Ireland Strategic Investment Fund

Sustainability and Responsible Investment Strategy

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Gníomhaireacht Bainistíochta an Chisteáin Náisiúnta
National Treasury Management Agency

Ciste Infheistíochta Straitéisí d'Éirinn
Ireland Strategic Investment Fund

Ireland Strategic Investment Fund (ISIF) Sustainability and Responsible Investment Strategy

This strategy document outlines, at a high level, the sustainability and responsible investment principles of the ISIF. The design and implementation of such a strategy is typically not an "all or nothing" decision. This strategy aims to address these issues at an overall fund level and will evolve over time as ISIF refines its approach to integrating material environmental, social & governance (ESG) issues into investment decision making across a range of different sectors and asset classes.

1. *ISIF - A universal owner and long-term investor*

The NTMA, as controller and manager of the ISIF believes that the Fund, as a large and long-term investor in Ireland, has a duty to actively contribute to the sustainability of the Irish economy for future generations and to encourage others to do the same.

As a Universal Owner[1] the ISIF owns a share of both the Irish and global economies and its actions need to be considered in the context of wider economic sustainability. ISIF wants to achieve better risk-adjusted returns from market exposures by removing inefficiency and costs associated with poor management of environmental, social and governance (ESG) issues – they are important drivers of long-term success and their inclusive consideration will benefit the ISIF not just through each transaction, but also at an overall portfolio level.

The NTMA believes that responsibly managed companies are best-placed to achieve a sustainable competitive advantage and provide strong, long-term investment opportunities. Organisations that manage ESG factors effectively are more likely to endure and create sustainable value over the long term than those that do not. Therefore the ISIF will endeavour to be a responsible investor, actively integrating ESG factors into its decision-making processes with a view to enhancing the overall outcomes for the Fund and ultimately its beneficial owner.

The overarching objective of the sustainability and responsible investment strategy is to protect and enhance both the value and the reputation of ISIF investments for the long-term through responsible investment practices and ESG risk mitigation – the tenets of sustainability. At all times the ISIF's investment strategies and portfolio management activities will have full regard to the maintenance of its reputation in both the Irish and global markets.

The ISIF's long-term commercial and economic impact mandate is a sustainability mandate.

[1] The Universal Owner hypothesis is that there are clear links between the performance of large, diversified investment portfolios and the economy overall.

2. *Investment Beliefs*

The NTMA's investment approach is founded on the principle that the design of the ISIF portfolio should reflect solidly based investment beliefs, which capitalise on its competitive advantages that deliver a risk diversified portfolio. Those investment beliefs, as they relate to responsible investing, include, but are not limited to the following:

- Regulation can affect the price of assets by influencing the type of assets which regulated institutions demand.
- Real assets will outperform financial assets over the longer term, driven by economic growth, which in turn is driven by productivity gains and demographics.
- Risk diversification is critical.
- A long-term investment horizon is an advantage given short-term volatility, which is inherent in real asset investments, can be accepted as a trade-off for higher return.
- Environmental, social and governance factors can affect long-term portfolio performance.
- All else being equal, lower volatility is better than higher volatility.
- Risk is multi-faceted and not fully quantifiable.

3. *Investing in Ireland to highest global standards*

One of the ISIF's core investment principles is to "to invest in accordance with global best practice standards of corporate governance, active ownership and with the UN-sponsored Principles for Responsible Investment (PRI)". As a founding signatory[2] to the Principles of Responsible Investment (PRI), the ISIF will continue to be guided by these six principles (Schedule A).

The ISIF, as a member of the International Forum of Sovereign Wealth Funds is also committed to the Santiago Principles, a set of 24 guidelines that assign "best practices" for the operations of Sovereign Wealth Funds (SWFs) largely focused on transparency, appropriate governance and accountability arrangements as well as the prudent and sound conduct of investment practices by SWFs (Schedule B).

[2] As the National Pensions Reserve Fund (NPRF), the predecessor to the ISIF.

4. Key Principles - environmental, social and governance (ESG) risks and opportunities

Environmental

- The ISIF aims to prioritise climate change risk and resilience considerations as part of environmental considerations.
- At a minimum, all ISIF investments need to meet legal and regulatory environmental requirements.
- Agriculture, one of Ireland's largest sources of emissions, will require a particular focus on energy efficiencies and environmental best practices.
- Investments should also anticipate both the complexity of climate change risks and opportunities which need a longer-term perspective.
- The ISIF will adopt a portfolio level approach in support of the transition to a low-carbon economy.

Social

- Social issues are relevant in the context of labour relations, health and workplace safety and stakeholder concerns and also managing reputation risk.
- ISIF investments should be aligned with the UN Guiding Principles on Business and Human Rights.

Governance

- Governance is at the heart of any ESG policy - high standards of corporate governance reduce risk and are linked to high quality business and management performance.
- The ISIF has a responsibility to ensure that all its investments are managed in line with an appropriate and best practice corporate governance regime and adhere to the relevant governance codes and guidance.
- The Fund aims to operate in line with the Santiago Principles (Schedule B). The ISIF will publish an annual self-assessment against the Santiago Principles.

Climate Change

As a long-term investor, the ISIF is exposed to climate change – it is a long term and material risk for the Fund. With policymakers and individual companies increasingly taking action, investors also have a role to play in tackling climate change and doing so is entirely consistent with our mandate.

The first step is to understand our own carbon exposure by measuring the ISIF's carbon footprint. This will be undertaken in phased manner and will be dependent on data availability and quality. The next step will be to mitigate the Fund's carbon exposure by setting a goal to reduce emissions over time, thereby contributing to an orderly transition to a low-carbon economy. This process of decarbonisation of the economy is expected to take time, as countries and industries gradually transition away from using fossil fuels towards sustainable energy sources.

5. *ISIF's Sustainability and RI/ESG strategies*

Primary implementation strategies and tools	
1. Integrated analysis	The ISIF integrates ESG issues into its decision-making processes both pre and post investment. At a minimum this contributes to prudent risk management and investment analysis, and over the longer term can positively impact both the value and sustainability of the underlying investments.
2. Active ownership	As a sovereign fund the ISIF is both an investor and steward of public assets. The ISIF is an active owner of its investments and will use its equity shareholding and / or debt exposure as an opportunity to influence and realise material ESG improvements in order to positively impact shareholder value in both listed and unlisted investments. ESG risks will be monitored throughout the life of the investment.
3. Legal and regulatory compliance & voluntary global best practice standards	The ISIF aims to invest in accordance with the relevant global best practice standards. At a minimum the Fund will comply with relevant regulation and Irish legislation to which it is subject. However, the ISIF will also strive to be a model of best practice taking guidance from internationally recognised guidelines, codes of conduct and platforms (Schedule C)
4. Alignment with Irish Government and European sustainability policies	As a public fund it is important that ISIF's investment decisions are consistent with Government policy. ISIF will support initiatives by investing in a manner that is aligned with Irish Government long-term sustainability commitments, targets and initiatives - both at a high level and across specific sectors. Sample policies set out in Schedule D.
5. Transparency	The ISIF will report to stakeholders regularly and to the Principles for Responsible Investment (PRI) reporting framework on an annual basis. The ISIF will also provide relevant ESG information both as part of its annual reporting and regularly on its website.
6. Exclusion / Negative Screening	The ISIF amended its strategy in December 2017 to allow for the exclusion of specific entities or categories of investment as a responsible investment tool on a limited basis. Such exclusions may be made where, having considered relevant, reliable and reasonable factual evidence, it has been reasonably concluded that investing in an entity or category of investment is not consistent with the Agency's statutory duties concerning investments of the Fund or with its investment strategy for the discretionary assets of the Fund. This is in addition to investment exclusions mandated by legislation.

Responsible transition from global to domestic investment

The ISIF is being transitioned from a largely global portfolio into an Irish portfolio, as investments in Ireland are executed and drawn down. The global "transition" and the domestic strategic portfolios both have very different time horizons, investment strategies and underlying asset mixes. It is appropriate to consider both portfolios separately in the context of this sustainability and responsible investment strategy. Growth assets are more sensitive to ESG factors, specifically climate risks, than defensive assets. The Irish portfolio will be more exposed to growth assets than the global portfolio. Given the expected asset mix and the longer-term mandate of the Irish portfolio this is where the ISIF's ESG emphasis will be on a pre-investment basis (integration). The global portfolio will be monitored largely on a post-investment basis (active ownership).

6. Screening or exclusion of companies

Certain exclusions from the Fund are mandated by legislation, specifically the Cluster Munitions and Anti-Personnel Mines Act 2008. The ISIF's predecessor, the National Pensions Reserve Fund, developed a list of prohibited securities in the context of this statutorily mandated exclusion and the ISIF continues to review this and update as appropriate.

In addition to this, the ISIF operates a strategy of limited negative screening or exclusions as follows:

1) That any proposed exclusion of an entity or category of investments is duly supported by relevant, reliable and reasonable factual evidence; and
2) That having regard to such evidence, it can be reasonably concluded that investing in the entity or category of investments would not be consistent with the Agency's statutory duties concerning investments of the ISIF or with the Agency's approved investment strategy for the ISIF's discretionary assets.

Exclusion types are listed in Schedule E.

All exclusions will be subject to practical implementation considerations, contractual obligations and portfolio management best practice.

The ISIF commits to monitoring all investments for exposures to sectors and/or companies with potentially controversial business exposures and associated reputation risks.

7. Review

As stated at the outset the objective of this Sustainability and Responsible Investment Strategy is to protect and enhance both the value and the reputation of ISIF investments for the long-term. It will be reviewed at least every two years or more frequently if needed.

Version 1: July 2016
Version 2: December 2017

Schedule A: UN Principles for Responsible Investment

As institutional investors, we have a duty to act in the best long-term interests of our beneficiaries. In this fiduciary role, we believe that environmental, social, and corporate governance (ESG) issues can affect the performance of investment portfolios (to varying degrees across companies, sectors, regions, asset classes and through time). We also recognise that applying these Principles may better align investors with broader objectives of society. Therefore, where consistent with our fiduciary responsibilities, we commit to the following:

1. Incorporate Environmental, Social and Governance (ESG) issues into investment analysis and decision making processes
2. Be active owners and incorporate ESG issues into ownership policies and practises
3. Seek appropriate disclosure on ESG issues by the entities in which they invest
4. Promote acceptance and implementation of the Principles for Responsible Investment within the investment industry
5. Work together to enhance the effectiveness of PRI within the investment industry
6. Report on activities related to and progress toward implementing the PRI

Further information at www.unpri.org

Schedule B: The Santiago Principles

The Santiago Principles are a voluntary framework of investment and operational principles and practices for Sovereign Wealth Funds (SWFs). They emphasise appropriate governance, accountability arrangements and prudent, commercial investment activity. The 24 Generally Agreed Principles and Practices (GAPP) are outlined below:

GAPP 1. Principle
The legal framework for the SWF should be sound and support its effective operation and the achievement of its stated objective(s).

GAPP 2. Principle
The policy purpose of the SWF should be clearly defined and publicly disclosed.

GAPP 3. Principle
Where the SWF's activities have significant direct domestic macroeconomic implications, those activities should be closely coordinated with the domestic fiscal and monetary authorities, so as to ensure consistency with the overall macroeconomic policies.

GAPP 4. Principle
There should be clear and publicly disclosed policies, rules, procedures, or arrangements in relation to the SWF's general approach to funding, withdrawal, and spending operations.

GAPP 5. Principle
The relevant statistical data pertaining to the SWF should be reported on a timely basis to the owner, or as otherwise required, for inclusion where appropriate in macroeconomic data sets.

GAPP 6. Principle
The governance framework for the SWF should be sound and establish a clear and effective division of roles and responsibilities in order to facilitate accountability and operational independence in the management of the SWF to pursue its objectives.

GAPP 7. Principle
The owner should set the objectives of the SWF, appoint the members of its governing body(ies) in accordance with clearly defined procedures, and exercise oversight over the SWF's operations.

GAPP 8. Principle
The governing body(ies) should act in the best interests of the SWF, and have a clear mandate and adequate authority and competency to carry out its functions.

GAPP 9. Principle
The operational management of the SWF should implement the SWF's strategies in an independent manner and in accordance with clearly defined responsibilities.

GAPP 10. Principle
The accountability framework for the SWF's operations should be clearly defined in the relevant legislation, charter, other constitutive documents, or management agreement.

GAPP 11. Principle
An annual report and accompanying financial statements on the SWF's operations and performance should be prepared in a timely fashion and in accordance with recognized international or national accounting standards in a consistent manner.

GAPP 12. Principle
The SWF's operations and financial statements should be audited annually in accordance with recognized international or national auditing standards in a consistent manner.

GAPP 13. Principle
Professional and ethical standards should be clearly defined and made known to the members of the SWF's governing body(ies), management, and staff.

GAPP 14. Principle
Dealing with third parties for the purpose of the SWF's operational management should be based on economic and financial grounds, and follow clear rules and procedures.

GAPP 15. Principle
SWF operations and activities in host countries should be conducted in compliance with all applicable regulatory and disclosure requirements of the countries in which they operate.

GAPP 16. Principle
The governance framework and objectives, as well as the manner in which the SWF's management is operationally independent from the owner, should be publicly disclosed.

GAPP 17. Principle
Relevant financial information regarding the SWF should be publicly disclosed to demonstrate its economic and financial orientation, so as to contribute to stability in international financial markets and enhance trust in recipient countries.

GAPP 18. Principle
The SWF's investment policy should be clear and consistent with its defined objectives, risk tolerance, and investment strategy, as set by the owner or the governing body(ies), and be based on sound portfolio management principles.

GAPP 19. Principle
The SWF's investment decisions should aim to maximize risk-adjusted financial returns in a manner consistent with its investment policy, and based on economic and financial grounds.

GAPP 20. Principle
The SWF should not seek or take advantage of privileged information or inappropriate influence by the broader government in competing with private entities.

GAPP 21. Principle
SWFs view shareholder ownership rights as a fundamental element of their equity investments' value. If an SWF chooses to exercise its ownership rights, it should do so in a manner that is consistent with its investment policy and protects the financial value of its investments. The SWF should publicly disclose its general approach to voting securities of listed entities, including the key factors guiding its exercise of ownership rights.

GAPP 22. Principle
The SWF should have a framework that identifies, assesses, and manages the risks of its operations.

GAPP 23. Principle
The assets and investment performance (absolute and relative to benchmarks, if any) of the SWF should be measured and reported to the owner according to clearly defined principles or standards.

GAPP 24. Principle
A process of regular review of the implementation of the GAPP should be engaged in by or on behalf of the SWF.

Schedule C: A selection of relevant guidance codes and principles

Guidance	ESG Scope
CDP/GRI and other disclosure and integrated reporting frameworks	Environmental (E)
Climate Change and Low Carbon Development Act 2015	Legal / Environmental (E)
Cluster Munitions and Anti-Personnel mines Act 2008	Legal Requirement
Global Investor Coalition on Climate Change	Environmental (E)
ILO Core Labour Standards	Social (S)
International Corporate Governance Guidelines (ICGN)	Governance (G)
Modern Slavery Act 2015 (UK) - relevant to Irish supply chains	Legal / Social (S)
OECD guidelines for corporate governance and finance	Governance (G)
The Equator Principles - environmental and social risk in projects.	E&S
UN Global Compact guidelines	E&S
UN Guiding Principles on Business and Human Rights	Social (S)
UN Sustainable Development Goals	ES&G

Schedule D:

Samples of relevant sustainability strategy and policies
1. 2020 Emissions targets: The EU's 20-20-20 goals of 20% increase in energy efficiency, 20% reduction of CO2 emissions, and 20% renewables by 2020. This extends to a 40% emissions reduction by 2030 and to be carbon-neutral and by 2050.
2. Energy White Paper: Ireland's Transition to a Low Carbon Future, Dept. of Communications, Energy and Natural Resources (DCENR) - core objectives of sustainability, security of supply and competitiveness.
3. EU Non-Financial Reporting Directive: Due to be transposed into legislation by end 2016 - will require greater disclosure by companies with regards to a wide range of ESG issues.
4. Food Harvest 2020 – "Smart, Green, Growth": Agriculture expansion needs to be such that carbon intensity per unit of output is reduced and carbon sequestration in soils and forests is increased.
5. Food Wise 2025 - Strategic goal of making Ireland's food sector a world leader in the production, management and marketing of high quality, environmentally sustainable and safe food production - "sustainable intensification" and 'local roots, global reach' are key themes.

Schedule E: Exclusion Principles

The following Exclusions apply to the ISIF:
1. Exclusions under the Cluster Munitions and Anti-Personnel Mines Act 2008 Operational since 2008
2. Tobacco Manufacturing Companies Implemented December 2016
3. Companies materially involved in the production and processing of Coal and Oil Sands Implemented December 2017