CANDRIAM
A NEW YORK LIFE INVESTMENTS COMPANY

Can emerging markets be sustainable?

60 seconds with the fund manager

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This marketing communication is intended for non-professional investors.

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We need innovative methodologies to apply the ESG (Environmental, Social & Governance) approach to emerging markets, as Paulo Salazar, Galina Besedina and Vivek Dawan, explain.

What challenges do you face when conducting ESG analysis to Emerging Markets?

Sustainable investing in Emerging Markets must overcome a lack of transparency and data, complicated by language barriers and limited access. These arise from cultural differences, the relative immaturity of EM financial markets, and history. Also, we find that EM companies face fundamentally different ESG challenges when it comes to Governance. We check for the overall level of Governance standards, but we have to pay close attention to the ownership structures as well; many EM companies are controlled by only a few shareholders.

Europe and the US have more financial requirements in general, and increasing requirements for ESG data disclosure. These are increasing in Emerging Markets, but they still lag. We believe it won't be too many years before EM disclosure catches up.

Is it possible to perform an ESG assessment for Emerging Market companies?

Candriam has been incorporating ESG analysis in investing since 1996. It is possible to do so in EM Equities, but until the same data is available, there is insufficient information to use the same methods as for DM companies. We have developed since 2008 a specific three-step ESG methodology for EM companies, including a Controversial Activities Check, a Norms-Based Analysis, and Governance Screening.

How do you begin?

We gauge the degree of involvement in controversial activities(1), such as arma ments, tobacco, coal, and businesses in countries with oppressive regimes. We then(2) assess whether the company is aligned with internationally-accepted standards. For example, we exclude companies that fail to meet the Ten Principles of the United Nations Global Compact – including Human Rights, Labour, the Environment, and Anti-Corruption. The third is to analyse corporate Governance, such as shareholder rights and board independence. As EM companies are increasingly willing

60 SECONDS WITH THE FUND MANAGER

(1) The Candriam Exclusion Policy can be downloaded here: https://www.candriam.com/en/professional/insight-overview/publications/
(2) https://www.candriam.com/es-es/professional/insights/publicaciones/#transparency

to dialog with their investors, those with better Governance are more open to incorporating Environmental and Social business strategies in their growth plans.

How can you measure this?

We target a carbon footprint for our Sustainable EM Equity portfolio that is at least 30% less than that of the index. Our in house ESG Analysts, established in 2005, calculates an ESG score for each company in the benchmark. Our objective is that our Sustainable EM portfolio should maintain an ESG score above that of the benchmark.

How do you identify investment opportunities for the portfolios?

Our process combines two unique approaches. First, our proprietary approach to ESG analysis of EM companies to develop the sustainable EM universe. Our Emerging Markets Equities investment process blends a thematic approach of defining supportive trends and "pockets of growth", with fundamental analysis to identify attractively-priced quality companies with strong and maintainable growth. Some of the supportive trends we incorporate include climate change, resource depletion, healthcare, demographic changes, developing economies and inter-connectivity across borders.

How do you maintain diversification in the portfolio?

We construct portfolios of around 100[3] conviction-based names while remaining broadly diversified by country, sector, individual companies and themes. We are able to achieve this through the strength of our multi-disciplinary teams. Our experienced and Emerging Markets team has a track record spanning nearly two decades. We believe we offer a unique strength in our integration of our thematic selection approach to emerging markets with our proprietary ESG methodology.

(3) Datos de carácter indicativo y susceptibles de variar con el tiempo.

Why should investors be interested in this strategy?

This strategy has a positive impact on the Environment, helps raise Social standards and encourages a responsible approach to corporate decision-making. It offers investment exposure to five key types of solutions: Climate Change, Resources and Waste, Digitalization and Innovation, Healthy Living and Wellbeing, and Demographic Shifts. By focusing on issuers that are best-positioned towards ESG challenges and opportunities, our responsible investment approach enables us to optimise portfolio risk/return profile, benefit from macro trends faced by all investors, and deliver a positive contribution to the global Environmental and Social challenges.

Investors are increasingly placing ESG-related considerations at the heart of their investment decisions. This strategy should appeal to investors who apply ESG criteria to their Developed Market portfolios and wish to do the same with their Emerging Market investments. While some institutional investors conduct their own ESG screening in larger markets, they may feel they lack the experience and capabilities needed for ESG analysis of Emerging Market companies. The strategy particularly fulfils the needs of investors who operate in jurisdictions where they are obliged to disclose their sustainable impact.

How do you balance sustainability and investment performance?

At Candriam, it is our conviction that sustainability generates investment performance. We believe that evaluating ESG criteria helps investors identify non-financial metrics which can augment long-term value and helps avoid accidents.

Conclusion? Our aim is to generate alpha from both our ESG analysis and from our thematic and financial selection process.

The main risks of the strategy are:

• Risk of capital loss:

There is no guarantee for investors relating to the capital invested in the strategy in question, and investors may not receive back the full amount invested.

• Equity risk:

Some strategies may be exposed to equity market risk through direct investment (through transferable securities and/or derivative products). These investments, which generate long or short exposure, may entail a risk of substantial losses. A variation in the equity market in the reverse direction to the positions can lead to the risk of losses and may cause the performance to fall.

• Emerging market risk:

Market movements can be stronger and faster on these markets than on the developed markets, which could cause the performance to fall in the event of adverse movements in relation to the positions taken. Volatility may be caused by a global market risk or may be triggered by the vicissitudes of a single security. Sectoral concentration risks may also be prevalent on some emerging markets. These risks may also heighten the volatility. Emerging countries may experience serious political, social, legal and fiscal uncertainties or other events that could have a negative impact on the strategies investing in them. In addition, local depositary and sub-custodial services remain underdeveloped in non-OECD countries and emerging countries, and transactions carried out in these markets are subject to transaction risk and custody risk. In some cases, it may be impossible to recover all or part of the assets invested or delays in delivery when recovering assets may arise.

• ESG investment risk:

The non-financial objectives presented in this document are based upon the realization of assumptions made by Candriam. These assumptions are made according to Candriam's ESG rating models, the implementation of which necessitates access to various quantitative as well as qualitative data, depending on the sector and the exact activities of a given company. The availability, the quality and the reliability of these data can vary, and therefore can affect Candriam's ESG ratings.

• Foreign exchange risk:

Foreign exchange risk derives from the strategy's direct investments and its investments in forward financial instruments, resulting in exposure to a currency other than its valuation currency. Changes in the exchange rate of this currency in relation to that of the strategy may negatively affect the value of assets in the portfolio.

The risks listed are not exhaustive, and further details on risks are available in regulatory documents.