Statement on sustainability risks and adverse impacts on sustainability

Responsible investing

OKTOBER 2022

1. What is sustainability risk and can it affect the value of investments?

KBC Asset Management NV ('KBC AM') defines sustainability risk as the risk that the value of an investment is adversely affected by environmental, social or governance events or trends. 'Environmental risk' refers to the risk that the value of an investment is adversely affected by environmental events or conditions, including factors resulting from climate change and other environmental degradation. 'Social risk' refers to the risk that the value of an investment is adversely affected by social events or conditions. 'Governance risk' refers to the risk that the value of an investment is adversely affected by events or conditions resulting from incompetent or otherwise inadequate corporate governance. The nature of these risks may vary over time:

- Short-term sustainability risk usually depends on a particular event. These types of risks generally only have an impact on the value of the investment at the time when the event occurs. Examples of such events include an accident (resulting in litigation, for example to compensate damage to the environment); court cases and penalties (for example, for failing to respect social legislation); scandals (for example, when a company gets bad publicity because human rights are not upheld throughout its supply chain or because a company's products do not uphold the ESG standards it promises, where ESG stands for 'Environmental, Social and Governance'). These sustainability risks are considered to be higher if an issuer is in any way negligent in applying the ESG standards.

- In the longer term, sustainability risk refers to risks that may develop over the long term, such as: exposure to business activities that may come under pressure due to climate change (for example, parts of the automotive industry); changing product preferences from customers (for example, preference for more sustainable products); difficulties in recruiting; increasing costs (for example, insurance companies that face claims due to changing weather conditions). As this risk develops over the long term, companies can mitigate it, for example by changing their product offer, improving their supply chains, etc.

However, since not all types of business operations can be adjusted with the same degree of flexibility, some operations are more exposed to sustainability risk than others (case in point: the oil industry). Sustainability risk therefore also depends on the specific investment policy of the individual fund or mandate.

2. To what extent is sustainability risk integrated into KBC AM's investment policy?

In its investment policy, KBC AM accounts for sustainability risks by:

- defining an exclusion policy which applies to all funds and discretionary mandates. Further information can be found at www.kbc.be/investment-legal-documents > General exclusion policy for conventional and Responsible Investing funds; and
- Responsible Investing funds and discretionary mandates may be subject to additional criteria for responsible investing. For a detailed description of these additional criteria, go to: www.kbc.be/investment-legal-documents > Exclusion policy for Responsible Investing funds.

As part of the investment policy, the management company continuously assesses the underlying investments at the issuer level, as well as (if relevant) at the level of the asset allocation and the regional or sectoral allocation. During these regular assessments, sustainability risk is considered one of the various elements that may impact investment returns. KBC AM's Responsible Investing research team assigns an ESG risk rating to most companies included in the best-known benchmarks and to a selection of small and medium-sized enterprises, based on reports it receives from an ESG data provider. This ongoing ESG risk assessment covers a number of ESG indicators (where available), ranging from companies' carbon emissions to their respect for fundamental labour rights in their supply chains. ESG risk ratings are a key part of KBC AM's investment policy and are shared internally with portfolio managers and strategists, so they can use these during the investment decision-making process. Finally, Responsible Investing funds aim to reduce the weighted average ESG Risk Rating (of companies) relative to the reference portfolio.

Based on these principles, KBC AM generally believes that our funds have a low sustainability risk, unless otherwise specified in the pre-contractual documents.

3. Principal Adverse Impacts (PAIs)

KBC AM aims to achieve long-term investment returns for its clients that take into account sustainability considerations. This means that KBC AM makes investment decisions on behalf of its clients based on an investment policy which makes allowances for sustainability risks and social, ethical and environmental standards.

The **Principal Adverse Impacts (PAIs) on sustainability** are largely hedged by the exclusion policy pursued. A number of activities are excluded from all actively managed investments funds (other than Responsible Investing funds). Examples of excluded companies include companies involved in controversial arms, thermal coal or the manufacture of tobacco products. The most serious violators of the principles of the UN Global Compact and companies involved in human-rights violations are also excluded. Government bonds issued by countries with the most controversial regimes are excluded, and KBC AM will not invest in financial instruments linked to livestock and food prices. Please note: passively managed investment funds, structured funds and funds investing in third-party KBC AM funds may not apply all the exclusion criteria.

A number of additional activities are excluded from our Responsible Investing funds. Companies which do not comply with the main international principles or standards are excluded. This includes, for example, the UN Global Compact Principles, the conventions of the International Labour Organization (ILO), the OECD Guidelines for Multinational Enterprises, the UN Guiding Principles on Business and Human Rights (UNGPs) and the UN Sustainable Development Goals (SDGs). Companies involved in severe controversies related to environmental, social or governance issues are also excluded. All companies involved in fossil fuels are excluded from Responsible Investing funds, with the exception of green bonds issued by these companies which promote the energy transition. Companies involved in defence contracts or small arms are also excluded. Restrictions also apply to companies involved in gambling, adult entertainment, palm oil, and fur and exotic leather. In addition, non-sustainable, controversial regimes and countries ranked among the 10% worst performers (according to the ESG rating model) are excluded, as are companies with high ESG risk ratings and all companies located in countries that encourage unfair tax practices. Ad-hoc exclusion or deliberation of companies is possible, but only on the recommendation of the Responsible Investing Advisory Board. You will find more information in the General exclusion policy for conventional and Responsible Investing funds and Exclusion policy for Responsible Investing funds.

In addition to the strict exclusion policy, our Responsible Investing funds promote the integration of sustainability into the policy decisions of issuers (i.e. companies, governments, supranational debtors and/or government-linked agencies), for example by showing a preference for issuers with higher ESG ratings, and by promoting the reduction of climate change by preferring issuers with lower carbon intensity, with the intention of achieving a predetermined carbon intensity target. Our Responsible Investing funds also, for example, support sustainable development, by including companies that contribute to achieving the UN Sustainable Development Goals and by promoting the transition towards a more sustainable world through investments in green, social and sustainability bonds, which implicitly take into account most of the Principal Adverse Impacts (PAIs) listed.

Within non-sustainable funds, the principal adverse impacts on sustainability are accounted for explicitly through the exclusion policy and implicitly through the integration of sustainability

risks into the management of non-sustainable products (see above point 2: 'To what extent is sustainability risk integrated into KBC AM's investment policy?'). KBC AM's Responsible Investing Research Team assigns an ESG risk rating to most companies included in the best-known benchmarks and to a selection of small and medium-sized enterprises, based on reports from an ESG data provider. This ongoing ESG risk assessment covers a number of ESG indicators (where available), ranging from companies' carbon emissions to their respect for fundamental labour rights in their supply chains. ESG risk ratings are a key part of KBC AM's investment policy and are shared internally with portfolio managers and strategists so they can use them when taking investment decisions.

In addition, a number of the Principal Adverse Impacts listed implicitly take into account our Proxy Voting and Engagement Policy. KBC AM exercises the voting rights associated with the shares managed in the funds. Under the Proxy Voting and Engagement Policy, KBC AM votes in shareholder meetings and actively communicates with companies, because KBC AM firmly believes that active share ownership can have a positive influence on its investee companies in the medium and long term. For further information, see Proxy Voting and Engagement Policy: (kbcgroup.eu).

For more information about the Principal Adverse Impacts, see the Statement on the Principal Adverse Impacts on Sustainability.

4. Shareholder engagement

As part of its commitment to responsible investing, KBC AM exercises the voting rights associated with the shares it manages in accordance with its Proxy Voting and Engagement Policy (the 'Proxy Voting Policy'). This means that KBC AM votes in shareholder meetings and communicates with a large number of companies in order to represent its clients' interests. The key principles of the Proxy Voting Policy and the annual report on KBC AM's activities related to proxy voting and shareholder engagement are available at www.kbc.be/investment-legal-documents.

5. Ethical standards

The KBC group, KBC AM's parent company, is committed to upholding the following international business codes, and KBC AM's investment policy and investment processes are aligned with these commitments:

- The United Nations Environmental Programme Finance Initiative (UNEP FI) Principles for Responsible Banking;
- The Collective Commitment to Climate Action, as part of which the KBC group commits to promoting the shift towards a greener economy as much as possible and, in doing so, reducing global warming to well below 2°C, striving for 1.5°C, in accordance with the Paris Climate Agreement;
- The Tobacco-Free Finance Pledge, which encourages financial institutions to divest from the tobacco industry; and
- The United Nations Principles for Responsible Investment.