Our approach to investments on stock and bond markets

Introduction

Triodos Bank is one of the world’s leading sustainable banks. Its mission is to make money work for positive change. In addition to its core business of taking in savings deposits and lending them directly to sustainable enterprises, Triodos Bank offers investment services that fit its mission and vision. These services are provided by Triodos Private Banking and Triodos Investment Management.

Triodos Investment Management is a wholly-owned subsidiary of Triodos Bank and manages impact funds. These funds invest directly in companies or projects with the aim of delivering social or environmental benefits, alongside financial return. Triodos Investment Management’s fund range also includes four funds, which invest in listed securities worldwide.

This document explains the investment strategy and portfolio construction process of these funds – Triodos Sustainable Bond Fund, Triodos Sustainable Equity Fund, Triodos Sustainable Mixed Fund and Triodos Sustainable Pioneer Fund, grouped under the Triodos SICAV I umbrella – both from a sustainable and a financial perspective. Triodos Private Banking shares this public market investment philosophy and follows the same selection process for its investment services.

Mission

The mission of Triodos Bank is to make money work for positive social, environmental and cultural change and to help create a society that promotes people’s quality of life and has human dignity at its core. Triodos Investment Management shares this mission. More specifically, our aim as an investor is to serve as a catalyst in the transition to an economy where people and planet come first.

Vision

Our investment philosophy is based on the belief that in the long term the most successful businesses will be those that achieve the right balance between their social, environmental and economic performance. Any company that intends to deliver long-term value must effectively manage its relations with all stakeholders and be responsive to their needs and demands. We believe companies that balance these interests effectively will deliver the greatest value to all their stakeholders, including the capital providers.

Strategy

We offer four different funds, each with their own strategy and thus their own risk-return characteristics. Our funds invest on public markets in a wide range of stocks and bonds (corporate, sovereign and impact) and have a long-term investment focus and a concentrated portfolio in common. The funds are registered under the umbrella of Triodos SICAV I.

Important elements of our investment strategy are:

- Rigorous selection process: we only invest in companies that contribute to a sustainable society or clearly lead the sustainability agenda in a particular sector. Furthermore, we will not invest in companies that are associated with unsustainable services, products or business processes.

- Constructive dialogue: we actively engage with companies to stimulate improved sustainability performance while enhancing company value creation opportunities. This dialogue has a threefold purpose: to raise awareness, to influence company management and prompt companies to act to further sustainable business practices, thereby seeking benefits for all stakeholders involved.

- Optimum transparency: by offering details about our investment approach and its implementation we aim to enable our clients to take a well-informed decision about whether to invest in the products we offer.

Our investment approach, engagement activities and transparency are detailed further below.

Investment approach

We build our portfolios based on the principle that only companies that fulfill our sustainability criteria can be invested in. We select them by using a three-step approach. First, we select companies based on sustainable activities (positive screening – step 1) with the caveat that these companies must also comply with our minimum standards (negative screening – step 2).

Once companies are deemed eligible for investment, integrated financial and sustainability analysis (step 3) is conducted to see whether companies qualify as portfolio candidates. Portfolio construction and investment decisions depend on price appreciation.
potential, portfolio manager conviction, risk-return characteristics and portfolio requirements and market circumstances.

Step 1: Idea generation and positive screen

From a broad universe of companies, we select those that offer products or services, or have operating models that support the transition to a sustainable society.

Triodos Investment Management has identified certain types of products and services that contribute to the transition to a sustainable world. These sustainable activities, which the United Nations have set forth to act on in their 17 Sustainable Development Goals (SDGs), address the global challenges posed by structural trends such as ageing population, resource scarcity, inequality and exclusion. Seven transition themes act as a lens to select the funds’ investments. A company that derives over 50% of its revenues from such sustainable activities, or that is expected to derive over 50% of revenues from exposure to one or more of these themes within the next three years, qualifies for investment by one of our SRI-funds.

Companies can also be selected for their leadership role in corporate social responsibility within their industry. These are the Corporate Social Responsibility (CSR) Pioneers. A company that qualifies as a CSR Pioneer is considered a real sector leader in terms of corporate social responsibility, with either best-in-class behaviour in its approach to stakeholder management or demonstrating clear leadership in its products or production process, giving its industry the path of transition to a sustainable society.

Seven transition themes

1. Sustainable Food & Agriculture

Triodos Investment Management selects companies that contribute to farming systems that preserve soil, water systems, nature and biodiversity as well as companies that promote sustainable food products and healthy diets. Also, companies that sustain depletable food resources such as fish may qualify. Examples of products and services that are part of this theme are natural and organic food products, vegetarian or vegan food products, sustainable fisheries, nutritious and healthy food products. Companies in this theme may be producers, processors, distributors, retailers or otherwise active in the promotion of food that is healthy for people and planet.

2. Sustainable Mobility & Infrastructure

The mobility systems of the future are likely to be different from what exists in most of the world today. Efficient mobility solutions that operate on sustainable infrastructures contribute to a sustainable future. Mobility and infrastructure solutions also enhance the quality of life of individuals and communities. However, private and public mobility, and the construction and usage of infrastructure have significant carbon footprints and social, environmental and ecological impact. We look for companies that offer sustainable solutions for mobility and infrastructure challenges such as urban mobility, sustainable buildings, and electric vehicles.

3. Renewable Resources

The growth of the world’s population and its wealth are two trends that increase global consumption and therefore the demand for natural resources. This increases the human environmental footprint well beyond the regenerative capacity of the earth. The challenges that these two trends pose is how to replace finite resources by renewable resources, increase efficiency of their use and preserve their origin. To contribute to these challenges, we invest in companies that provide an alternative to fossil fuel-based resources, like renewable energy, produce bio-based materials as alternatives to finite resources or contribute to more efficient water infrastructure and responsible water use.

4. Circular Economy

An economy that fits within the boundaries of the earth means that our production system needs to transform from linear to circular. This implies a transition from a take-make-waste economy to an economy where products are designed to last as long as possible, where less finite resources are used and where all materials are used as long as possible. We select companies that organise their process following principles of the circular economy. Re-use of materials, products and parts of products, reduction of the use of (finite) resources and the recycling of materials are the main ways to contribute to a circular economy. Examples of companies aligned with this theme can be found in the waste management and recycling sector, among companies using product-as-a-service business models and companies which outperform in eco-efficiency combined with product-life extension.

5. Prosperous & Healthy People

All humans have the right to a standard of living that is adequate to maintain health and well-being of themselves and their family – this is one of the human rights laid down in the UN Universal Declaration of Human Rights. In line with this human right, we look for companies that offer solutions for health issues, such as medical technology and healthcare services. Also captured within the theme are companies that offer products and services that help build healthy lifestyles, such as personal hygiene and leisure. In addition, companies that help maintain a good health by preserving the environment are considered.

6. Innovation for Sustainability

Innovation is one of the catalysts for a more sustainable future, but only if steered in the right direction. Examples of products and services that fall in this theme are ICT, cybersecurity, telecommunication and robotics. We look for
companies that are technological front-runners in sustainable innovation and technology not captured by previous themes.

7. Social Inclusion & Empowerment
This theme focuses on the way individuals and groups can take part in society, to develop themselves and prosper. Due to technological development, aging, increased inequality, migration and skill shortages, the active participation of all people is under pressure. A company that qualifies in this theme contributes to the participation of all people in society, and to equality and inclusion in this respect. We invest in companies that provide education, access to media and information, and access to financial services. Additionally, companies that excel as a role model in advancement of social inclusion and equality may also qualify.

Step 2: Minimum standards check and exclusion
We review companies for the possible risk that their business practices could jeopardize the transition we envision by evaluating the company against our process, product and precautionary minimum standards. Companies that do not meet our Minimum Standards are ineligible for investment in our funds.

Every company is subjected to a thorough analysis and, if included in the Triodos investment universe, continuously monitored to see whether it still meets our Minimum Standards. If we find that a company no longer meets these investment criteria or is in danger of no longer meeting the Minimum Standards, we will approach the company and call it to account. If this does not lead to the desired change in behaviour, the company will be removed from our investment universe and the stock or bonds of the company will be divested from all portfolios within a period of three months after removal from the investment universe.

See our Minimum Standards and Exclusions for more details.

Step 3: Integrated analysis – portfolio construction
For companies that have passed the first two hurdles, we then conduct a complete integrated financial and sustainability analysis. This step focuses on the potential impact of sustainability factors on a company's future financial value, making our approach both solutions-focused and forward-looking. The actual portfolio construction is based on a comprehensive risk/return analysis. Stocks or bonds from our sustainable investment universe with the best risk/return perspectives will be added to the portfolio. Based on a long-term investment horizon, our investment approach results in concentrated portfolios with a low turnover.

Equity portfolio
If a company fits with at least one of our seven transition themes, we look for confirmation by checking its vision, mission and culture, as supported by management, to ensure its positive impact. We then identify the company's financial value drivers (the underlying determinants of revenue growth, operating profit margins, capital needs and cost of capital) and evaluate the interplay between financials and sustainability.

We assess how the identified value drivers are affected by the ESG issues Triodos deems most material in the field of operations the company is active in. The outcome of this integrated analysis results in a cashflow-based valuation for the company. The price appreciation potential and fund manager conviction of a company are key elements in the portfolio construction process.

Bond portfolio
As with equities, we first check if the fit of a corporate bond or impact bond with one or more of our seven transition themes is supported by a vision, mission and a culture supported by management to ensure its positive impact. At the same time, we monitor macro-economic developments to determine our view on the development of interest rates and the credit cycle.

Based on this view, we construct a fixed income portfolio with a clear allocation towards the impact themes through corporate bonds and impact bonds.

Triodos Sustainable Bond Fund and Triodos Sustainable Mixed Fund may also invest in sovereign bonds. This bond category is used to manage the interest rate risk, liquidity risk and credit exposure of the portfolio. In the annex you can read more about the selection of sovereign bonds and impact bonds.

Engagement
Engagement with companies is one of the cornerstones of our SRI strategy. Through dialogue we aim to raise awareness of sustainability, to stimulate action and to create lasting positive change.

Engagement starts during the investment selection process and continues after selection into the investible universe. We actively monitor companies, doing full re-assessment every twelve months. A potential breach of Triodos' minimum standards prompts an in-depth investigation and could result in exclusion from the portfolio.

Dialogue with companies
Where appropriate, we discuss substantial and relevant issues regarding companies' ESG performance, aiming to enhance their business performance. Our engagement strategy is designed to have meaningful dialogue with companies, aiming to maximize positive change and create long-term value for all stakeholders of a company, including society as a whole.

To this end, we carefully choose relevant topics, set goals and select the most appropriate engagement type and tools. Fundamental company research, thematic research, and a well-managed relation with companies...
are key ingredients of the engagement strategy. As part of our engagement strategy, we develop an engagement plan, which defines the engagement topics and goals, and describes and motivates the choice of how to engage with a company.

**Voting for change**

We take our responsibility as a shareholder seriously, strongly believing that by exercising our voting rights, we can exert a positive influence on a company’s long-term strategy. Triodos Investment Management has a mandate to vote by proxy at shareholder meetings of all companies that we invest in. We use basic voting advice from Pensions Investment Research Consultants (PIRC), in addition to applying our own voting guidelines. We inform all investee companies about our voting decisions, to stimulate awareness of our vision and the minimum standards we apply.

As an active shareholder, we also attend AGMs to raise questions and encourage continuous improvement in sustainability performance. Whilst the companies we invest in are already top corporate responsibility performers, we challenge them to further improve their sustainability performance in such a way that it benefits not only the shareholders, but all stakeholders.

**Shareholder collaboration**

In addition to seeking dialogue with individual companies, we also regularly work together with other investors, for example pension funds, to further steer sustainable performance. Partnerships with other shareholders help maximise the effectiveness of actions. We participate in the European Social Investment Forum (Eurosif) and four of its national member organisations (UKSIF, Forum Nachhaltige Geldanlage, Dutch Association of Investors for Sustainable Development and SpainSIF), the International Corporate Governance Network (ICGN), Euamedion and United Nations-supported Principles for Responsible Investment (UNPRI). Several of these organisations engage in an active dialogue with listed companies about corporate sustainability or focus on bringing institutional investors together for joint dialogue with companies.

**Wider engagement**

To enable us to maintain our strict minimum standards, we aim to stay on top of changes in best practice and regulation, by engaging with companies, non-governmental organisations, governments and independent experts.

**Transparency**

We believe in full transparency, so that clients can decide for themselves whether our investments match their own personal values. We publish our complete investment portfolios for each sub-fund and our minimum standards online. This information, together with our guidelines on proxy voting, our voting ballots and our annual engagement report, are available at www.triodos.com/en/investment-management. Triodos SICAV I is a signatory to the European Transparency Code since its launch in 2008.

Triodos Bank, March 2018.

Important note: For the implementation of its investment strategy, Triodos Investment Management relies on publicly available information communicated by the companies and countries themselves and by third parties. Triodos Investment Management is therefore unable to ensure that such information is complete and/or accurate. At any time, Triodos Investment Management may reconsider previous investments based on newly available information.
Annex

Selection of impact bonds

Triodos Sustainable Bond Fund and Triodos Sustainable Mixed Fund may invest in bonds that qualify as Impact Bonds, such as green, social and blue impact bonds, climate awareness bonds and/or bonds issued under the Climate Bond initiative. These bonds are listed, euro-denominated and have an investment-grade credit rating.

The selection process consists of three steps:

Step 1: Triodos Bank’s Minimum Standards for the issuer
The Triodos Bank’s Minimum Standards are the starting point. These are absolute criteria Triodos Bank applies to ensure not to fund any business engaged in controversial activities, or activities that are harmful to individuals, society or the environment. The issuer of the impact bonds must comply with these Minimum Standards.

Step 2: Measurable impact
The proceeds of the impact bonds need to be invested in projects that contribute to sustainable activities in one or more of the seven themes: Food & Agriculture, Mobility & Infrastructure, Renewable Resources, Circular Economy, Prosperous & Healthy People, Social Inclusion & Empowerment and Innovation & Technology. Furthermore, the sustainability of the projects financed through the impact bond needs to be measurable, so that the positive impact can be calculated.

Step 3: Sustainable process
In order to become eligible for sustainable investment, impact bonds need to meet the following process criteria:
- Transparency: issuers must be clear on which activities are financed and the investment decision-making process.
- Traceability: the proceeds need to be earmarked, tracked and publicly disclosed (at least) on an annual basis.
- Assurance: activities and practices related to impact bonds require annual verification by an external auditor.

Bonds eligible for investment are monitored on a continuous basis to see if they continue to meet the sustainability criteria.

Selection of sovereign and sub-sovereign bonds

In order to manage the risk profile of their investment portfolios, Triodos Sustainable Bond Fund and Triodos Sustainable Mixed Fund may invest in investment grade, euro-denominated sovereign bonds and sub-sovereign bonds issued by (regional or local authorities of) countries that are a member of the European Union. The selection process consists of the following:

Step 1: Currency and country risk mitigation
Sovereign bonds and sub-sovereign bonds issued by regional or local authorities are used as a liquid, low-risk investment category to manage the risk profile of the investment portfolio. To prevent exposure to currency risk and country credit risk for these investments, only euro-denominated sovereign bonds of investment grade members of the European Union and euro-denominated sub-sovereign bonds issued by regional or local authorities of those countries are selected.

Step 2: Free of international sanctions
Countries (and their regions), eligible for investment for the purpose of currency and country risk mitigation, also need to be free of international (EU and UN) sanctions. Moreover, countries need to have ratified or be in the process of ratifying the most widely accepted United Nations backed conventions including the most important ones focusing on human rights and the environment.

Given the dynamic nature of the process of proposing and ratifying these conventions, the application of this criterion will change from time to time. If a country does not comply fully with this criterion, the background and the materiality of its non-compliance will be assessed as part of the decision to exclude the country for government bond investments or not.