

Our approach to investments on the stock market

Introduction

This document contains the second version of the Investment Strategy for stock market investments used by Triodos Investment Management B.V.* for its Socially Responsible Investment (SRI) funds and by Private Banking for its investment services. The first version of this document was published in 2004. These SRI products and services are designed to manage assets invested by clients in stock-exchange listed companies and countries that fulfil the strict sustainability criteria of Triodos Investment Management.

Triodos Bank separates its savings and lending activities from its investment activities. Our lending criteria (see “Our approach to lending” paper) are a core part of our banking business which connects savings deposited with us to loans to sustainable enterprises. Triodos Bank also offers investment services that fit its mission and vision through Triodos Investment Management and Private Banking. Clients can invest in listed companies worldwide that provide sustainable products and services or achieve above average social and environmental performance through these products and services. This paper explains our approach to this latter type of investment.

It is our policy to further expand and update it regularly in the light of new developments.

Mission

The mission of Triodos Bank is to help create a society that promotes people’s quality of life and that has human dignity at its core. The financial services made available by Triodos Bank to support this mission include lending, payments, savings, investments and mortgages for both institutional and retail clients. For each service, Triodos Bank has a policy that describes how it contributes to this mission.

* Triodos Investment Management, a 100% subsidiary of Triodos Bank, is responsible for managing the Triodos investment funds. These funds allow individuals and institutions to invest directly in a number of sustainable sectors including microfinance, sustainable trade, sustainable real estate, renewable energy, organic farming, conservation, cultural projects and investments in listed companies worldwide that provide sustainable products and services or achieve above average social and environmental performance. This is an important pillar of Triodos Bank activity, but is separate to Triodos Bank’s core business of taking in deposits and lending them directly to sustainable enterprises.

Vision

When investing on the stock market, Triodos Investment Management and Private Banking aim to ensure that:

- Investments are made in companies that contribute to a sustainable society or clearly lead the sustainability agenda in a particular sector. Also, Triodos Investment Management and Private Banking will ensure that their SRI products and services do not invest in companies that they consider to be associated with unsustainable services, products or processes.
- Constructive dialogue is conducted with companies to stimulate improved sustainability performance. Where appropriate substantial and relevant social, environmental and governance performance issues will be discussed. The dialogue has a threefold purpose: to raise awareness, to influence company management and prompt companies to act to further sustainable business practices.

Strategy

Triodos Investment Management and Private Banking invest in companies that deliver long-term financial, social and environmental value. A company that intends to deliver long-term value must effectively manage its relations with all stakeholders and be responsive to their needs and possibly changing demands. Triodos Investment Management and Private Banking believe that companies that balance these interests effectively will deliver maximum value to all stakeholders, including their shareholders.

As managers of a number of SRI products and services Triodos Investment Management and Private Banking provide clients with the opportunity to invest in companies and countries. They also enter into dialogue with companies on behalf of their clients to encourage the improvement of their business practices in the areas of governance, society and the environment. Dialogue is seen as key in enhancing business performance and strengthens the ‘license to operate’ of companies. Through dialogue Triodos Investment Management addresses business practices and impacts and suggests possible improvements. The results of sustainability analyses on companies and dialogue activities are published on the website of Triodos Bank.

The selection process for companies and countries differs significantly and is detailed further below.

Selection of companies

The assessment of companies takes place in two steps. The first is a sustainability assessment conducted by Triodos Sustainability Research, a department of Triodos Investment Management. It assesses if companies meet the strict sustainability criteria for investment on the stock market by Triodos Investment Management and Private Banking. The investment universe is defined based on the outcomes of these assessments. The second step is a financial assessment. This step is conducted by external asset managers. An investment decision is made on the basis of these two assessments. In this document we further outline the first step.

The sustainability criteria that Triodos Investment Management and Private Banking apply are dynamic. Changes may be prompted by legislation, public debate, best practice standards or company behaviour. Triodos Investment Management has set up an international advisory panel to provide an advisory platform for frequent dialogue on our investment process and sustainability criteria for stock market investments. The panel consists of 11 experts each with a background from employers, consumer and environmental organisations, trade unions, human rights groups, development and aid organisations, and academia. It meets four times per year.

The companies that are stock listed are, by definition, sizable companies. Often they are also located and/or source products and services from around the world. This makes researching them a labour intensive process. Basic sustainability data is derived from Sustainalytics with whom Triodos Sustainability Research has an active and long standing relationship. The research process includes the following three steps:

Step 1: Sustainable activities

Companies that derive over 50% of their revenues from sustainable products or services qualify for inclusion in the Triodos Investment Universe. Triodos Sustainability Research first identifies companies that actively contribute to a clean planet, climate protection or healthy people through specific sustainable products or services. Because these companies make a significant contribution to sustainable development, they are not subjected to the 'best-in-class' assessment described in step 2 of the selection process.

Clean planet

Triodos Investment Management and Private Banking want to encourage companies to make a positive contribution to a clean earth and the development of sustainable solutions for environmental pollution. This is an urgent issue because our natural environment is under increasing pressure. Companies that are active in this field are usually involved in new environmental technology developments aimed at combating pollution, and cleaning up the earth. Companies that specialise

in recording environmental pollution and energy consumption are also categorised within this theme.

Climate protection

Climate change poses a serious threat to the long-term health of the environment and therefore to the world's population and requires global action by governments, companies and citizens. Triodos Investment Management and Private Banking aim to encourage companies that make a positive contribution to combating climate change. Companies focusing on this theme are active in the field of sustainable energy production by using natural resources, such as the sun, wind, waves and geothermal energy. Companies involved in storing energy and enhancing energy efficiency are also classified under this theme.

Healthy people

Triodos Investment Management and Private Banking aim to encourage companies that make a positive contribution to realising a healthy lifestyle for everyone. Companies focusing on this theme offer solutions for health care issues, like medical technology, drugs aimed at curing diseases in developing countries, clean drinking water and innovative health care. Other relevant activities include medicines based on natural ingredients and organic food production.

In addition to the sustainable activities above, in specific situations or as part of new developments, other sustainable activities may also be considered. This could include activities that are focused on products or services that have particular importance from an environmental and/or social perspective.

Step 2: Identification of best-in-class companies

Companies that do not supply typically sustainable products or services can be eligible for investment if they are considered to be best-in-class with regard to their sustainability performance in their sector. Best-in-class selection is only applied to mid and large cap companies.

To determine if a company belongs to the best-in-class segment of their sector, its sustainability policies and performance are scored, based on at least seventy generic and sector-specific sustainability criteria. These criteria are grouped into three themes that cover Environmental, Social and Governance (ESG) issues.

Environmental

This theme encompasses an analysis of the business process design and the nature of the products supplied. Through inefficient management or by supplying obsolete or wasteful products, enterprises needlessly exhaust natural resources and create pollution. To justify their long-term existence, enterprises must make every effort to minimize their negative impact on their natural environment.

Social

The manner in which businesses fulfil their role in society is examined within this theme. It includes relations with community, employees, contractors, customers and competitors. Enterprises fulfill a role within the local communities in which they operate as well as in society in the broadest sense. Good employee relations are an important condition for the long-term success of an enterprise. Therefore employment terms, working conditions and labour relations are analysed.

Given the trend of outsourcing parts of the production process, the extent to which companies make use of their influence to protect the interests of employees in the supply chain is assessed. Whether companies make unreasonable demands on their suppliers is also taken into account. Finally the relationship of companies with customers and competitors is also analysed. The analysis includes customer satisfaction, the quality and safety of products supplied by the enterprise and whether the company respects free competition and uses responsible marketing practices.

Governance

Ethical business management is an important condition for a sustainable relationship between an enterprise and its stakeholders. The Governance theme includes an analysis of the corporate structure, a company's business ethics, and the integrity of its business practices. Director independence and remuneration (pay structure) are included in the theme, as well as the quality of the company's administration as a prerequisite for business continuity.

Having analysed these three themes the total sustainability score of a company is compared with that of other companies within the same sector. The top 50% of best performing companies in a particular sector qualify for inclusion in the Triodos Investment Universe.

For Triodos Sustainable Pioneer Fund, which focuses on small and midcap companies, this analysis is taken a step further for companies that do not supply typically sustainable products or services as described under step 1. A company can only be eligible for investment as a Corporate Social Responsibility leader when it is considered to be truly leading in sustainable business processes in its sector.

Step 3: Minimum standards

Following the selection of companies with sustainable activities (step 1) and the identification of best-in-class companies (step 2), companies are assessed against Triodos Bank's minimum standards. None of the companies selected for inclusion in the Triodos investment universe may be involved in activities that materially prevent the long-term development of a sustainable society.

A full and up-to-date overview of the minimum standards used is published on the Triodos Bank website (www.triodos.com).

Dialogue

Sustainability analyses are used to enter into dialogue with companies. In order to stimulate companies to improve their sustainability performance, Triodos Investment Management and Private Banking apply a number of instruments, which can be categorized into three aims:

- raise awareness;
- convince;
- motivate change.

Triodos Investment Management and Private Banking may cooperate with other stakeholders to maximize the effectiveness of its actions. Partnerships that have already been developed in this field are memberships of Eurosif and five of its national member organisations (Belsif, Uksif, Forum Nachhaltige Geldanlage, VBDO and SpainSIF), Eumedion and UNPRI. A number of these organizations actively engage with listed companies on corporate social responsibility.

As for the assessments, dialogue with companies is conducted by Triodos Sustainability Research on behalf of Triodos Investment Management and Private Banking.

Raise awareness

Two instruments are particularly aimed at raising sustainability awareness of the companies analyzed. The actions undertaken by Triodos Sustainability Research are a good starting point for further dialogue with the company. Both instruments are applied for every company it researches. The instruments are:

Engage with companies throughout the research process

The interactive collection of data stimulates companies' awareness about sustainable investment and helps to encourage them to improve their own sustainability. In addition to standard dialogue undertaken by Sustainalytics, Triodos Sustainability Research also approaches companies directly to obtain information regarding specific issues that may not have already been addressed. This dialogue also strengthens a company's insight into those issues that are important to shareholders.

Triodos Sustainability Research may respond to new trends in specific sectors by tightening the investment criteria, and will revisit the performance of listed companies in the light of these changes. If companies do not react adequately to these emerging developments, Triodos Sustainability Research may choose to exclude them from the investment universe.

Provide a rating for investment

Based on the data collected during the research process, a comparison of a company's sustainability performance within a sector is then produced. This facilitates a more detailed assessment of the company, taking into consideration key themes and sector specific issues. Results are shared with the companies, including a full overview of individual performance on seven key sustainability themes, as well as comparative performance.

In addition, companies are informed whether or not they are eligible for investment by Triodos Investment Management and Private Banking. An overview of aspects that Triodos Sustainability Research considers to best contribute to an improvement of sustainability performance is also provided. The research is repeated periodically. Experience shows that many companies contact us to discuss how they can improve their performance as a result of their assessment.

Convince

Triodos Sustainability Research applies two instruments to convince companies that changing their behaviour is of strategic importance. The relevance of these instruments is judged upon the potential impact on the sustainability performance of companies, the present interest for the theme within society and the likelihood that our efforts will lead to a change in behaviour,

Both instruments apply to all companies researched by Triodos Sustainability Research. The potential positive impact of improvement is considered largest for companies not found eligible for the investment universe. The instruments are:

Periodic dialogue with companies on specific themes

Triodos Sustainability Research strives to periodically define a number of sustainability themes on which it actively engages with companies. By addressing these subjects at the right time, and by using its position as a shareholder, Triodos Investment Management and Private Banking aim to enlarge the impact of this approach.

Placement of sustainability themes on the public agenda

In order to stimulate public debate, Triodos Sustainability Research may periodically address relevant sustainability themes in the media, if and where possible in collaboration with other stakeholder groups. Triodos Sustainability Research will also increase pressure on companies to improve their sustainability performance by publishing the results of its research.

Motivate change

In order to trigger action from companies, Triodos Sustainability Research has a mandate to exercise the shareholder rights of the SRI funds. Even though the companies invested in meet the strict investment criteria, there may still be areas of improvement. The instruments Triodos Sustainability Research uses are:

Voting

On behalf of the SRI funds, Triodos Sustainability Research votes at Annual General Meetings whenever it is technically possible. For this reason, the SRI funds have voting guidelines that describe the way voting rights are used. The guidelines have been influenced by Triodos Bank's vision for a sustainable society and Triodos Investment Management's sustainable investment criteria. A detailed overview of all voting records on companies is published on the Triodos Bank website (www.triodos.com). All investee companies are informed about voting decisions in order to stimulate awareness of the Triodos Bank vision and Triodos Investment Management's sustainable investment criteria, and to help the companies improve their sustainability performance.

Speaking at Annual General Meetings

Triodos Sustainability Research, on behalf of the SRI funds, makes use of speaking rights at a small number of Annual General Meetings. Comments focus on the strongest and the weakest aspects of the sustainability performance and are intended to be a starting point for future, and more profound dialogue with the companies.

Shareholder resolutions

As a final engagement instrument Triodos Sustainability Research may (co-)file a shareholder resolution focusing on weak aspects of sustainability performance, on behalf of the SRI funds. Where this is already taking place, for example in the US, initiatives from other investors that ask for more sustainable behaviour from the company involved will actively be supported. This instrument will only be used when dialogue with management has proven to be unsuccessful in the past.

Selection of countries

As well as equity, Triodos Investment Management and Private Banking manage a number of SRI portfolios that invest in bonds, either solely or mixed with equities. For corporate bonds the same screening methodology as for equity investments are applied. Due to the strict selection approach there may be insufficient investment opportunities in corporate bonds. So, to meet fiduciary obligations, investment in country bonds is also possible. Investing in them guarantees a sound spread and liquidity in the bonds portfolio. This decision is reinforced by poor liquidity of company bonds and the volatility of the capital market.

Triodos Investment Management and Private Banking consider it neither feasible nor desirable to engage with governments as an investor, despite the goal to influence sustainable behaviour. Governments should be supervised and influenced only by its citizens through democratic processes. Country bonds are therefore considered a neutral investment category that both Triodos Investment Management and Private Banking want to limit as much as possible.

The research process includes the following three steps:
Step 1: Countries must belong to the fifty best functioning democracies within the group of 100 largest economies.
Step 2: Countries must be free of boycotts supported by the United Nations.
Step 3: Countries must underwrite the most important, broadly supported conventions of the United Nations.

Triodos Bank, March 2011 (2.0)