



Sustainability risk policy for investments

Article 3 SFDR

2024



Préambule

Regulation (EU) 2019/2088 of the European Parliament and of the Council of 27 November 2019, known as the Disclosure Regulation or SFDR, lays the foundations for the European sustainable finance framework. This regulation, which came into force on 10 March 2021, sets out demanding rules designed to harmonise the sustainability practices of financial players.

SFDR introduces two concepts relating to the consideration of sustainability factors - environmental, social and good governance factors - in investments. They are closely linked and complementary:

- Sustainability risks: these arise when there is an environmental, social or governance event or situation which, if it occurs, could have a significant adverse impact on the value of an investment;
- Principal adverse impact (PAI): this refers to the negative impact of investment decisions from an environmental, social or good governance point of view.

To ensure transparency for our investors, we publish our sustainability risk policy for investments, in accordance with the requirements of Article 3 of the SFDR regulation. This policy is part of our overall approach as a responsible investor, and complements the various policies and reports published on our website.

Our annual «Article 29 of the Loi Energie Climat» report includes an assessment of climate and biodiversity risks at two levels: on Rothschild & Co Asset Management as an asset manager and a company, and on our activity and the assets we have under management.

<https://am.eu.rothschildandco.com/en/responsible-investing/>

This policy covers Rothschild & Co Asset Management and all the financial products it manages. It presents:

1. Identification of sustainability risks
2. Management of sustainability risks in the investment process
3. Risk management and governance of sustainability risks

1. Identification of sustainability risks

Definition of sustainability risk

Sustainability risk is defined as an environmental, social or governance event or situation that, if it occurs, could have a material adverse impact on the value of an investment.

Sustainability risks form an integral part of the risk maps drawn up by Risk Management and Compliance, as well as the associated controls carried out by these two teams.

Risk Identification

The three families of sustainability risks - environmental, social and governance - cover a wide range of hazards and associated indicators. We believed it was important to identify a short but sufficiently exhaustive list of indicators to cover the major sustainability risks to which our financial products are exposed.

We have chosen to pay particular attention to:

- Climate risks, particularly those of transition. The risks associated with biodiversity are also significant in terms of the potential for adverse impacts.
- Social issues, particularly those relating to working conditions and the quality, diversity and development of human capital.
- Governance issues relating to fraud and corruption, diversity and checks and balances within governing bodies, and making representatives accountable for the company's sustainable strategy.

Indicators have been identified to measure and monitor exposure to each family of sustainability risks. The choice of sustainability indicators was initiated by Risk Management in collaboration with the Sustainable Investment and Compliance teams, and validated by the Investment teams.

For these indicators, we use MSCI ESG Research as our main source.

Each of these sustainability risks and associated indicators is treated without hierarchy in terms of probability of occurrence or potential impact on investment value. Moreover, they are common to all asset classes, regardless of funds' SFDR classification, and regardless of the level of ESG integration in their strategy.

The multi-management activity has a similar sustainability risk map. However, this is less expanded, due to the limited availability of indicators for underlying funds.

Sustainability risk mapping and associated risk indicators

In terms of Environmental issues

Physical climatic risk: risk associated with physical impacts, consequences of climate change

- Acute: extreme events such as floods, hurricanes or avalanches
- Chronic: gradual changes such as rising sea levels and oceans, water stress or rising temperatures

Related indicators:

- Climate VaR: extreme heat scenario, coastal flooding and aggregate indicator for all 10 available scenarios

Climate transition risk: risk associated with new economic, political, technological or market conditions

- Political and legal: increasing the price of carbon emissions or tightening regulations
- Technological: lack of investment in innovations leading to technological breakthroughs
- Market: changes in supply and demand, changes in raw material prices
- Reputation: changing consumer preferences

Related indicators:

- Share of operations in carbon-intensive business sectors
- Share of operations in geographical areas facing high regulatory risk in terms of carbon emissions
- Controversies
- Carbon intensity of companies
- Carbon emissions reduction target approved by the Science Based Target initiative “SBTi”

Biodiversity: risk associated with the diversity of living species and the ecosystems in which they live

- Loss of biodiversity: destruction of natural habitats
- Scarcity of resources: reduced genetic biodiversity

Related indicators:

- Share of operations in business sectors with high potential for disturbance of terrestrial and marine areas
- Exposure to biodiversity and land use

In terms of Social issues

Diversity and Inclusion: risk associated with the lack of equal rights and opportunities in terms of access to employment, training, qualifications, mobility, promotion, work-life balance and pay

- Remuneration: pay gap between employees
- Diversity: lack of diversity and discrimination

Related indicators:

- Gender pay gap
- Discrimination and diversity controversies
- Labour rights: discrimination & workforce diversity

Labour and human capital management: risk of misuse of employees' knowledge and skills, as well as the risk of human rights violations

- Working conditions: low levels of employee satisfaction, difficulties in recruiting talent
- Regulations: regulatory non-compliance

Related indicators:

- Employee turnover
- Human capital development score
- Workforce strike rate
- Compliance with the UN Global Compact and OECD Guidelines for Multinational Enterprises, and monitoring mechanisms

Health and safety at work: risk of workers not being protected against accidents at work and illnesses

- Infrastructure: poorer quality infrastructure leading to injuries
- Hygiene: non-compliance with hygiene measures leading to illnesses

Related indicators:

- Labour rights - employee health and safety
- Share of operations in sectors with high accident and fatality rates
- Controversies related to workplace accidents

In terms of Governance issues

Board of Directors: risk associated with the management body that defines a company's strategy

- Non-independence of the Board of Directors: low level of independence
- Gender inequality: low gender diversity
- Protection of minority interests: inadequate protection of minority shareholders/bondholders from majority interests
- Remuneration policy: risk associated with the remuneration committee

Related indicators:

- Independence of directors, Chairman and Lead Director
- Gender diversity on the Board of Directors
- Shareholder score and control
- Independence of the Remuneration committee
- Concerns relating to the Remuneration committee

Business ethics: risk associated with the behaviour of a person accepting benefits of any kind in order to perform an act within the scope of his or her duties, as well as with litigation

- Unethical behaviour: cases of corruption and controversy

Related indicators:

- Corruption controversies
- Anti-corruption policies
- Tax controversies

Transparency of external controls and documents: risk associated with regular controls of companies and financial/extra-financial documents reflecting their true status

- Regulations: non-compliance with financial and tax accounting requirements

Related indicators:

- Auditor's term of mandate
- Audits of ethical and anti-corruption practices
- Independence of the audit board/committee
- Tax transparency

2. Managing sustainability risks in the investment process

Rothschild & Co Asset Management approach to sustainability risk is fully integrated within its financial risk approach. It is used to monitor portfolio exposure to sustainability-linked hazards, to which all financial products are subject. Thus, we apply the same level of thoroughness and robustness to the sustainability issues monitoring, as we do to the financial aspects.

Sustainability risks monitoring is managed by Risk Management.

Control framework and warning thresholds

The control framework is common to all direct and multi-management financial products, regardless of asset class, SFDR classification or level of ESG integration in the investment strategy.

These indicators are monitored by Risk Management on a granular basis. The control framework varies according to the indicators. This may involve:

- A follow-up of the indicator's evolution over time,
- A maximum threshold not to be reached for the financial product, or
- A warning threshold for the issuer or a formal prohibition on investing.

Warning thresholds have been determined within a preventive framework in order to target the limits of non-alignment of companies with the strategy and responsible commitment of Rothschild & Co Asset Management investments, and to prevent potential financial risks that could impact the value of investments.

Indicators and thresholds are voluntarily the same, regardless of the issuer's geographical area or business sector.

Adjustment of the process and the chosen indicators depends on their evolution: in a context of constant change and improvement in ESG matters, the control framework is reviewed annually. Adjustments may concern the indicators selected, the levels or types of thresholds, the frequency of calculation, the reinforcement of the alert severity level or the introduction of «hard» constraints.

Monitoring tool

Rothschild & Co Asset Management has developed an in-house sustainability risk monitoring tool. This tool is a means of exchange between Risk Management and the Investment teams. It shows results of the above-mentioned indicators, and which financial products are vulnerable to one of the risk families, while identifying the issuers contributing to this vulnerability. The tool also makes it possible to track the evolution of these indicators over time and identify trends.

The data used to map sustainability risks is updated every six months. Financial products and issuers that have exceeded their alert thresholds are discussed and acted upon by analysts and investment managers. In practical terms, issuers with the most negative and/or least positive sustainability performance are subject to in-depth and rigorous analysis. The selected issuers profiles are reviewed and linked to market dynamics, sector trends and strategic developments. This analysis is carried out in collaboration with various management expertise's analysts to broaden the perspective and ensure the right match between the results provided and the profiles of the issuers concerned.

This proactive, data-driven approach strengthens Rothschild & Co Asset Management's ability to make decisions and continuous progress towards its sustainability goals.

This monitoring helps to raise awareness of sustainability risks among all our Investment teams. In fact, every employee has access to the internal monitoring tool. This control makes it possible to extract most relevant information in the light of established thresholds for each indicator and investment strategies of the various portfolios. Finally, the tool is reviewed at least once a year to ensure that it remains in line with best practices and constantly evolving standards.

Integration

Risk Management is responsible for integrating these indicators into the operational systems and calculating them at portfolio level. It is responsible for informing managers of any particular exposure to a hazard.

Focus on the E, S and G pillars

To identify any weak signals and areas of risk within the issuers in portfolios, and in addition to the indicators selected within the sustainability risk map, E-S-G pillar scores below 2 out of 10 are monitored by Risk Management.

If a trade is initiated for a company with a pillar rating below the threshold, the order placement system alerts the manager during the pre-trade phase. In addition, on a quarterly basis, Risk Management produces a summary and informs the managers concerned by investments in this type of issuer. It also keeps the organisation and its managers informed through the Risk Committee.

Focus on physical climate risks

As a result of climate change, we are seeing an increase in the frequency, intensity and duration of climatic hazards. This has a direct impact on the economic and financial performance of companies.

Rothschild & Co Asset Management has therefore integrated the risks associated with climate change into its investment strategies and monitors their development.

We carry out an indicator of potential loss of a company's market value under a given extreme climate scenario: the Climate Value at Risk (Average outcome). The potential loss figures for a company are subject to an internal limit which serves as a warning reference. If this limit is exceeded, an alert is sent to investment managers.

The results calculated on all our outstandings are presented in our annual report on Article 29 of the French Energy and Climate Law. The latest report is available on our [website](#).

Climate VaR is an indicator developed by MSCI ESG Research. This indicator is designed to align with the recommendations of the Task Force on Climate Related Financial Disclosure (TCFD), which recommends calculating the impact of climate scenarios on the value of invested portfolios. Climate VaR assesses the potential consequences of an extreme climate scenario on a company's market value. MSCI ESG Research model:

- Covers 300,000 financial instruments, but does not cover mutual funds
- Models ten extreme climate hazards
- Incorporates future technology opportunities
- Calculates and analyzes transition risks for +1.5°C, +2°C and +3°C scenarios

MSCI ESG Manager considers 10 specific event scenarios: extreme heat, coastal flooding, river flooding, precipitation, low river flow, tropical cyclones, extreme wind, extreme cold, extreme snowfall and fire. Our supplier also gives us access to an aggregate scenario corresponding to the sum of the results of the previous 10 indicators.

For the purposes of our Article 29 report, we have chosen to use the Climate Var aggregate indicator, whose results are mainly influenced by two out of the 10 scenarios proposed: extreme heat and coastal flooding. These two scenarios give discriminating results from one issuer to another, and have the greatest impact on all our assets. However, our risk mapping for physical risks includes all three indicators.

Principal adverse impacts (PAI)

The principal adverse impacts (PAI) defined by the SFDR regulation correspond to the adverse impact of an investment decision on a sustainability issue and constitute for us a complementary tool for monitoring our sustainable trajectories and our investment choices.

There is a link between PAIs and sustainability risks, creating a certain synergy underlined by the principle of double materiality.

We believe that the selection of indicators meeting these two criteria is more representative of the interdependence link.

More details on our policy of taking into account the main negative impacts are available in a dedicated policy, published on our [website](#).

3. Risk management and governance of sustainability risks

The Risk Management team

Rothschild & Co Asset Management has a permanent Risk Management function that is hierarchically and functionally independent of the operating units. It reports directly to the Managing Director, and functionally to the RMM Group Risk Manager. The Risk Management function has the human and technical resources it needs to carry out its duties effectively. The company does not use a third party for this activity.

Risk Management is responsible for measuring and monitoring all the risks associated with portfolio management, including sustainability risks.

On a day-to-day basis, Risk Management monitors the limits imposed by more specific fund constraints (AMF doctrine, SRI or Towards Sustainability labels, SFDR regulations).

The main aim is to ensure compliance with:

- Product-specific exclusions,
- Targets for weighted average ratings and floor ratings for issuers,
- Performance and/or coverage targets for sustainability indicators,
- Minimum taxonomic alignment and sustainable investment,
- Reinforcement/purchase bans in the event of controversy,
- And the calculation of PAIs (principal adverse impacts),
- And the consistency of portfolios with their initial investment universe.

If these limits are exceeded, Risk Management is responsible for passing on the information within the organisation.

The Risk Committee

Sustainability risks are also monitored on a monthly basis by the Risk Committee. The purpose of the Risk Committee is to carry out a monthly review of risk monitoring of UCIs and mandates. At this committee meeting, the Risk Management function reports on the performance of its tasks.

It is made up of permanent members representing the entity's various management, consultative and decision-making bodies, including:

- Managing Partners,
- Head of Compliance and Internal Control,
- Chief Risk Officer,
- RMM Group Risk Manager,
- Heads of Asset Management Divisions,
- Multi-management Division Analysts Manager.

This committee informs its members of the levels of risk incurred by the funds, raises managers' awareness and makes collective decisions. With regard to sustainability risks, Risk Management ensures:

- Compliance with the sustainability policy and the derogation agreement,
- Monitoring alerts on indicator limits and investment/adjustment decisions,
- Analyses and trends relating to these risks,
- Raising management teams' awareness of sustainability risk,
- Any other related subject.

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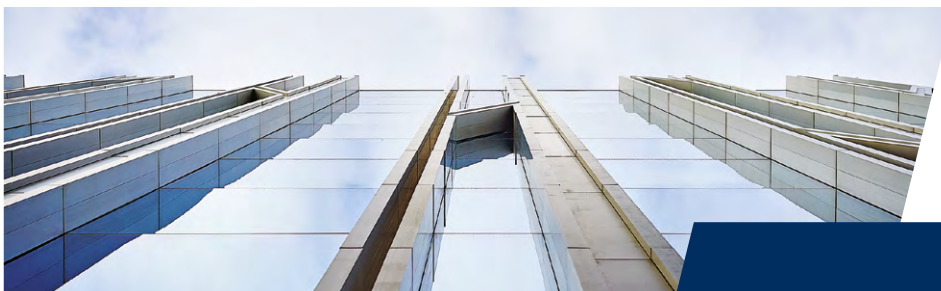
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