Investing with principles

Our guide to responsible investing

BMO Global Asset Management

Contents

What is responsible investing?

Investment priorities are changing. More and more people are concerned both with the investment returns they can make on their savings, and whether their money is being managed in a sustainable way.

Reasons why you may want to invest responsibly...

- You may not want to invest in companies that pollute or damage the environment, deal in the arms trade or support child labour.
- You may not want to tolerate tobacco companies or those that profit from gambling, pornography or the production of alcohol.
- You may want to invest in funds run by managers who engage with the companies they invest in to encourage them to improve their business practices.
- You may want to invest in companies actively working to find solutions for global challenges such as climate change.

Making a difference

More and more we are trying to "do our bit" – we recycle our waste, perhaps buy free range or organic food, and seek out more energy-efficient white goods. We can extend this principle to our investment decisions too.

As the saying goes "money talks". It's true – we can make a difference by where we choose to invest our savings, pensions and ISAs without compromising on the opportunity to grow our money.

On the following pages we share our thoughts on responsible investing. As ever, the world of investments is about expectations, not certainties. However, the views we hold are all based on over 30 years' experience running a broad range of investment funds with a responsible remit.

Understanding 'ESG' – three key areas in responsible investing.

Environmental – how does a company's activities impact on the world? If they pollute for example, what steps do they take to reduce their contribution to things like global warming?

Social – here we consider factors like how a company treats its workforce, suppliers and customers.

Governance – this relates to how a company is run. Does a company have the right structures in place to ensure it is well managed? And how does it decide executive pay?

Paying the price

History provides many examples of what can happen when businesses fail to consider and prioritise environmental, social and governance (ESG) related factors. By investing in a responsible fund, you can avoid investing in companies operating in a manner that contradicts your values. The investment merits of such an approach are increasingly recognised.

Deepwater Horizon disaster

In April 2010, the explosion and sinking of the BP operated Macondo Prospect led to the Deepwater Horizon disaster, the largest marine oil spill in US history. BP bore the brunt of blame with cost-cutting and poor safety systems cited as contributing factors. BP's share price lost 50% between 20 April 2010 and 29 June 2010 and the total costs borne by BP were around US$62 billion.

"The way people's pensions and savings are managed should not be isolated from their personal values."

The Most Reverend Justin Welby, Archbishop of Canterbury, President of the BMO Responsible Investment Advisory Council

Volkswagen emissions scandal

Announcements by Volkswagen in late 2015 about manipulation of emissions data of engines, reportedly affecting over 11 million vehicles worldwide, raised extremely serious concerns about the commercial impact on the company, the reputational impact on the Volkswagen brand and the potential penalties arising from legal action in the US and Europe. At the time of writing the company has already provisioned costs of €18 billion.

Rana Plaza collapse

In April 2013, the Rana Plaza clothing manufacturing factory collapsed in the Bangladeshi capital of Dhaka. The incident resulted in more than 1,100 fatalities and was a result of poor building structure. Many international clothing brands were supplied directly and indirectly from the factory. It brought worldwide attention to the working conditions in Bangladesh as well as the practices of the global multi-national corporations sourcing from the country.

The new investment reality – performance of responsible funds

When responsible investing first began, the perception was that principles might mean a trade-off with investment returns. But over the three decades that we have run responsible funds, our experience is that by avoiding companies with poor environmental, social and governance credentials, and positively targeting companies that respect their workforce, suppliers, customers and the environment, we can make good choices and always strive to deliver strong long-term investment returns.

Performance with principles

But don't just take our word for it. Numerous studies have looked at how sustainability and governance link to a company's performance and that of its shares.

Responsible investing moving mainstream
The UN Principles for Responsible Investment have more than 2,000 signatories from over 60 countries, representing over US$80 trillion of assets.[1]
88% of senior business leaders believe that greater integration of sustainability issues in financial markets will be essential to making progress.[2]
Barclays found that a portfolio of corporate bonds[3] biased towards companies with good governance generated 5.5% outperformance over 7 years versus companies without good governance.[4]
A review of over 200 academic papers found that 88% showed a link from good ESG practices to good business performance.[5]
Morgan Stanley analysed over 10,000 open-ended[6] mutual funds[7] over 7 years – 64% of the sustainable equity[8] mutual funds had equal/higher returns and equal/lower volatility compared with non-ESG products.[9]

But isn't responsible investing riskier?

Investing places capital at risk and it's generally known that diversification (holding a selection of different investments) reduces risk, so if you screen companies out on ethical grounds, you are potentially limiting the number of companies you can invest in. As a result, you may be taking on more risk.

The flip side is that less responsible companies are running risks to their business by neglecting social or environmental practices. This puts them at risk of a whole range of costs such as regulatory fines, supply chain interruptions, labour disputes, or loss of reputation. This could then have a detrimental effect on their credibility, performance and future profitability.

Our belief is that sound corporate governance, robust management of environmental and social risks, and the pursuance of strong business ethics play an increasingly important role in delivering investment performance.

For some of our funds, it is true that ethical exclusions do mean that some industries like tobacco, defence and oil and gas are largely excluded. In the short term, if these industries do well, the funds might feel the impact. But our experience over three decades is that in the long term, our responsible focus gives us an edge. By choosing companies with a strong responsible track record, we can identify good quality investments that help us deliver our investment objectives.

[1] UNPRI (United Nations' Principles for Responsible Investment) 2019
[2] The UN Global Compact – Accenture CEO Study on Sustainability 2016 "Agenda 2030: A Window of Opportunity" (Accenture, 2016) https://www.accenture.com/us-en/insight-un-global-compact-ceo-study-sustainability
[3] A form of loan issued by a company in order to raise capital and an alternative to issuing stock through a rights issue. Bonds pay a fixed rates of interest over a fixed term, with the principal repaid at maturity.
[4] Barclays – Sustainable investing and bond returns https://www.investmentbank.barclays.com/our-insights/esg-sustainable-investing-and-bond-returns.html
[5] From the Stockholder to the Stakeholder – How Sustainability Can Drive Financial Outperformance, (University of Oxford & Arabesque Asset Management, March 2015)
[6] Investment funds that are not restricted in the number of shares they may issue.
[7] An investment vehicle made up of funds collected from many investors for the purposes of investing in securities.
[8] Shares in a company listed on a stock exchange. Shareholders are effectively the owners of the company and typically have the right to vote on company matters.
[9] Morgan Stanley Sustainable Reality Report – http://www.morganstanley.com/sustainableinvesting/pdf/sustainable-reality.pdf

“The good news for investors is that there is now an unprecedented choice of funds with an ESG approach.”

Claudia Wearmouth,
Co-Head, Responsible Investment

Responsible funds
– what are your options?

The amount of money invested in responsible funds has grown rapidly and the popularity of responsible investing looks set to continue.

When thinking about whether to invest in a responsible fund, there are two main considerations. The first is the ability of the fund manager. As with any investment, you should have confidence in the quality of those you select to be responsible for managing your money.

Second, you need to understand the ethical and ESG criteria followed. What sort of companies are considered for investment, and what checks are in place to ensure these criteria are rigorously applied?

Most responsible funds tend to screen out, or avoid investing in, certain companies on ethical grounds. There is, however, a range of approaches to choose from. Some combine more than one approach – such as our own BMO Responsible Global Equity Fund, which has ethical exclusions, a positive thematic approach to company selection, and engagement. Screening, thematic investment and engagement are explained below.

Screened funds

Sometimes also known as Responsible, SRI (Socially Responsible Investment), ethical or "dark green" funds. These have the strictest investment criteria, and avoid investing in any company that may have a poor record on environmental, human rights or other ethical grounds. Dark green funds normally exclude companies in industries such as defence, tobacco, gambling and alcohol.

May be suitable for: investors wishing to align their investments with moral or ethical values.

Best-in-class funds

Also sometimes termed "light green" funds. These take a 'best in sector' approach – not excluding whole industries, but concentrating on the most socially responsible companies in a particular sector.

May be suitable for: investors who want their manager to look at environmental, social and governance issues but don't feel comfortable with excluding entire industries.

Thematic funds

Thematic, sustainable or, more recently, impact funds select companies on the basis of their positive contribution to environmental or social solutions. Some funds focus on one theme such as water or healthcare, but more often you will find multi-themed funds which offer access to a range of related themes.

May be suitable for: investors looking to generate performance from companies involved in industries of the future.

Engagement funds

This approach means that the fund manager is committed to engaging in dialogue with the companies they invest in on a range of sustainability or governance issues, as well as using their right to vote on major corporate issues at shareholder meetings. This is a strategy that can be applied to any type of fund, whether exclusionary or not.

May be suitable for: investors who want their managers to be actively involved in engagement with companies.

The Sustainable Development Goals – **roadmap to a better future**

By investing in companies and using the Sustainable Development Goals (SDGs) as an engagement framework, we believe we can contribute to building a more sustainable world.

Individuals increasingly want to make a positive impact. As consumers, there is a growing recognition that we can align our investment decisions with our values. Ultimately, we want our money to drive improvement in the world around us.

Finding solutions typically requires a global perspective together with commitment and coordinated action from international organisations, governments, companies and individuals. We all have a role to play and the Sustainable Development Goals (SDGs) were designed with that in mind.

The SDGs set out a roadmap for a more sustainable global economy and society by 2030. Developed by the United Nations, they were endorsed in 2015 by all 193 member states.

The 17 SDGs are ambitious high-level goals with 169 granular targets, which provide a universally-recognised framework for assessing and accelerating progress towards a more sustainable world. The SDGs provide a clear framework for our investment specialists to encourage improvement within investee companies.

"We exist to convene, catalyse and empower change that sustains growth for good"

Darryl White, Chief Executive Officer
BMO Financial Group

World Economic Forum, 2019

Our credentials in responsible investment

At BMO Global Asset Management we have worked in this area for over 30 years. We manage a wide range of fund types for both private investors and institutions, across equities[10] and bonds[11] as well as geographic regions.

BMO Global Asset Management's Responsible Investment (RI) team is one of the largest RI specialist teams in Europe. We were also the first fund management group to employ an independent advisory body to oversee our responsible screening process and, in 1984, we launched Europe's first ethical fund for private investors.

Our range of responsible funds forms only part of our approach and related activities. At BMO Global Asset Management, we are committed to being a responsible investor. We believe that prudent management of ESG issues can have an important impact on long-term investment performance. Companies that successfully manage their ESG risks, and proactively follow ESG best practices, may outperform other companies over the longer term.

Material ESG considerations feed into our wider investment decisions. Our research analysts and fund managers[12] follow a process that considers the potential impact of ESG issues related to investments in our portfolios.[13]

We were a founding signatory of the UN Principles for Responsible Investment (UNPRI), and as a group we received the maximum possible A+ rating for our governance and strategy.*

16
professionals in our Responsible Investment team

A+ Rated*
by UN Principles for Responsible Investment

1984
Launched Europe's first social and environmentally screened fund

665+
Companies engaged with in 2018

£3.0bn
Assets under management in Responsible Funds**

* See our Transparency Report (www.bmogam.com/documents/principles-for-responsible-investment-transparency-report). This rating is for our Strategy and Governance and should be taken in the context of the full methodology of the UN Principles for Responsible Investment reporting framework. See www.unpri.org for details. ** As at 30 April 2019.

[10] Shares in a company listed on a stock exchange. Shareholders are effectively the owners of the company and typically have the right to vote on company matters.

[11] A form of loan paying a generally agreed rate of interest over a fixed term, with the principal (original sum borrowed) paid at maturity (end date of the loan). Bonds may be issued by governments or companies. Bonds can generally be traded on the stock market and therefore may trade above or below their issue price (price at which the security was initially made available for purchase).

[12] The people responsible for the day-to-day management of the fund.

[13] The collection of investments held by an investor or a fund.

A clear philosophy

Our range of responsible funds offer you a way to invest in the shares and bonds of companies that adhere to certain values and standards. We do this by applying ethical and ESG principles to the selection of investments and their ongoing management.

Our responsible funds are built around a three-pronged philosophy of:

Invest: we invest in companies that are making a positive contribution to society and the environment;

Avoid: we avoid companies with damaging or unsustainable business practices;

Improve: we use our influence as an investor to encourage best practice management of environmental, social and governance issues through engagement and voting.

How do we set the ethical and responsible standards?

Ethics are not black and white. Whilst some standards, such as the exclusion of tobacco producers, are straightforward to implement, deciding whether companies have strong enough processes and performance in areas like climate change, labour standards and pollution control requires careful analysis, consideration and judgement.

And ethical norms and perceptions change over time. In the three decades since our funds were first launched, we have kept our criteria under continuous review, and developed new standards in areas such as oil sands, bank business ethics and climate change.

Every company selected for investment in our responsible funds is researched in-depth, by our Responsible Investment team. They assess whether it satisfies the ethical and sustainability criteria of the fund. Borderline cases are referred to the Responsible Investment Advisory Council for their views. The Council meets quarterly with the team, to discuss both updates to our criteria and standards, and how these are applied in practice.

Active ownership

Once we have invested, we are active owners. We engage with companies to address ESG risks and exercise our voting rights to encourage good governance. We view engagement as critical in ensuring that positive ESG momentum is maintained. In turn, this helps support long-term risk management and performance.

We track and measure the impact of our engagement with companies. Examples of results achieved include:

Royal Dutch Shell: set reduction targets for methane emissions, a potent greenhouse gas, from natural gas production. Tackled methane leakage across its operations.

Inditex: collaborated with peers to improve wages along apparel supply chains. Leads to address industry risks related to high employee turnover, reduced productivity and social unrest.

Danske Bank: removed its CEO and Chair in a welcome move to draw a line under past governance shortcomings.

Disgarded ocean waste.
SDG targets 12.5 and 14.1.

Improve

We believe that the best way to achieve our engagement goals is by constructive dialogue with key decision makers on the most relevant ESG issues to each company.

Investing with impact

Our objective in analysing the impact of our engagement is to understand how the companies in our strategies contribute to sustainable development – by delivering solutions to sustainability needs through their products and services, and through the way they operate their own businesses.

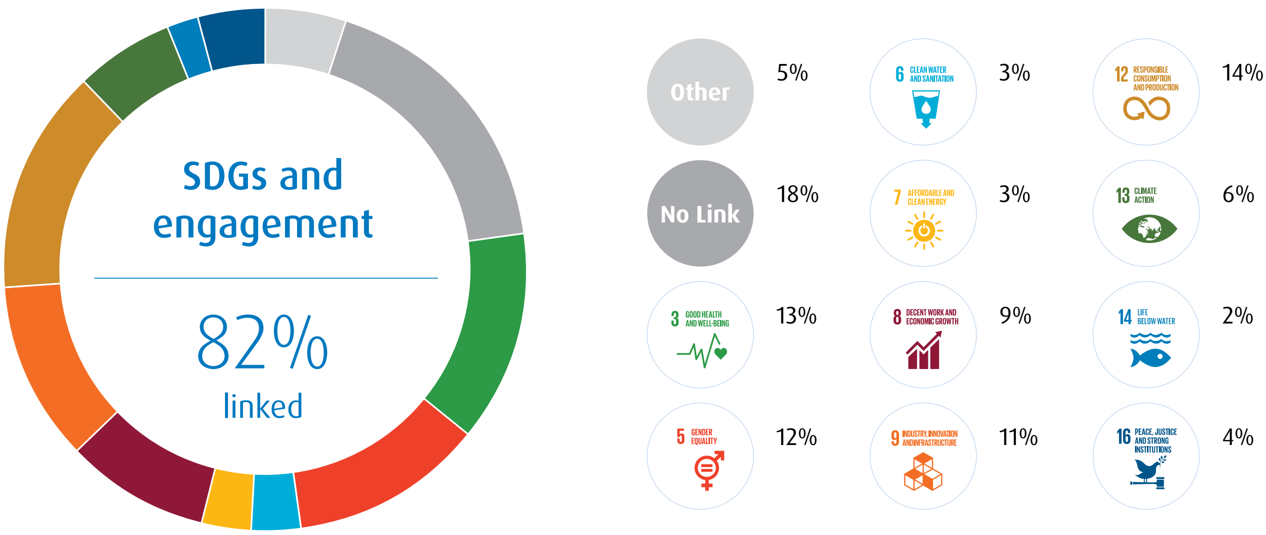
Measuring impact presents challenges, including the fact that companies have a multitude of impacts – some positive, some negative – which cannot be simply netted off to achieve a single score. There are also obstacles in finding relevant, reliable data. Even companies with strong sustainability standards are at early stages of translating this into impact.

Our starting point was the 17 SDGs. As shareholders we discuss important environmental and social issues with the companies we, and our clients, invest in to create positive behavioural change. We are engaging with companies on SDG targets where we can have the most impact and influence. We aligned our engagement to the SDGs in order to gain a clearer picture between initiatives and objectives.

In 2018, we mapped the activities of companies we invest in to the SDGs. We have also looked at the extent to which companies reference the SDGs in their own reporting. 24 of our 55 holdings do so; this shows an encouraging level of awareness, though does not on its own provide proof that actions are being taken in response.

This approach creates a greater possibility of impact from our engagement. By using the common language of SDGs, investors and companies can create a more efficient engagement relationship. The link between the SDGs and engagement, in our view, is one of the most direct ways that investors can see real sustainability impact from the actions they take.

Alignment of our engagement in 2018 to the SDGs



Our fund range

We manage a range of funds offering responsibly-minded investors a choice of income and/or growth focused options.

	BMO Responsible Global Emerging Markets Equity Fund	BMO Responsible Global Equity Fund		BMO Responsible Sterling Corporate Bond Fund	BMO Responsible UK Equity Fund
Summary	This fund seeks to deliver long-term capital growth by investing in the world's emerging markets.	This fund aims to provide capital growth by investing in an ethically-screened and diversified portfolio of sustainable global equities. It uses positive themes to drive portfolio construction.		This fund aims to deliver an attractive level of income through investment in a portfolio of ethically-screened UK corporate bonds. The fund aims to deliver the same level of returns as an unscreened portfolio.	This fund aims to achieve long-term capital growth with some income from ethical investment in a diversified portfolio of equities.
Aim	Long-term growth	Long-term growth		Income with some scope for long-term growth	Long-term growth
Invests in	Emerging market equities	Global equities		Investment grade corporate bonds	UK equities
Structure	SICAV	OEIC	SICAV	OEIC	OEIC
Sector	Lipper Global Equity Emerging Market Global	IA Global Growth	Lipper Global Equity Global	IA £ Corporate Bond	IA UK All Companies
Launch date	01/07/1994	13/10/1987	12/12/2005	01/10/2007	01/06/1984
At a glance					

Thematic – The portfolio is orientated around defined themes such as technology, resource efficiency and sustainable mobility.

Screened – Companies involved in areas like tobacco and gambling are excluded. Each company must be 'approved' before the fund manager invests.

Engagement – Active ownership to address ESG risk and opportunity.

"I am proud of our heritage and track record in responsible investing, which allow us to offer our clients a range of market-leading funds"

Kristi Mitchem, Chief Executive Officer
BMO Global Asset Management

BMO Responsible UK Income Fund	BMO SDG Engagement Global Equity Fund	BMO Sustainable Opportunities Global Equity Fund
This fund aims to achieve income with capital growth from ethical investment in a diversified portfolio of equities.	This fund aims to provide capital growth by investing in a well-diversified selection of global small and mid-sized companies. The fund seeks to achieve a positive impact through targeted, impact-focused, active engagement with companies, using the SDG framework.	This fund aims to achieve medium to long-term capital growth, with some income.
Income and long-term growth	Long-term growth	Long-term growth
UK equities (up to 20% corporate bonds)	Global equities	Global equities
OEIC	SICAV	OEIC
IA UK Equity Income	Lipper Global Equity Small/Mid Cap	IA Global
13/10/1987	01/03/2019	09/09/1987

Risks to consider

The value of your investments and any income from them can go down as well as up and you may not get back the original amount invested. Changes in rates of exchange may also reduce the value of your investment.

Screening out sectors or companies may result in less diversification and hence more volatility in investment values. Investing in emerging markets is generally considered to involve more risk than developed markets due to the possibility of low liquidity, high currency fluctuation, the adverse effect of social, political and economic security, weak supervisory structures and weak accounting standards.

Please note that we cannot give you any advice on the suitability of investing in our funds.

The OEIC funds are sub-funds of the BMO Investment Funds (UK) ICVC V, an open-ended investment company with variable capital (ICVC) incorporated with limited liability and registered in England and Wales under registered number IC 118.

The SICAV funds are sub-funds of the BMO Investments (Lux) I Fund, a limited liability company organised as a société d'investissement à capital variable ("SICAV") under the laws of the Grand Duchy of Luxembourg.

Prospective investors should consult the Key Investor Information Document for the relevant share class before investing, which is available from your financial adviser or BMO Fund Management Limited.

Want to find out more?

For more information on BMO Global Asset Management or our range of funds please contact your financial adviser.

Information in this publication are intended only to provide a general outline of the subject and should not be considered advice, comprehensive nor a sufficient basis for making decisions. The opinions given are relevant at the time of going to press and may change in the future. Investors requiring advice on their individual circumstances or if unsure about a financial decision should consult a professional adviser.

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