rights to the company's assets and profits should be treated equally in public offers to acquire shares.
7. Companies should seek to establish an open dialogue with their shareholders. Information and disclosure should be clear, correct and transparent.
8. Companies should seek to manage the financial and economic implications of environmental and social matters, which may have an impact not only on reputation but may also represent operational risks and cost to the business.

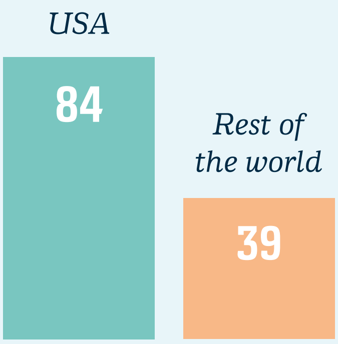
Based on our experience, we have concluded that you cannot talk about Sustainable Investments by mainly walking away from a risk, a problem, or a dilemma and hoping that someone else will assume the responsibility. On the contrary, we are convinced that it is more sustainable to address challenging issues through active ownership as our first option.

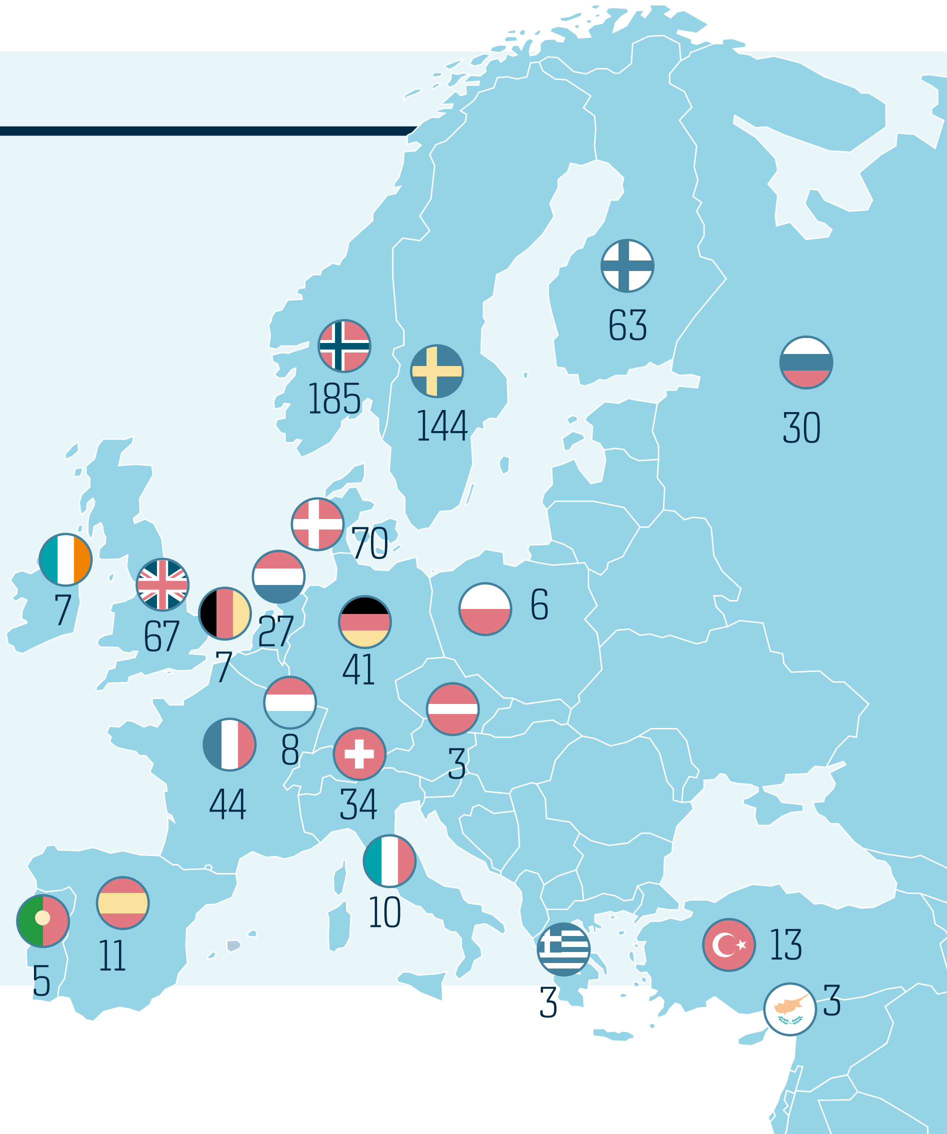
# *Engagements in 2019*

In 2019, our investment teams increased their number of interactions with companies they invest in compared to 2018. The increase illustrates the maturing of our processes, the importance of sustainability matters and its potential impact on company performance, and thereby the potential return to Danske Bank's customers. In 2019, we had the following engagement activities.

| Companies | Country domiciles | ESG engagement topics | Interactions |
|---|---|---|---|
| **544** | **37** | **105** | **909** |
| *422 in 2018.* | *34 in 2018.* | *59 in 2018.* | *643 in 2018.* |

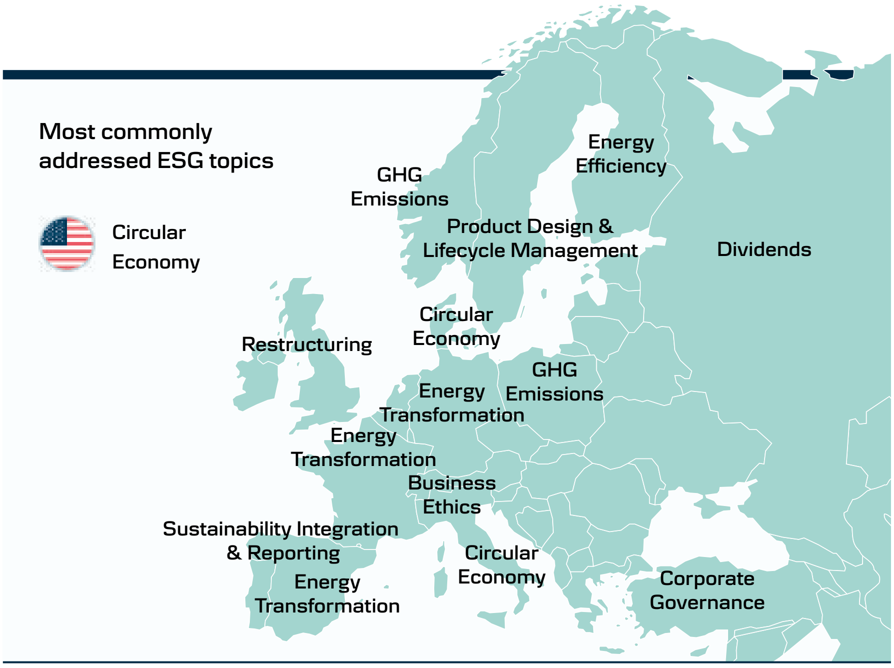
**We engaged with companies in 37 different country domiciles.**



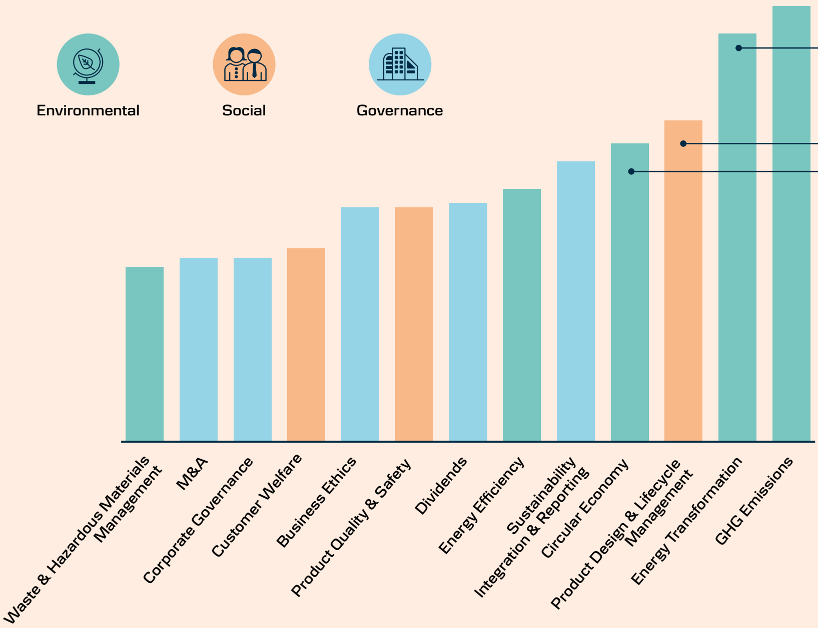

Learn more about our engagement activities in our Active Ownership Report at danskebank.com/sustainable-investment.

**Most commonly addressed ESG topics**




Split between ESG engagement themes


Among the 105 ESG engagement topics, energy-related matters continued to be the most discussed topics in 2019, which accentuates the green transition's business impact. In addition, circular economy moved into top ten in 2019, and that development is a result of both our investment teams' and companies' increased focus on addressing business sustainability in a holistic way.




*Energy transformation is a shift from fossil energy resources to "greener" energy alternatives entailing a lower carbon footprint. A company's approach to energy and carbon emissions can directly impact its cost structure, risk profile, resilience and brand value with its stakeholders.*

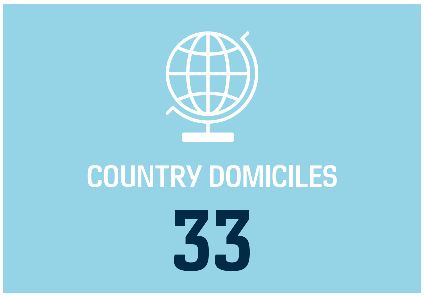
*Product design and lifecycle management includes e.g. the managing of impacts of products and services, such as those related to packaging, distribution, use-phase resource intensity, and other environmental and social externalities that may occur during their use-phase or at the end of the life.*

*Circular economy is a system of closed loops in which the usage of raw materials, components or products are reduced, reused or recycled. It can also bring positive impacts on social and climate aspects and increase resource efficiency. Companies taking a circular approach to their business by aiming at maximising the value of their assets can achieve competitive advantages and benefit financially.*

# *Voting in 2019*

**In 2019, we had the following voting activities.**

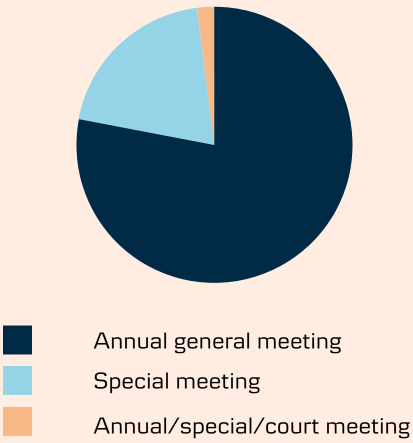

*313 in 2018.*




*22 in 2018.*


*4,627 in 2018.*

**We voted primarily at annual general meetings**





Learn more about our voting activities in our Active Ownership Report at danskebank.com/sustainable-investment

## We predominantly voted FOR the proposals

5,796 proposals

| FOR | AGAINST | ABSTAIN |
|---|---|---|
| 95.5% | 2.7% | 1.8% |

## Most common topics where we voted against management recommendations


*Concerns about the board of directors' option to pay an extraordinary dividend to executive management meant that we voted against the proposal. The main issue was the potential lack of alignment between the interests of the shareholders and day-to-day management as there was no ceiling on the extraordinary dividend.*

*We voted against a proposal that authorized the board of directors to fill vacant board seats. We believe that it is the annual general meeting that elects new board members and not the board of directors. Our approach is founded in our ambition to meet the best interests of shareholders.*

*In one case, we voted against electing a company's CEO to the board of directors as it may have negative governance implications and compromise the independence of the board.*

# *An opportunity to make a greater difference*

Thomas Otbo,
Head of Solutions, Copenhagen

Active ownership through voting at general meetings is an important part of our ability to create long-term value for the companies we invest in and for our customers. The annual general meeting is an opportunity to voice our opinion, vote on issues of key importance to the running of a company, and contribute to good governance of the company.

Voting refers to the exercise of ownership rights at the General Meetings of companies where we own shares. We vote on management or shareholder resolutions to approve or disapprove of corporate governance as well as relevant environmental and social matters.

Index funds have become more popular in recent years among both institutional and private investors. Given this trend, being able to offer index products that integrate active ownership into their setup will become increasingly important, according to Thomas Otbo,

Head of Solutions, who is responsible for index products at Danske Bank. Our recent initiative start voting for holdings in our index funds has already been positively received by Danske Bank's customers, says Thomas Otbo.

"Index funds have historically had less focus on active ownership. Exercising active ownership through voting with passively managed assets is needed to create long-term value and build trust as a universal owner. Our new voting initiative provides us with a stronger foundation for actively contributing to companies becoming even better at focusing on long-term value creation that benefits both investors and society in general," says Thomas Otbo.

Danske Bank's index funds can encompass thousands of companies – and based on the newly developed voting scope, Danske Bank aims to voting at the GMs of a clear majority of those. In addition to the increased voting scope, the bank has also developed Voting Guidelines. These guidelines steer our voting activities on passively managed assets and help investee companies and customers understand how we are likely to vote in a given situation.

"As a major index investor, we have a responsibility to use our position to safeguard our customers' assets. Moreover, we have strong corporate governance competences, which we can bring into play in index funds to help shape companies, so they have a positive impact on society. By exercising our voting rights, we can also help ensure companies address business-critical sustainability issues. A competent Board of Directors, for instance, is a key prerequisite for focus on long-term value creation. Investors' votes at GMs are an effective instrument that helps ensure the Board of Directors has the right structure to future-proof the company's business potential," says Thomas Otbo.

As an investor in listed equity, we also exercise our right to impact our portfolio companies by voting at general meetings or supporting shareholder proposals that address standards of corporate governance or sustainability. We are firmly convinced that addressing challenging issues through active ownership is the more sustainable approach, as this is where we can have an impact and make a difference.

"

*Our new voting initiative provides us with a stronger foundation for actively contributing to companies becoming even better at focusing on long-term value creation that benefits both investors and society in general*

# A nuanced approach to corporate governance in Russia

Olga Karakozova,
Senior Portfolio Manager, Eastern European Equities, Helsinki

Traditionally, investing in Russian equities has been associated with weak corporate governance. In this article Senior Portfolio Manager Olga Karakozova gives her view on a much debated topic.

It is probably not too far-fetched to expect that a big chunk of the scientific articles and books discussing corporate governance in Russia in recent years focuses on the negative side of this topic. Investments in Russia are typically associated with weak institutions, high levels of ownership concentration, underdeveloped capital markets, a high degree of state involvement in business, etc. So how do you deal with corporate governance issues when compiling a portfolio of Russian companies? The short answer is that you engage with the companies and dig deep in order to understand. We have asked Olga Karakozova, Senior Portfolio Manager at Danske Bank's Eastern European Equity team, with a focus on Russian equities, to elaborate on this.

"It is true that weak corporate governance is a significant factor for minority investors to consider when investing in the Russian stock market. At the same, if you are too headline-oriented here, you will form an unnecessarily dark picture of the situation. Things do not change overnight, but we are now seeing some significant improvements, indicating new times in terms of corporate governance in Russia," says Olga Karakozova.

One way to assess the importance of corporate governance for our Eastern European Equity team is to look at the team's active ownership activities in 2019. At an aggregated level, a clear majority of the engagements focused on corporate governance-related matters rather than environmental or social aspects. Indeed, 68% of the company meetings focused on corporate governance in 2019.

*As portfolio managers, we need to engage with companies in order to both understand complicated matters as well as influence and support them in the right direction.*

"That is a high number and we sometimes get asked whether there is a 'crowding out effect', i.e. does corporate governance being such a dominant issue mean less time to focus on relevant environmental or social aspects. I don't think focusing on governance means we cannot cover other material matters. After all, if we sit in a meeting and think that a certain environmental or social aspect is relevant to bring up, we will bring it up. Right now, we believe that pushing Russian companies to improve corporate governance practices is key to share price performance."

Olga mentions stronger dividend policies as one important corporate governance aspect of the Russian market. She sees some important steps being taken towards a more structurally changed policy, both in terms of higher pay-out ratios and increased transparency. Decent dividend schemes mean that companies are willing to share their profits with minority shareholders. In absolute terms, Russian companies paid around $32 bn in dividends in 2019, with some $10 bn of this going to minority investors – a significant amount for a market with a $225 bn free float.

"There is no doubt that improved pay-outs have been a major reason for the Russian market's outperformance in 2019," Olga says, and gives an example:

"We can see that a company like Gazprom has taken some significant steps. We have met Gazprom several times over the years, something that helps in assessing the current situation. As portfolio managers, we need to engage with companies in order to both understand complicated matters as well as influence and support them in the right direction."

At the end of 2019, Gazprom's management announced a new dividend policy entailing an increase in the dividend pay-out ratio to 50% of IFRS[1] net income within two to three years. This substantially improves the investment case, and Gazprom's 2019

[1] *International Financial Reporting Standards*

dividend upgrade caught many investors by surprise.

"The fact that Gazprom is a state-owned enterprise (SOE) is interesting from two perspectives: First, there is a government plan to privatise some of those SOEs and, secondly, the Finance Ministry is seeking to raise more funds from these companies via dividends. This effort has in fact already contributed quite a lot to the overall pay-out increase. We expect the government to continue pushing pay-outs higher, providing meaningful upside for the overall market numbers," says Olga.

She also points to their deputy CFO's plan to expand its Investor Relations (IR) work and deliver the key strengths of the company's investment case to the broader investment community. This, coupled with a hike in dividend, suggests to Olga that changes within the company are going to be bigger than a pure one-off dividend hike.

Many probably know Gazprom for its extremely low valuation. How does that play into the concept of corporate governance?

"

*Right now, we believe that pushing Russian companies to improve corporate governance practices is key to share price performance.*

"That's indeed true. Gazprom trades at a low P/E, mainly due to poor capital allocation, low Free Cash Flow (FCF), etc. For years, the company destroyed value in most of its projects. A shift towards spending more earnings on dividends rather than future reinvestments in low-return projects would considerably improve its return metrics, which should be reflected in a higher valuation multiple. In this way, there is a clear link between the valuation and the company's corporate governance standards."

On a more general note, what is your view on the Russian Finance Ministry's efforts to raise more funds from SOEs – such as Gazprom – through dividends rather than taxes, considering that a tax hike would elevate the level of funds collected? After all, the Russian state's ownership in these SOEs is not 100%.

"This is indeed interesting, because it tells me there is a commitment to a better corporate governance environment from the Russian state too. I discussed this with Gazprom some time ago and their view was that one of the strategic targets of the Ministry of Finance – which by the way consists of young technocrats – is to improve the investment climate in Russia in order to attract more Foreign Direct Investment (FDI). Those investments declined significantly after the economic sanctions that were introduced a few years ago. More FDI would be positive not only for the Russian economy but also for corporate governance, as it would set a standard for more transparent and efficient ways of allocating capital. In my view, this is still the biggest challenge for many Russian companies," Olga Karakozova concludes.

# *Taking an active part in the green transition*

Kasper From Larsen
Senior Portfolio Manager, Euopean Equities, Copenhagen

Investors are an important voice in the oil industry and can use their influence to push oil companies in a green direction, says senior portfolio manager Kasper From Larsen. He believes that engaging actively with oil companies makes sense both from a return and a climate perspective.

As an investor, how do you contribute most effectively to the oil industry getting onboard the green transition? Remain invested in oil companies, says Kasper From Larsen, Senior Portfolio Manager with Danske Bank's European equity team specialising in the energy and utilities sector. In that way Kasper can use his voice and position as a shareholder to push and support companies to move in a green direction. He believes in actively contributing to their transformation, and he would not have the chance to influence developments and make a difference if he divested oil companies. Kasper From Larsen sees a clear trend of traditional oil companies embracing the climate agenda and increasing their investments in renewables.

"In recent years, several oil majors have increased their investment budgets for the production of solar and wind energy, in particular, and that is the result of pressure from various actors. Oil companies face a new reality where the world around them is shifting towards greener energy alternatives and where the demand for oil will most likely not continue at the same level as before," says Kasper.

> *I see no reason to divest from oil companies when you can influence them to reduce their $CO_2$ emissions and turn to greener forms of energy.*

His view is that pressure from consumers and politicians along with investors has been the main reason why some oil companies are increasingly joining the transition towards a low-carbon economy.

**Investors have good opportunities to influence**

One of the oil companies' most important goals is to be an attractive investment and to have access to capital to e.g. expand their businesses. This provides investors with good opportunities to influence oil companies in a green direction.

"Companies listen to us because they are keen to present an attractive investment case, so they are interested in hearing about what we view as material business matters from an investment perspective. Failure to listen and adjust their businesses could essentially increase their cost of capital in the longer term. Moreover, it could mean a lower external ESG rating, which would also weigh on the companies' cost of capital. In combination, these factors can have huge financial consequences for companies and make them poor investments," says Kasper From Larsen.

**Engaging actively in the transition**

In Kasper's opinion there is no contradiction between creating a good return for customers and at the same time pushing oil companies to reduce their climate impact.

"Pushing this process along involves being actively engaged in the transition and contributing to the journey. That is why I am constantly in active dialogue with many oil companies, pushing for change. Oil companies will not become green overnight, it is a long, hard slog, but acting responsibly and using your influence as an investor to help drive the transition is important. In my view, this is the most effective way to make a difference to the green transition, rather than selling out of oil companies and losing your influence opportunities."

He emphasises that the oil industry is a super tanker and that changing direction takes many years. The level of oil production reflects society's demand, and in 2060, Shell, for example, still expects the demand for oil to equal 50-60% of current production. Hence, the dialogue should not only be viewed over a 2-5-year period but over decades, and it is vital that investors are actively engaged and influence companies to drive developments towards green energy.

**Preparing for the age of electrification**

Electrification is one of society's predominant pathways to decarbonising

the economy, with sectors such as transportation and construction already shifting their energy consumption towards electricity. Against this backdrop, one of Kasper's key points in his engagements with oil companies is the need to increase investment levels in renewable energy and that fossil fuel production should take up an ever smaller portion of the business in the coming years.

"It is crucial that oil companies progressively position themselves for the energy transformation by changing their energy production and gradually increasing their renewable energy capacity to meet the higher power demand stemming from e.g. electrification. Entire industries are undergoing a major transformation, with the auto industry as a prime example. The majority of auto manufacturers have launched ambitious targets for electric vehicle production, and we expect this to be one of the major drivers towards increased electrification," explains Kasper From Larsen.

He points to Equinor, Shell, and Total as companies pursuing strategies to transition from being oil companies to energy companies. As an example, Equinor and its partner SSE Renewables have been awarded contracts to develop the world's biggest offshore wind farm in the Dogger Bank region of the North Sea with a total installed capacity of 3.6 GW, enough energy to power the equivalent of 4.5 million UK homes. Shell's renewable energy activities include operating and developing several offshore and onshore windfarms across Europe and the US, acquiring an electric vehicle charging company and developing numerous large-scale solar power plants. Total is well under way to have 6GW of renewable power generation installed by the end of this year and targeting at least 25GW by 2025.

**A climate focus is good for business**

Being invested in oil companies makes sense from a business perspective so long as they are moving in a green direction. The companies know this is their licence to operate, for if they do not move in this direction, they do not have a relevant business or will not be an attractive investment, says Kasper From Larsen, who adds:

"I see no reason to divest from oil companies when you can influence them to reduce their $CO_2$ emissions and turn to greener forms of energy. A few years ago, the industry was focused on increasing oil production, but senior management now has a greater focus on investing massively in renewable energy. One important reason for this is that consumer demand has moved in a green direction, and that provides us investors with a financial incentive to push the oil industry along a climate-friendly path."

Kasper meets up with the management teams of certain major European oil companies several times a year to discuss, among other things, their climate strategies and how they are transforming production to cleaner energy technologies, so they can have the right sustainable energy products on their shelves. He has observed a clear trend towards investors very much wanting to pay less for companies that are not transitioning and more for companies that are moving in a green direction. For Kasper From Larsen, this is a clear example of how it makes return and climate sense to remain invested in companies that are shifting towards a greener profile, and how investors can use their financial muscle to contribute to international climate ambitions.

## Renewable energy investments

Traditional oil companies have set ambitious goals for energy production from renewable technologies *.

| Company | Planned annual investments in renewable energy going forward to 2025 |
|---|---|
| Shell | DKK 14-21 billion |
| Total | DKK 28 billion |
| Equinor | DKK 14-21 billion |

**Data are from the companies' latest available financial reports.*

*"Shipping is high on the agenda of the international society's efforts to combat climate change. In the light of this development, we are even more focused on whether shipping companies are working actively with climate challenges to be better prepared if climate regulation moves forward faster than expected."*

Anders Grønning, Portfolio Manager, Credit, Copenhagen

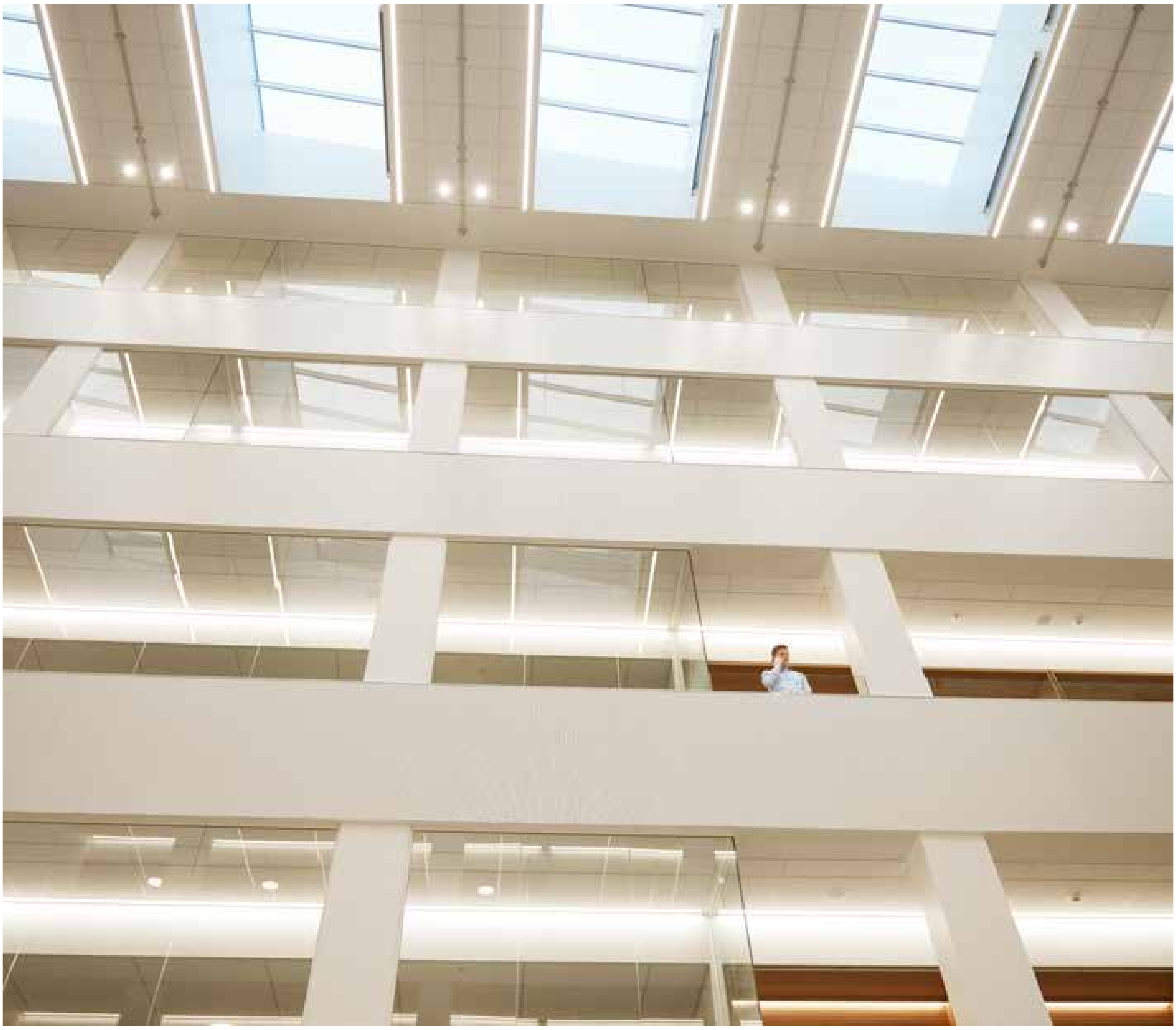
## Introduction:

# *Screening & Restrictions*

As investors, we believe we can make a difference by using our ability to influence portfolio companies to integrate sustainability into their business strategies, and to manage their ESG risks and challenges. Excluding companies with an identified risk, concern, or dilemma would reduce our efforts to a minimum and remove our ability to influence. Hence, our first option is always to stay invested, manage difficult matters, escalate our efforts through solid analysis and active ownership, and take responsibility by engaging with our portfolio companies.

Investment restrictions are commonly implemented by investors and asset managers as a threshold before any investment analysis or decision takes place, and is contrary to ESG integration, where financial and ESG factors are integrated into the portfolio construction and security selection process. We take a cautious approach to investment restrictions, as they relate to excluding companies, sectors, or countries.

However, we serve a great number of customers across the Nordic region with a diverse set of values, preferences and needs. We are committed to meeting their needs through our capability to incorporate criteria, thresholds and restrictions using screening as a tool to identify particular companies, sectors, or countries.



# *Meeting customer demand with tobacco restriction*

In 2019, we implemented investment restrictions on tobacco companies for all our Danske Invest funds, based on our customers' request across the Nordics.

Our customers' preferences and values develop and change over time. Listening to our customers and taking their demands and expectations into account is an integral part of our sustainable investment strategy ESG Inside®. As an asset manager, we see it as part of our fiduciary duty to our clients to offer solutions that reflect and captures their needs and demand. At the end of 2019, we implemented a tobacco investment restriction for all Danske Invest funds and for Danica.

An internal study of the 300 largest Nordic asset owners' investment policies concluded that our institutional client base across the Nordics to a high degree do not wish to invest in tobacco. A survey among our retail clients confirmed this picture. We also analysed the possible implications on our ability to deliver attractive risk-adjusted returns and concluded that a tobacco restriction would not compromise this ability. The decision to implement the tobacco restriction was taken by our investment organisation through the ESG Integration Council[1].

**Applies to equity and bond investments**

The tobacco restriction applies to both equity and bond investments across all Danske Invest funds and Danica Pension investments. The restriction on tobacco expands the investment restrictions already in place for thermal coal, tar sands, and controversial weapons.

## The tobacco restriction

Definition:
Tobacco products are products made entirely or partly of leaf tobacco as raw material. Tobacco products are also electronic cigarettes and other 'next generation products'.

Restriction criteria:
Companies with revenues exceeding 5% of turnover from tobacco products are restricted from the investment universe.

*[1]You can read more about ESG Integration Council in Chapter 1*

# *A portfolio manager's view on investment restrictions*

Peter Nielsen,
Chief Portfolio Manager, European Equities, Copenhagen

Our portfolio managers also play an important role in our ongoing dialogue with customers

The decision to refrain from investing in tobacco companies in all Danske Invest funds and Danica was not only based on our internal analysis of the largest Nordic asset owner's investment policies and our internal survey among Nordic retail clients. We also received feedback directly from clients and prospects in one-to-one meetings. Our advisors and relationship managers have an important role here, and equally so our portfolio managers. Not only do they meet investee companies to engage on material ESG topics, they also regularly meet with clients and prospects directly as well as with the investor community at conferences and events.

One of those portfolio managers is Peter Nielsen, who is the lead manager of a European equity portfolio with a clear high dividend tilt.

"Meeting clients and prospects is an important aspect of my role as portfolio manager. To get direct feedback on what I do in terms of the investment process, philosophy and not least investment decisions, is not only valuable but also critical for the long-term development of my portfolio."

Peter Nielsen has been responsible for the European High Dividend strategy since 2004 and has met many clients over the years, both in the Nordic area and globally. Being tested on investment decisions and asked to give a detailed rationale for the portfolio set-up at any given time is an important aspect of his role as lead portfolio manager. In his client dialogues, Peter Nielsen also spends a significant amount of time on ESG-related issues.

"What has become clear to me is that specific value preferences have grown in significance over the past 5 years. When our strategy was launched in the early 00s, only a select few talked about values, but I would say the focus on these issues has grown quite significantly, especially in recent years. I have learned much from these talks, as they have helped me advance my own integration of ESG matters. To be able to quantify and justify the risk premia assumed from an ESG perspective is now part of my everyday portfolio management life."

> *To get direct feedback on what I do in terms of the investment process, philosophy and not least investment decisions, is not only valuable but also critical for the long-term development of my portfolio.*

Peter Nielsen continues:

"There has also been one specific topic where the discussions have changed in character. Over the past few years, I have had more conversations about tobacco companies where the end-point has not been about the risk/reward of a given company. Rather it has ended with a values-based "no" – regardless of valuation and outlook. In these cases, the client tells me the investment is unacceptable, irrespective of the business case as such. This takes the discussion into new territory where it is sometimes difficult, if not impossible, to find common ground."

Even though he also meets clients willing to invest in tobacco companies, especially outside the Nordic area, Peter Nielsen has seen more and more clients putting their values in terms of tobacco ahead of any other variable. As he saw the issue grow, he decided to bring it to the table of the ESG Integration Council, where he is a member.

"The sheer magnitude of the issue prompted me to raise the discussion in our ESG Integration Council. The other alternative would be to self-regulate by implementing a voluntarily portfolio-level restriction, but I thought the issue here was of a more general character and probably applicable in a broader context."

Several members of the ESG Integration Council were well aware of the tobacco issue. An important aspect of this was to analyse the risk/reward implications in order to make sure that a potential restriction would not have any significant implications for our ability to create attractive risk-adjusted return in our portfolios.

"Six months after I raised the issue, we reached a conclusion and made the decision that I thought was solid, with a clear client-oriented foundation. As a portfolio manager, I obviously have no interest in imposing investment restrictions per se, but our clients' feedback is paramount in our business. To have an investment forum such as our ESG Integration Council, where you can land these kinds of discussions and decisions is valuable and important, and I believe we ended up with a solution that is beneficial for our clients in general."


### Introduction:

# *Communication & Reporting*

One of the most important initiatives for Danske Bank is to improve the storytelling around our ESG approach. Our customers and other stakeholders increasingly require high quality ESG Communication & Reporting on our ESG activities in the form of documents, dashboards, raw data, reports, videos and other formats. Customers may use this information to comply with their own internal duties and regulatory obligations, and to understand our sustainable investment work. In addition, ESG Communication & Reporting allows for a more robust monitoring by and accountability to customers, beneficiaries, regulators, standard-setters and other stakeholders.

In the past year, we have launched our Active Ownership Report with data and analytics on our company dialogues, voting, engagement topics, themes and scope. We have also published Active Ownership Stories, where our portfolio managers share examples of their specific company engagements, dialogue focus, interaction with company management and the expected outcome. The stories add a narrative to the data and analytics and support our ambition to be transparent about what we do and how we progress in creating impact.

# *ESG Inside® our products – clarity on ESG characteristics*

To help our customers choose products that meet their financial goals as well as their specific sustainability preference, we have mapped our wide range of funds and positioned them according to their specific sustainability characteristics. While ESG Inside® is the foundation for all Danske Invest funds, each fund also has its specific focus. We have grouped the funds using three main ESG characteristics, namely ESG Inside: Integrated; ESG Inside: Restricted; or ESG Inside: Thematic.

Funds that do not have a particular ESG characteristics, are labelled ESG Inside® only, to clarify its foundation of ESG Inside® including our group-wide restriction for controversial weapons, tar sands, thermal coal, and tobacco.

All Danske Invest funds, including externally managed funds will be labelled according to our product positioning framework. During 2019 we completed the first round of fund positioning and the second wave in 2020 will for example cover our externally managed funds.


The fund systematically integrates sustainability in the investment process in order to make better-informed investment decisions.


The fund targets specific sustainability themes and solutions such as climate, water, circular economy or the UN's Sustainable Development Goals.


The fund restricts specific companies or sectors according to set criteria, such as e.g. alcohol, gambling, or fossil fuel.


## New one-pagers

During 2019, we launched a set of new so called one-pagers for our funds, with the overall idea of bringing ESG Inside® down to an individual portfolio level. Providing and presenting distinct sustainability perspectives of our different portfolios is an important measure in our quest to guide and help customers and other stakeholders in terms of sustainable investments. The one-pagers serve to give customers detailed information about:

1. Specific themes or topics such as carbon footprint.
2. Product positioning and information about our ESG integration, Active Ownership, and Screening & Restrictions.
3. Customers' choice of 3rd party ESG portfolio rating.

At www.danskebank.com/sustainable-investment you can find general information about sustainable investment and our strategy ESG Inside, whereas you can find information about specific funds including our ESG one-pagers at www.danskeinvest.com

# *Investing globally in the transition towards a sustainable future*

Martin Slipsager Frandsen,
Senior Portfolio Manager, Global Equities, Copenhagen

Thematic investments can have many perspectives from a sustainability point-of-view. In this article, Martin Slipsager Frandsen, Senior Portfolio Manager at Danske Bank Asset Management shares his views on thematic investments in global equities.

The demand for a more sustainable future is clear, the focus has accelerated over the past years, and today most countries in our part of the world have set ambitious targets within this area. For example, my home country, Denmark, is ambitiously targeting a 70% CO2 emission cut by 2030 and carbon neutrality by 2050. In order to meet this target, Denmark will have to comprehensively extend its capacity within renewable energy, as well as transform its heating, transportation, and industrial production.

In societies where privately run companies are the backbone of the economy, a transition of this scale, cannot happen without a corresponding corporate transition. Our societies can reach these sustainability targets only by leveraging the innovative mind-set that many of the leading global companies master. Governments setting sustainability targets bring investment potential. They steer through regulations and directives, but it is often the private companies that come up with the solutions. We believe that these companies stand to benefit from delivering these solutions, and that is tremendously interesting as an investment professional.

> *In a society like ours, where deep technical knowledge and competence is a main driver, companies need to collaborate in order to fully achieve the potential of the transition.*

**New game plan for competition and cooperation**

The transition is going to take decades, and is probably the biggest since the industrial revolution. In a society like ours, where deep technical knowledge and competence is a main driver, companies need to collaborate in order to fully achieve the potential of the transition.

I see many examples of companies flourishing with innovation when applying a more open mind-set. While companies 10 years ago often took a myopic approach to protecting their intellectual property fending others off, there is now a clear trend to be more open and collaborative.

One example of this is Cerner, an American supplier of health care technology, which has entered into a strategic partnership with Amazon regarding data processing. Cerner has great data and knowledge about patients from the electronic healthcare records, and Amazon is a leader in applying Artificial Analytics to predict consumer behaviour. By combining these capabilities, the partnership seeks to predict health outcomes for patients, which can help hospitals plan better and thereby work more efficiently and save costs. Ten years ago, a company like Cerner had most likely tried to keep Amazon out of its sphere, and thus do everything themselves. They could have been successful, but it would have required large investments and a lot of time. Therefore, we see the partnership with Amazon, as a smart move. In the end, it will mean better diagnosis of patients,

better health outcomes, and a more efficient hospital sector.

**Dialogue as the most important tool**
This open and collaborative mindset among companies also means that there is greater will to listen to investors such as us and others. I see active ownership and not least the direct dialogue with companies as a fundamental part of our investment process. Companies want to listen, and we are keen to engage in constructive dialogues to contribute to a positive change and improvements, while creating value for our clients.

We want to remain long term sparring partners for the companies we invest in, supporting their efforts to stay relevant by exploiting the opportunities that the global transition creates.

In this context, dialogue is also a highly important mechanism to protect ourselves from greenwashing. If you claim to invest in companies benefitting from a transition to a more sustainable future, you need to be able to show real progress. I need to be able to show that every single investment makes sense also from a sustainability perspective. The challenge is not to find companies claiming to be part of the transition; the challenge is to find those who actually are. Companies can set up ever so great targets and goals, but when we scratch the surface, historical trends and current actions have to make us comfortable enough to believe that they will actually live up to what they promise.

This challenge seems to magnify when looking at ESG data and company assessments from third-party data providers and rating agencies. They can point in all different directions and often I get the impression that these company ESG scores are based on what is reported rather than what is taking place. To me, lack of disclosure and lack of understanding the material sustainability perspectives gives an opportunity to get insights directly from the companies through dialogue. Speaking directly with senior management helps me understand what is for real, and few things are as powerful as to speak directly with the CEO or CFO about if their efforts are a matter of commitment, or of marketing. The dialogue is essential and as such, it serves as the most important tool to assess the true sustainability perspective of a company. It gives us an opportunity to get insights directly from the company, which is a competitive advantage we as a firm have built up over many years, and essential when we invest in a long-term transition towards a sustainable future.

**Setting targets for each investment**
An important aspect of our investment process is that we also set targets for our portfolio companies' contributions towards a sustainable future. We work with primary, secondary, and even tertiary targets for each of our portfolio companies that we systematically follow-up. We have also created a scorecard, which helps us track and monitor the progress of each investment. This is a journey and talking to many of our clients, I sense their appetite and clear interest in participating in the journey. I welcome that.

”

*We want to remain long term sparring partners for the companies we invest in, supporting their efforts to stay relevant by exploiting the opportunities that the global transition creates.*


*"In all we do, we seek to be transparent and clear in our reporting and disclosure. Apart from this annual report, we have launched publications such as our 'Active Ownership Report' and 'Active Ownership Stories, which provide not only the facts and the figures from our dialogue and voting activities but also the more in-depth stories of dialogue carried out by our portfolio managers."*

Ulrika Hasselgren
Global Head of Sustainability & Impact Investment

*“The analyses and decisions taken from a sustainability point of view need to be placed where the competence, knowledge, and insights into the asset class and the concrete investment opportunities reside. In other words, it is integrated into all other relevant analyses at an investment team level.”*

Christian Heiberg
CIO

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