EQ investors

Sustainable Investment Exclusions Policy

Introduction

EQ Investors (EQ) developed its exclusion targets based on a thorough review of the academic and non-governmental organisation (NGO) evidence around inhibitors to the UN Sustainable Development Goals (SDGs). This was supported by target client research and feedback from existing clients.

EQ manages different sustainable investment strategies, which are first and foremost defined by their positive focus on sustainability objectives. The EQ Positive Impact, EQ Future Leaders and EQ Climate Action portfolios all differ in their positive sustainability objectives and cater for the different preferences of our clients. This is what primarily drives our investment selection, management and reporting of the portfolios. Please see our portfolio brochures or impact reporting for more detail on how these differ in their positive impact.

However, it is also important to touch on the exclusions applied by each strategy. The number and degree to which we exclude or avoid “negative” business activities also varies between our portfolio strategies. EQ has research processes in place to assess that eligible funds and companies match the relevant criteria of a given investment strategy. We track all underlying funds and their holdings on a monthly basis, to ensure the exclusions are being observed and to be made aware of any potential red flags. We have an established escalation process that follows any red flags if they occur.

Establishing the exclusions and monitoring thresholds

Below we list the business activities that the portfolio strategies aim to exclude, which are also matched and tested with fund managers’ processes & policies. This provides the first line of defence and is the most important. However, we also monitor each underlying investment within the EQ research team to ensure each portfolio passes with the relevant exclusion categories.

The below listed associated thresholds have been developed to reflect that “zero” exposure is hard to monitor given the lack of transparency in company disclosures on insignificant revenues. For all categories possible, we aim to monitor that holdings do not exceed a 5% (or in rare case 10%) revenue threshold for any given controversial product involvement.

However, poor sustainability data availability still restricts monitoring capabilities in some places, and this is why we have had to set a higher threshold to reflect this for these categories. As a result we monitor certain categories for “core” revenue exposure only, which we define as 40% of revenues. These are categories where external data providers cannot cover our exclusion categories and monitoring is therefore necessarily driven by EQ analysts looking at company reports and accounts feeding into the EQ UN SDG mapping database (data is also used in our reporting).

EQ analysts apply the same threshold to map companies to EQ’s list of UN SDG “negative” categories and thus, we achieve an alignment of exclusion policy and our monitoring capability. 40% gives EQ’s analysts more security that it would be picked up through the tools available to us, and that each company’s status remains relevant over time. Practically, very few businesses involved in these negative categories do so for only a small % of their revenue, it's usually the whole business. Therefore 40% does capture most of the companies that would flag at lower thresholds.

Please see below all relevant negative categories that EQ aims to adhere to, and monitors strategies for, in alphabetical order.

Category	Positive Impact policy	Future Leaders policy	Climate Action policy
Adult entertainment	5%	5%	5%
Air freight and airlines	CORE (40%)		
Alcohol	5%	5%	
Animal farming (meat, dairy, eggs, aquaculture)*	CORE (40%)		
Armaments (controversial)	5%	5%	5%
Armaments (civilian firearms)	5%	5%	10%
Automotive pollution	CORE (40%)		
Cruise Lines*	CORE (40%)		
Fossil fuel servicing, indirect production and distribution (utility gas distribution is excused)	25%		
Gambling (services, operations, products)	5%	5%	10%
Military contracting (non-weapons)	25%		
Military contracting (weapons and weapons-related)	5%	5%	5% (direct only)
Mining	CORE (40%)		
Ocean/Marine freight	CORE (40%)		
Oil & gas electricity generation	CORE (40%)	CORE (40%)	
Oil & Gas exploration & production	5%	5%	5%
Palm Oil	5%		
Pesticides	5%		
Thermal coal extraction	5%	5%	5%
Thermal coal generation	10%	10%	25%
Tobacco	5%	5%	10%
Unhealthy food and beverages	CORE (40%)		

Note on EQ Positive Impact: *Given that the EQ Positive Impact Portfolios aim to invest in companies with net-positive impacts on the UN SDGs, this list of exclusions is not necessarily exhaustive. The portfolios aim to avoid investment in any company that has a net-negative impact on the achievement on the UN SDGs, which is qualitative in nature, and can only be delivered though a best-in-class impact management investment process by the relevant fund managers.*

Integrating exclusions into fund selection

The exclusion policies are fully integrated into EQ's fund selection process. A fund will be recommended as eligible for one or more of the EQ investment strategies, and for this to pass the analysis needs to demonstrate that the applicable exclusions can be adhered to. This forms part of EQ's due diligence questionnaire, our fund manager meetings and will be reflected in the final fund recommendation.

The exclusions may either be adhered to directly, through a matching exclusion policy applied by the relevant fund manager, or indirectly, through an ambitious positive inclusion process.

Monitoring of exclusion adherence

Monitoring primarily occurs at the fund level. Each fund on the EQ BUY list is tagged with the eligible strategies, and if relevant to multiple, will be monitored to adhere the most stringent exclusion targets of the relevant strategies.

a. Monitoring at fund-level (majority of exclusion categories)

For most exclusion criteria, EQ's sustainability and fund research team utilise external independent data sources for monitoring at the fund-level. The source is Morningstar/Sustainalytics negative product involvement data, and MSCI carbon/fossil fuel involvement data.

Each month, a report covering all of EQ's Buy-List funds is prepared that details any negative exposures across exclusion categories at fund-level. Any flag will result in a member of the sustainability team investigating the relevant holding for breaches to the exclusion thresholds set out in our policy.

Whether or not a holding/fund breaches EQ's exclusions remains at the discretion of the analysts, given that the data is not always accurate or up-to-date and definitions can be blurry. Notes on any flags are kept in a centralised location, including the justification for dismissing any flag from Morningstar/Sustainalytics.

b. Monitoring at stock-level (some less common exclusion categories)

EQ's exclusion criteria are more extensive and detailed than most competitor fund selectors. The data providers do not offer coverage for all exclusion categories listed in our policy. For all categories, but especially for those marked with a (*), EQ utilises its own company-level negative mapping database to monitor adherence.

The UN SDG database maps every company to a relevant UN Goal (positive), a set of negative categories (EQ Positive Impact exclusion list) obstructing the delivery of the UN SDGs, or neutral. This database now spans over 6000 companies and will be updated by our sustainability team to reflect new exclusion policy and thresholds of EQ PIP.

c. Escalation process for flagged holdings

EQ predominantly invests in funds, and therefore does not directly hold agency over the buy or sell decision on individual holdings. Therefore, once a holding is flagged through EQ's monitoring processes, we need to apply an escalation process.

1. Qualify the flag: Data received on controversial product involvement is not always accurate or up-to-date, and definitions can be blurry. The first step requires EQ's sustainability team to conduct internal analysis to qualify the flag. At this stage, a flag can be dismissed. Notes on any flags will be kept in a centralised location, including the justification for dismissing any flag from Morningstar/ Sustainalytics.

2. Engage with the fund manager: If a flag is qualified by the EQ analysts or there remains a lack of disclosure, the relevant fund analyst will contact the relevant fund manager to discuss the holding. We herein aim to establish whether the flag can be dismissed or whether it indeed results from a shortcoming in the fund mangers' process of monitoring capabilities. We will then aim to engage to improve processes. This process is limited to six months.

3. Fund conviction: If the engagement fails to result in a change in investment process and the company/fund continues to breach EQ's exclusion policy, it will reflect in a loss of conviction in the fund by the relevant fund analyst. This means alternatives will be sought to replace the fund on the EQ BUY list, and it will be added as a priority to the EQ research agenda. Our aim is to find a replacement in less than twelve months from initial flag.

Reporting and disclosure

The issuer level SDG mapping database is used to map every underlying holding within EQ's portfolios to the highest level of exclusions, defined as those covered by EQ Positive Impact's exclusion policy. This data is integrated into portfolio management systems to inform investment decisions.. The data also informs public disclosures including on EQ's website, portfolio factsheets or impact reports.

Risk warnings

Past performance is not a reliable indicator of current or future performance. The value of investments, including the income from them, can fall as well as rise meaning you may get back less than your invest. Such information is not intended to provide legal, tax, accounting, investment, financial or other professional advice on any matter.

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To discuss our services in more detail please contact us:

020 7488 7110
enquiries@eqinvestors.co.uk
eqinvestors.co.uk