



Capital Partners
your partner for alternative investments

ESG REPORT 2021



“As people and planet face ever greater challenges – global warming, the COVID-19 pandemic, increasing inequality – ESG efforts are increasingly focusing on real world outcomes.”



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Introduction

As people and planet face ever greater challenges – global warming, the COVID-19 pandemic, increasing inequality – ESG efforts are increasingly focusing on real world outcomes. LGT Capital Partners (LGT CP), and the industry more broadly, have made significant progress with respect to ESG in the last 15 years. ESG is now part of almost every investor's process, and most sizeable organizations have dedicated substantial resources to this end. However, it has been difficult to precisely define success and the outcomes we wanted to achieve. The industry has moved from awareness toward outcomes, supported by global initiatives including the Paris Agreement and the unanimous approval of the UN Sustainable Agenda 2030 with the 17 Sustainable Development Goals (SDGs).

The shift in focus to outcomes has gained even more momentum recently ahead of the COP26 Global Climate Change Summit, planned for November 2021 in Glasgow. Governments globally are announcing new programs to “build back better” in response to the pandemic and to support the transition to carbon neutral economies. At the same time, new investor initiatives are working to develop “net zero” portfolios, accelerating the trend further.

This shift from process to outcome orientation is the most important trend in ESG, but implementing it is not easy. Many institutions at the forefront of sustainable investing are working on and often struggling to find solutions. At LGT CP, we too have been moving towards a greater outcome orientation in our ESG

approach, and it forms the core focus of this year's ESG Report. We look across our various asset classes – private markets, insurance-linked strategies (ILS), hedge funds, public equities and fixed income – to show outcomes in our portfolios. For our multi-manager strategies, such as private markets, hedge funds and long-only, we highlight the achievements of our managers, whether in aligning portfolios to meet carbon emission reductions or in enhancing the role of diversity and inclusion in investment decision-making. For direct investment strategies, we illustrate how our equity portfolios align with emission targets of the Paris Agreement, as well as how our fixed income portfolios impact the SDGs. Finally, we highlight the work we have been doing to select ILS counterparties that share our commitment to positive ESG outcomes and to combating climate change.

We also show how these various approaches to ensuring desirable ESG outcomes can work together in the LGT endowment. In this case, we focus on how we are working to achieve net zero carbon emissions within the portfolio, in line with the Paris Agreement.

Finally, this year we put the “ESG spotlight” on LGT CP as a firm, highlighting our efforts to further the goals of greater diversity and inclusion within our industry.

We hope you find this report insightful and, as always, we would be pleased to discuss any questions or comments you may have on it.

On behalf of LGT Capital Partners



Tycho Sneyers
Chairman of the ESG Committee
Member of the PRI Board

Fact and figures

344

MANAGERS
ASSESSED ON ESG

50%

OF PRIVATE EQUITY MANAGERS
HAVE A D&I POLICY IN PLACE

47%

OF PRIVATE DEBT PORTFOLIO
COMPANIES CREATED NEW JOBS

60%

INCREASE IN HIGH
SCHOOL GRADUATION
RATES FROM IMPACT
INVESTMENT

61

METRIC TONS OF CO₂ ARE SAVED BY
OUR GLOBAL EQUITY STRATEGY OVER
THE BENCHMARK¹

THE LGT SUSTAINABLE BOND
GLOBAL STRATEGY HAS A
POSITIVE IMPACT ON

15

OF THE 17 SDGs

¹ per USD 1 million of revenue

ESG assessment of managers – how we do it

Each year we conduct an assessment of managers, which forms part of the firm's larger ESG due diligence, monitoring and manager engagement process. The assessment serves a two-fold purpose. First, it shows our investors the extent to which managers are considering ESG factors in their investment, ownership and reporting practices. Second, the assessment facilitates our engagement with managers on ESG, highlighting excellence in implementation and flagging areas for improvement.

In the assessment, we ask managers about, and score them on, four key areas of ESG practice:

- Manager commitment – the extent to which they have demonstrated their commitment to ESG through actions such as defining a policy, committing to an industry initiative like the Principles for Responsible Investment (PRI) and engaging with their portfolio companies
- Investment process – the extent to which they have formally integrated ESG into their investment processes, using it as a framework for evaluating investments and identifying areas for improvement
- Ownership – the extent to which they have exhibited active ownership through activities like defining ESG guidelines, establishing key performance indicators (KPIs) or assigning ESG responsibilities for portfolio companies
- Reporting – the extent to which they have provided regular and relevant reporting on ESG on a portfolio company level and on the aggregate fund level

Managers receive a score of 1 to 4 (where 1 = excellent and 4 = poor) on each of the four areas, resulting in an overall rating for each manager, which is then documented in our monitoring system. Managers who receive low scores (3 or 4) on specific indicators are encouraged to improve over time.

Rating	Description
1	Manager is genuinely committed to ESG, with institutional processes in place. Applies ESG criteria in investment decision-making, is an active owner and reports on ESG
2	Manager has taken steps to integrate ESG into its approach and investment process. Process is institutionalized, but manager may not follow through on all levels (e.g. reporting)
3	Manager demonstrates some commitment to ESG or has begun some initiatives, but lacks institutionalized processes
4	Manager demonstrates little or no commitment to ESG

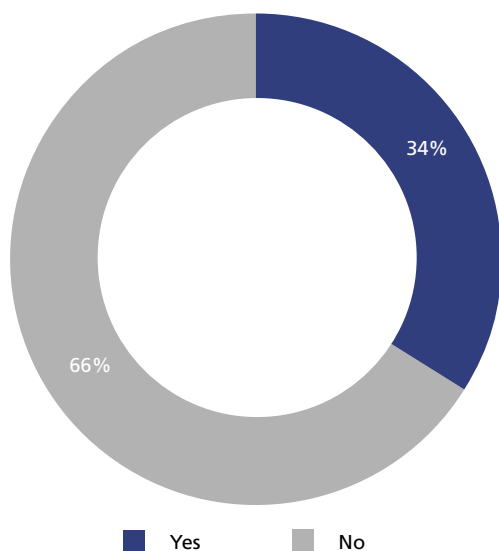
Private equity

This year we look at ESG outcomes in private equity through the lenses of climate change, diversity and inclusion, company key performance indicators, the SDGs, as well as our usual ESG ratings of managers. They paint a picture of ever-deepening ESG integration in our portfolios across a wide range of metrics.

How managers are responding to the challenge of climate change

As climate change has climbed ever higher on investor agendas, the 267 private equity managers in our portfolios are responding to the challenge.² In this year's ESG assessment, we find that 34% of them specifically address climate change in their ESG policies.

Figure 1: Proportion of managers that address climate change in their ESG policy



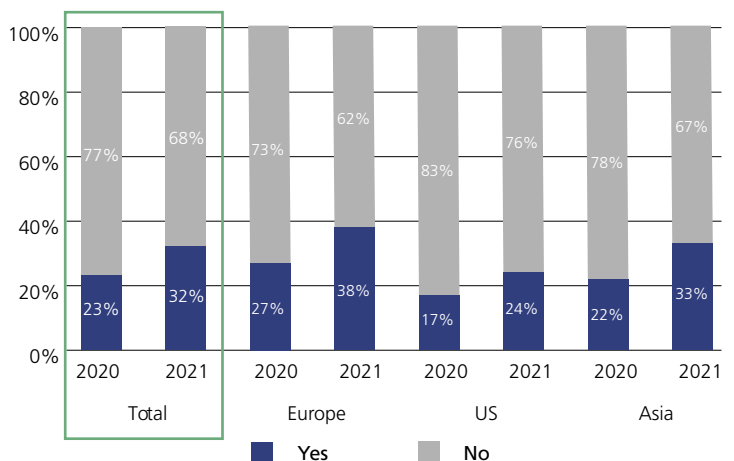
Source: LGT CP

Approaches vary across managers, with some having very clearly articulated policies and targets, while others are still developing their process. For example, one middle market European buyout manager spells out its ambitions to tackle climate change in terms of measuring and reducing its own emissions, with the aim of becoming a carbon neutral company. The manager also measures the emissions of the portfolio and encourages companies to reduce

their emissions and “work towards carbon neutrality, in line with industry trends and regulations.” A large buyout manager has a policy that seeks to align itself with the Task Force on Climate-related Financial Disclosure (TCFD) by integrating analysis of climate-related risks and opportunities throughout the investment cycle. It also aims to promote awareness and enhance expertise on climate issues internally and within its portfolio. As part of this, the manager encourages portfolio companies to continuously expand their reporting on climate-related risks and opportunities in the value chain.

Most of the managers who address climate change in their ESG policy (34%) also actively assess these risks within their portfolio companies (32%). The policies appear to have substance and are more than just well-articulated intentions. It is also encouraging that this number is on the rise, as it represents a nine-point increase over last year for the global sample set. As we saw in last year's assessment, there is significant regional variation in the responses, as 38% of European managers and 33% of Asian managers have implemented an approach to climate change, while 24% of US managers have done so.

Figure 2: Proportion of managers with a standard framework for assessing climate change risks

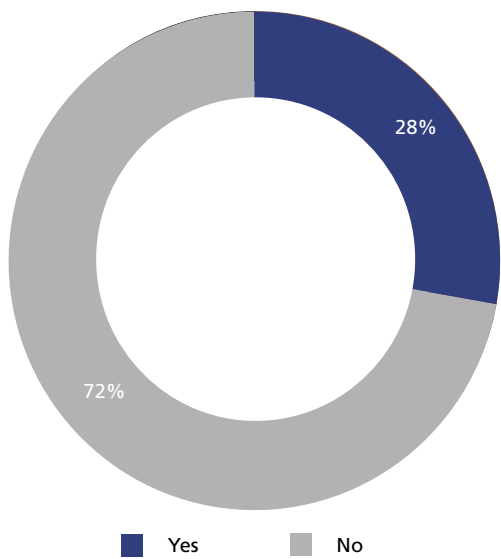


Source: LGT CP

² Based on this year's ESG assessment of 267 managers in our private equity portfolios across all investment programs managed for clients.

We observe that 28% of managers actively measure the CO₂ emissions of their portfolio companies. It shows the depth of their commitment to managing climate change risk, as they follow up on their initial risk assessment with ongoing monitoring. Overall, we would expect these numbers to increase in the future, as more managers respond to the need for better data on climate change risks and opportunities.

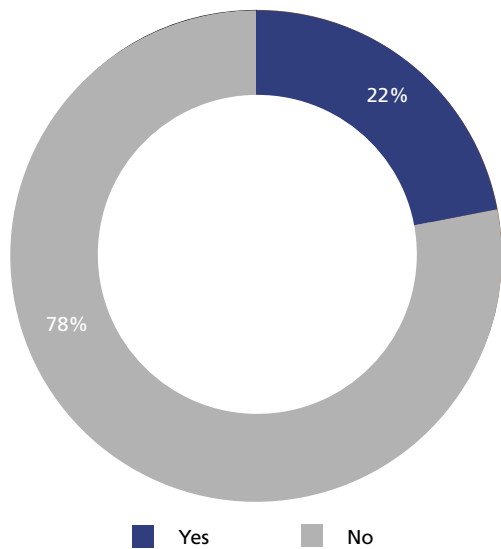
Figure 3: Proportion of managers that monitor greenhouse gas emissions



Source: LGT CP

As we often see with ESG practices within private equity, reporting is the least well-developed piece of the puzzle. This is also true with reporting on climate change metrics, as 22% of our managers provide such reporting. We anticipate that the proportion of managers reporting will increase over time, as processes for measuring climate change risks improve and industry-wide standards continue to develop.

Figure 4: Proportion of managers that report on climate change activities



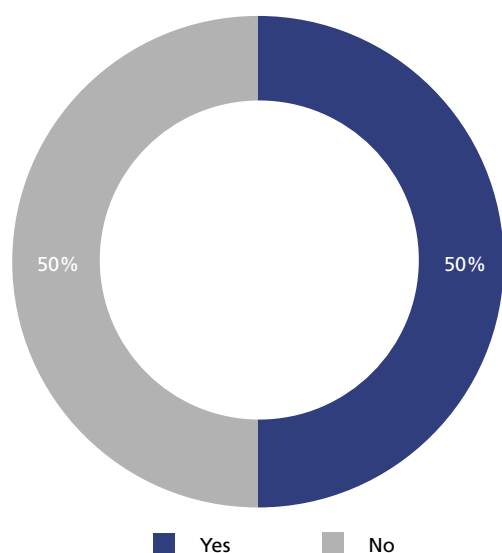
Source: LGT CP

One European large buyout manager points the way, as it publishes an annual “Carbon Footprint Report”, which provides a detailed breakdown of its portfolio carbon emissions. This includes a year-on-year comparison of emission sources, with factors such as refrigerant gas, natural gas from the grid, business travel, staff commuting and outbound deliveries. It also breaks down the portfolio by emission scope (Scope 1, 2 and 3) and provides qualitative commentary on emission sources and likely avenues for further reductions.

How managers approach D&I

Diversity and inclusion (D&I) has increased in importance in many regions around the world in recent years, as companies have recognized the importance of a workforce that reflects the full set of talents available in their local communities. Investor interest has also grown, driven by a desire to optimize performance as well as to meet stakeholder expectations on social inclusion. Private equity managers are responding to these drivers, as 50% of our managers have formal diversity policies in place. The GTCR case study on the next page shows how one manager has responded to the challenges and opportunities of D&I.

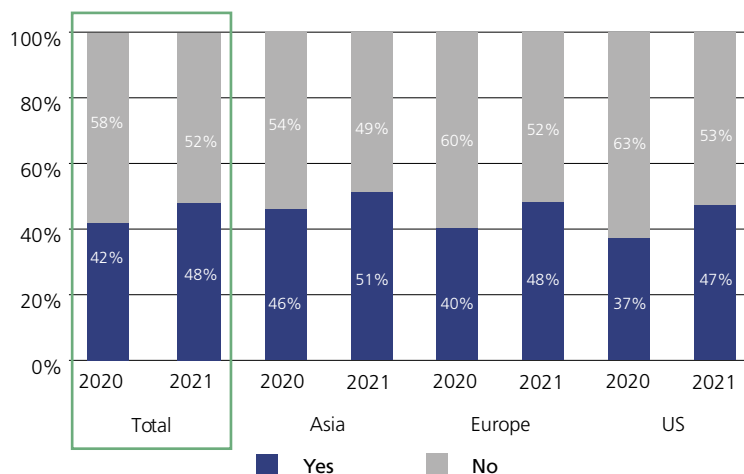
Figure 5: Proportion of managers that have a D&I policy in place



Source: LGT CP

We observe an increase of six percentage points since last year in the proportion of managers who consider D&I in investment decision-making, which now stands at 48%. Interestingly, we observe only minor regional differences on this metric. Asian managers are in the lead at 51%, with European managers closely following at 48% and the US just behind at 47%.

Figure 6: Proportion of managers that consider D&I in their investment decisions



Source: LGT CP

Like with climate change and other ESG practices, managers take a variety of approaches to integrating D&I in their investment process. For example, one of our managers, the global software investor Hg, embedded D&I factors directly into a target company's financing package in order to ensure accountability across stakeholders. Hg worked with the lender to include diversity-linked targets into the terms of the loan that, if met, will reduce the annual interest cost. The criteria include:

- implementation of policies to facilitate a balanced and inclusive recruitment process at all levels of the organization
- tracking of diversity statistics including gender, ethnic and LGBTQ+ across all levels of the organization
- increasing the ratio of female employees each year

LGT CP welcomes such innovation in D&I and looks forward to tracking its progress as managers increase their focus on the topic.

Responding to the challenge and opportunity of D&I

GTCR LLC (GTCR) is a Chicago-based private equity firm with 40 years of investment experience. Their team of more than 100 professionals invest across the Financial Services & Technology, Healthcare, Technology, Media & Telecommunications and Growth Business Services sectors.

GTCR

What drives their D&I efforts

GTCR fundamentally believes that diversity of experience, culture, race, ethnicity, gender and sexual orientation – both within the firm and at its portfolio companies – can help foster better decision-making. It can also help to create a more inclusive culture and working environment and drive more attractive outcomes for its investors. The firm has recognized that D&I has become increasingly important to many of its stakeholders, including investors, employees and the executives with whom they partner in managing portfolio companies. GTCR believes it is important that these critical relationships are aware of their initiatives and progress in this area.

What GTCR has accomplished so far

GTCR sees significant enthusiasm and commitment for D&I initiatives across the firm and has made significant progress recently. At the beginning of 2020, the firm appointed Melissa Mounce to lead its D&I initiatives as GTCR's first Managing Director – Leadership Talent and Diversity. The firm's D&I initiatives touch three separate but related areas: GTCR itself, its portfolio companies and the governing bodies of its portfolio companies.

GTCR has broadened its networks to attract diverse talent to the firm, and these new relationships are gaining momentum. In February, GTCR became a signatory to ILPA's Diversity in Action initiative, having met all four foundational requirements and five of the nine optional

activities. It has also made progress in its investment team hiring, adding three new female investment professionals in the last year, with an additional four to join GTCR's summer class in 2021. In addition, the firm has added twelve female independent directors to its portfolio company boards in the last year. Despite these accomplishments, GTCR says its work on various D&I initiatives "remains a work in progress," and the firm continues to invest significant time and firm resources in this important area.

How D&I impacts the investment process

The firm's Managing Director – Leadership Talent and Diversity, Melissa Mounce, takes an active role in discussions with the chief human resources officers at each of GTCR's 27 portfolio companies to highlight D&I as one of three priorities for 2021. GTCR expanded its annual ESG survey this year to collect additional information from portfolio companies on their D&I initiatives. It considers material D&I issues during its investment underwriting process, including identifying companies that can benefit from D&I initiatives after a transaction has closed.

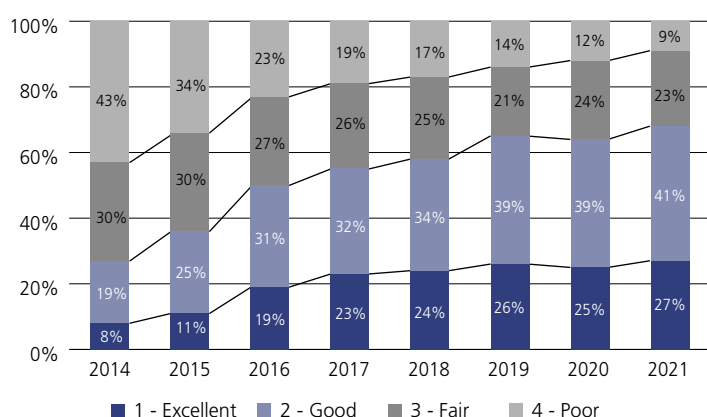
How GTCR sees D&I developing in private equity

GTCR believes D&I is a business imperative that will have a substantial impact on the private equity industry and more broadly across the economy. Private equity sponsors that are slow to adapt to this reality will face challenges, both in terms of building dynamic firm cultures and fostering better decision-making and results. The firm is convinced that GTCR's focus on D&I will allow it to continue to be an employer of choice and a preferred partner for the executives with which it partners for the management of portfolio companies.

Continued progress in global ESG ratings

The aggregate ESG profile of our global group of 267 managers supports the positive outcomes observed in the climate change and D&I indicators. The vast majority of managers, 68%, have strong ESG practices in place, as indicated by their ratings of 1 or 2. It represents an increase of four percentage points over last year, continuing the long-term improving trend in the portfolio since 2014.

Figure 7: ESG ratings globally

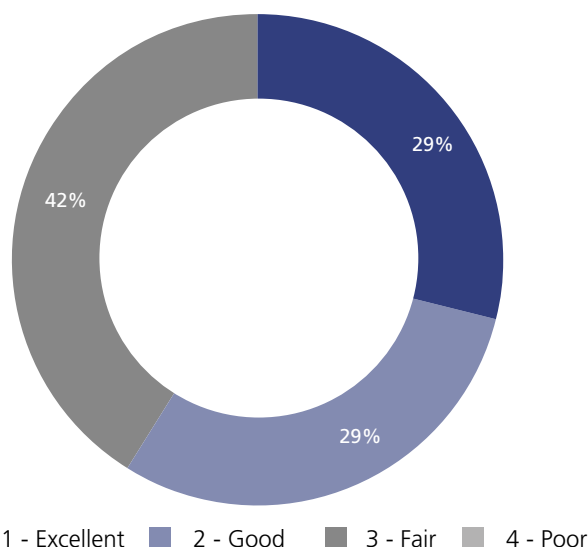


Source: LGT CP

Majority of new managers received high ESG ratings

The global group of managers includes 17 new relationships for LGT CP, including 11 from Europe, five from the US and one from Asia. The majority – 58% – are rated 1 or 2, while the rest are rated 3. The latter group will be able to benefit from our active engagement on ESG, which should help to drive improvement over time. No new managers carry the lowest rating of 4, which indicates that they do not integrate ESG into investment decision-making. This is in keeping with our commitment to making no new investments with the ever-shrinking pool of managers who elect to ignore ESG.

Figure 8: ESG ratings of new managers



Source: LGT CP

Engaging with managers through “Implementing ESG in private equity 2.0”

Each year we engage with our managers on ESG through an annual ESG assessment and discussions with individual managers. In addition to our regular engagement, we published a new and second edition of our ESG best practice guide, “Implementing ESG in private equity 2.0.” The publication highlights the latest developments in ESG integration, ranging from climate change, diversity and data security to active management of ESG value creation.

The new guide includes eight case studies that illustrate best practice through the lenses of manager commitment, investment process, ownership and reporting. It features case studies from leading private equity managers,

including AEA, GenBridge, Genstar, Hg, KKR, NewQuest, Summa and Triton. It shows that there is no one “right way” of integrating ESG considerations into private equity decision-making. Approaches vary as much as the managers themselves.

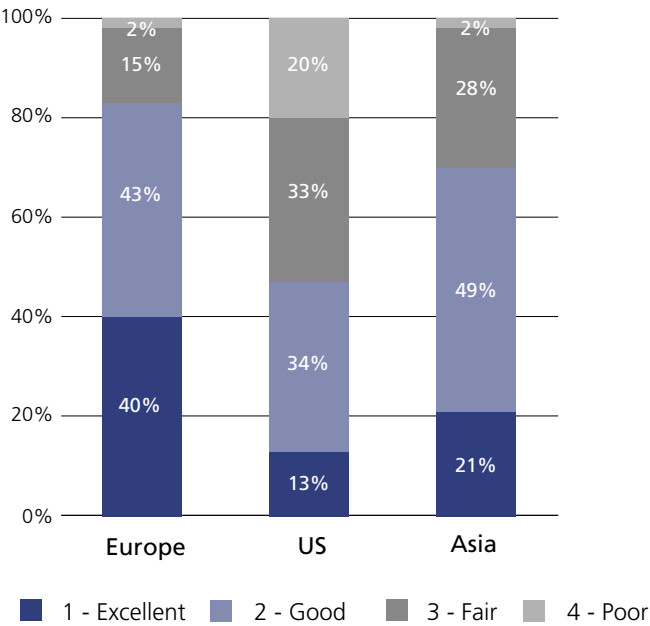


Significant regional variation persists, along with opportunities for ESG engagement

As we have seen in previous reports, European managers continue to lead on ESG practices, as 83% have achieved the top ratings of 1 or 2, compared with 70% for Asia and 47% for the US. The US is the only market where there remains a meaningful cohort of 4-rated firms (20%), the majority of whom are small buyout managers.

These managers continue to be a focus of engagement for us, which this year included sharing with them our new ESG best practices guide, “Implementing ESG in private equity 2.0”. The publication highlights the latest developments in ESG integration, ranging from climate change, diversity and data security to active management of ESG value creation.

Figure 9: ESG ratings by region

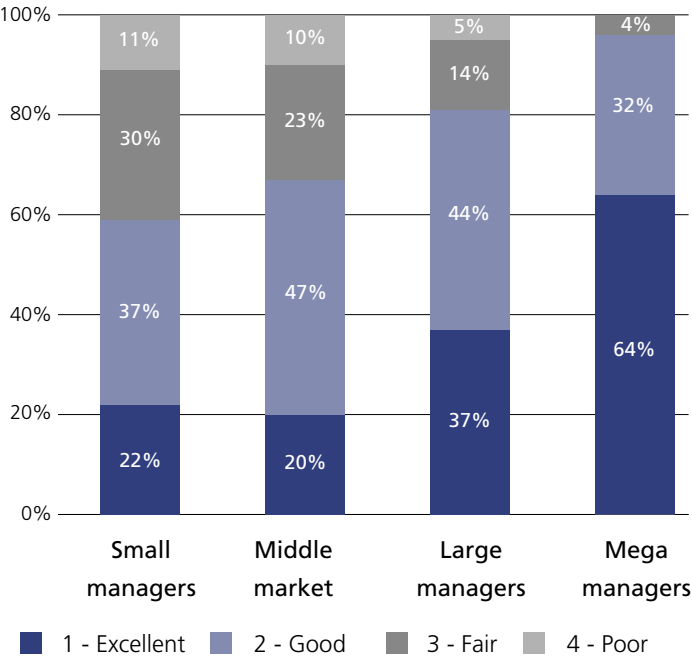


Source: LGT CP

Fund size remains a factor in ESG integration

The long-term trend of larger managers generally having stronger ESG approaches remains firmly in place. This is typically driven by their greater economies of scale, which provides more scope for dedicated ESG resources. They also tend to have a global investor base, including investors that are very vocal in pressing the case for ESG. Nearly all large and mega buyout managers (81% and 96%, respectively) have solid ESG processes in place, as indicated by their 1 or 2 ratings, versus 67% for middle market buyout managers and 59% for small buyout managers.

Figure 10 ESG ratings by size of funds



Source: LGT CP

Case study: food logistics company supports the circular economy and stands out on ESG



One of LGT CP's co-investments stands out for its strong ESG profile, particularly for its positive environmental footprint. IFCO is the world's leading supplier of Reusable Plastic Containers (RPCs), which support the circular economy. RPCs help to reduce food waste by promoting the "sharing, reusing, reducing" concept for food packaging. In addition to its compelling business model, the company also contributes to reducing the CO₂ footprint of the food supply chain through smarter packaging and faster, more reliable delivery of food products.

LGT CP also recognized IFCO's well-demonstrated commitment to ESG across the company's operations. IFCO's RPC and logistics solutions play a key role in the circular economy of the grocery supply chain, and its services cover every aspect of RPC management. IFCO delivers the containers to growers and packers, who pack the produce in the RPCs and ship it to retailers. IFCO then collects the RPCs from retailers, cleans and sanitizes them, and puts them back into circulation. The company has a global network of 89 service centers and over 1,100 employees worldwide that remove over 1.7 billion units of single use packaging from the fresh food supply chain each year, with 314 million RPCs in circulation.

Compared with single-use packaging, which is prevalent in the retail world, RPCs produce up to 60% less CO₂ emissions and 86% less solid waste, while using 64% less energy and 80% less water. IFCO's solutions also minimize food waste, as there is 96% less damage to fresh produce when it is packed and transported in a plastic crate compared to single-use packaging. The company makes

a clear contribution to SDG 11, Sustainable Cities and Communities, and SDG 12, Responsible Consumption and Production.

The company also adheres to sound ESG principles across its operations. Broken RPCs are either repaired or granulated and made into new IFCO RPCs. This process prevents materials from being downgraded or ending up in landfills. When cleaning RPCs between uses, IFCO's automated systems are programmed to minimize water consumption and use eco-friendly detergents and disinfectants. At its fast-paced facilities, IFCO maintains a strong focus on worker health and safety. The company has implemented an effective framework for interacting with suppliers and customers to ensure active management of ESG issues in a highly competitive market. In March 2021, IFCO's European Lift Lock RPCs were designated "Cradle to Cradle Certified®" (C2C) at Silver level, making IFCO the first and only C2C certified reusable packaging container.

Beyond this, the company encourages its customers to follow its sustainable standards, issuing annual sustainability certificates to them, where it calculates resource savings and waste reductions for each customer. The certificates highlight the amount of CO₂, water, energy, solid waste and food waste they have saved by utilizing IFCO RPCs in their supply chain. IFCO also makes a tangible contribution to the communities in which it operates by donating funds and thousands of RPCs to food banks and other charities. Finally, the company demonstrates its commitment to high standards of ESG governance through the firm's ESG Subcommittee and the IFCO Advisory Committee.

Co-investment KPIs

This is the third year that we are reporting on ESG KPIs for our co-investments. The number of participating companies has increased again and now stands at 50. The three-year time span enables us to make certain observations on trends within the portfolio.

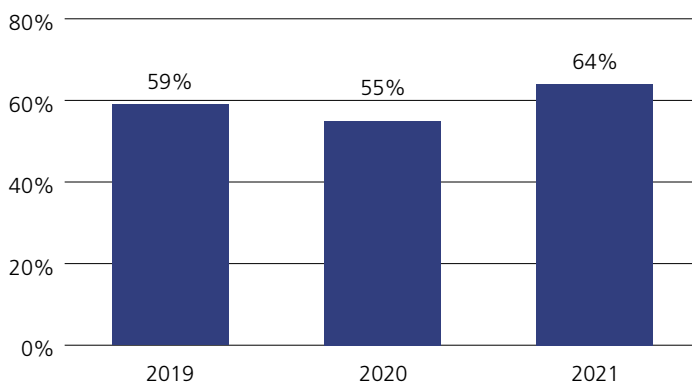
Within social topics, it is clear that diversity initiatives are becoming more important for many companies. Nearly two-thirds (64%) of our portfolio companies have initiatives in place that focus on diversity at the workplace, up from 59% two years ago. With respect to governance, the vast majority of portfolio companies (90%) have a code of conduct or a code of ethics in place, an increase of eight percentage points since 2019. In today's world of increasing regulation, this is to be expected, as it is largely part of the license to operate. Two indicators where we would like to see higher numbers are on having an environmental policy and the number of women in executive management teams. We continue to push for awareness and further action on these topics.

Figure 11: ESG KPIs

ESG KPIs 2021	ESG metric	Portfolio score
General	Implemented an ESG policy	44%
	Provide ESG training to employees	54%
	No ESG-related litigation	94%
Environment	Implemented an environmental policy	40%
Social	Implemented diversity initiatives	64%
	Established a remuneration committee	54%
Governance	Adhere to a code of conduct or ethics	90%
	Women in executive management	21%
	Independent board members	29%
	Established an independent audit committee	46%

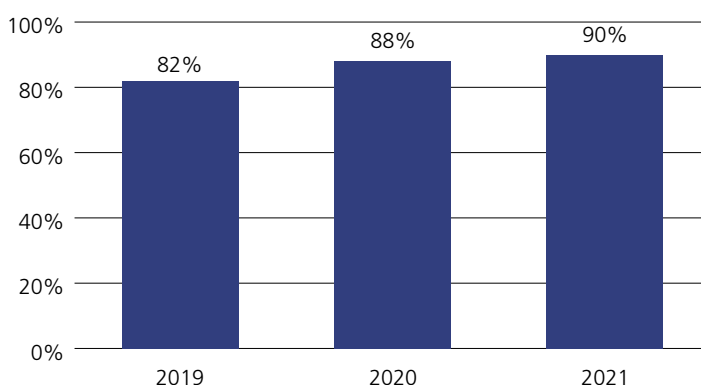
Source: LGT CP

Figure 12: Proportion of companies with diversity initiatives in place



Source: LGT CP

Figure 13: Proportion of companies with code of conduct or code of ethics

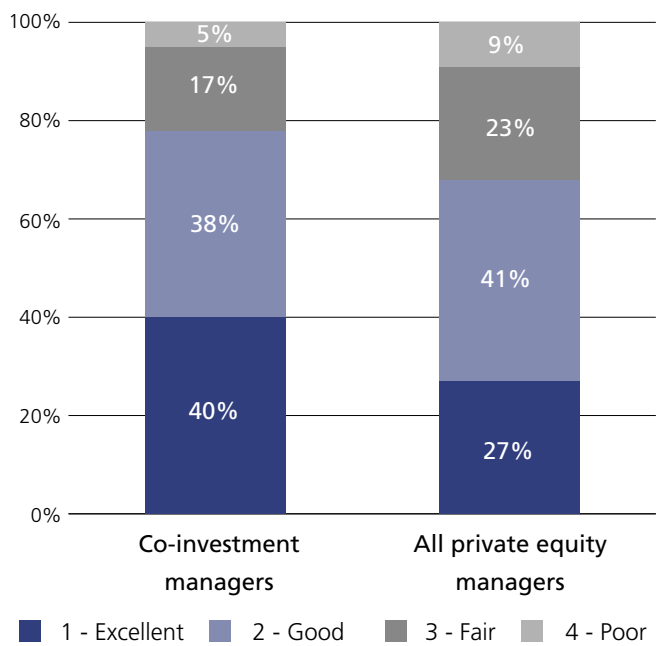


Source: LGT CP

ESG practices of the managers with whom we co-invest

ESG is an important part of our investment and monitoring process for co-investments, as ESG analysis is used to identify potential risks in co-investments as well as to capture upside opportunities. We look at both the individual portfolio company as well as our co-investing private equity manager. We tend to co-invest with managers that have higher-than-average ESG ratings, where 78% have achieved ratings of 1 or 2, versus 68% for our global set of private equity managers. We regard this as a positive sign, suggesting that we “walk the talk” when selecting co-investment opportunities.

Figure 14: ESG ratings: co-investments vs. private equity managers



Source: LGT CP

How our private equity portfolios impact the Sustainable Development Goals (SDGs)

Many investors are increasingly interested in understanding how the companies they invest in impact the environment and society. This can be difficult in private equity because the industry lacks standardized sources of data on companies, which are widely available in the public markets. While there is no easy way of getting around this obstacle, LGT CP has developed an approach that provides investors with a sense of a company’s “SDG footprint” by using public market industry sectors as a proxy. We use data from an external data provider to measure how the company’s products and services impact the SDGs, the set of environmental and social goals unanimously adopted by the UN member states in 2015 and broadly used as a framework within the investment community.

Impact is measured on a scale from -10 to +10 for each product and service the company provides. This proprietary approach covers 300 different product and service categories across all 17 SDGs. Scores for each company are calculated, based on the share of revenue from each product and service category. They are then aggregated at the portfolio level to provide a proxy snapshot of the portfolio’s SDG footprint. The resulting value gives an indication of the portfolio’s strengths and weaknesses from an SDG perspective. The results can be used to analyze further details and review specific investments.

In Figure 15, we highlight the SDG footprint of one of our co-investment private equity portfolios. The chart shows that the portfolio overall has a more positive SDG footprint than the benchmark (MSCI World) for most SDGs. The blue lines show that the portfolio has a positive exposure to SDG 3 (Health and Well-being) which is due to investments in Pharma and Healthcare, while it has a slightly negative exposure to SDG 14 (Life below water) due to certain investments in industrial companies. Finally, it has a positive exposure to Sustainable Cities and Communities (SDG 11), driven by investments in companies providing elderly care and other services.

Figure 15: SDG proxy footprint of the LGT CP co-investment portfolio vs. the MSCI World



Source: LGT CP/MSCI World

Focus on impact

Following many years of ESG leadership and focus on sustainable investing, LGT CP has recently launched a dedicated impact strategy. The program focuses on making co-investments in highly impactful businesses across the US, Europe and Asia, which will be complemented by strategic primary and secondary impact investments. The strategy targets commercial private equity returns. We interviewed one of the strategy's investment professionals, Natalie Sediako, to get her views on impact investing.

Impact investing has seen significant growth in terms of interest and assets. What are the reasons for this?

The growth comes from the increasing urgency and visibility of the environmental and social challenges we face as a society. Damaged ecosystems and stressed social fabrics have created a need for innovative business models that can provide affordable, effective solutions. Capital provided by governments and philanthropic organizations are not adequate to bridge the funding gap towards achieving the necessary progress, and private capital is both desperately needed and well positioned to effect change. As investors and their stakeholders increasingly recognize that their capital can be directed to build a more equitable and sustainable society, they are demanding investment solutions that deliver a clear, measurable impact.

What are the key challenges the impact program looks to address?

Our impact program focuses on four key themes – healthcare, education, inclusive growth and climate action. Across these areas, we look for truly differentiated business models that offer direct and highly effective solutions towards better social and environmental outcomes. To assess impact, we utilize an evidence-based framework that measures the effectiveness, affordability and scalability of the solution, as well as any impact risks.

What are examples of impact investments in the portfolio today?

Over the years, we have made many highly impactful investments. One example is our recent investment in Miami Beach Medical Group (MBMG), a US Medicare Advantage healthcare provider. Medicare Advantage is a program targeted at the elderly population, and is intended to encourage providers to assume overall accountability over patients' care. As Medicare Advantage providers are compensated for delivering better healthcare outcomes rather than for the quantity of services provided, their focus is on prevention and active care management. MBMG is the leading Medicare Advantage provider in South Florida, offering high-quality primary care and a wide range of ancillary specialties. The company also provides additional patient support, such as transportation, home visits and telehealth to ensure the best care for its members.

Another example is our most recent impact investment, Weld North Education (WNE), a leading education technology company developing digital curriculum and tools for students in all grades, from preschool to high school. Lower graduation rates, particularly prevalent in economically disadvantaged communities, lead to crime, unemployment, and the perpetuation of socio-economic inequalities. WNE offers a range of digital learning solutions that are complementary to in-class learning and are highly effective and affordable for school districts. School district data and independent studies confirm the efficacy of WNE's solutions, demonstrating a material uplift in student learning outcomes, particularly in low income and rural communities. In one such district outside Detroit, where approximately 70% of the students were from low-income families, graduation rates increased from approximately 20% to 80% over five years with the help of WNE solutions.

How can an investor best implement impact investing in their portfolios?

We believe that private equity is well positioned to drive meaningful impact because of its long-term investment horizon and the typical high degree of control over value creation. LGT CP's impact program is weighted towards co-investments because this allows us to best drive intentionality across the portfolio. With over 500 manager relationships across Europe, US, and Asia, we see a strong flow of highly impactful co-investments across our private equity platform. This large funnel allows us to be highly selective and invest in the most attractive and impactful opportunities.

Measuring impact is critical in this area of investing. What are the relevant frameworks you leverage?

We look to the Operating Principles for Impact Management, which are commonly accepted as best practice for ensuring that impact considerations are purposefully integrated throughout the investment life cycle. For outcomes, we map impact to the relevant SDGs and targets. Impact efficacy and value creation are measured and tracked over the course of the investment through specific operating metrics.

Could you share some examples of such metrics?

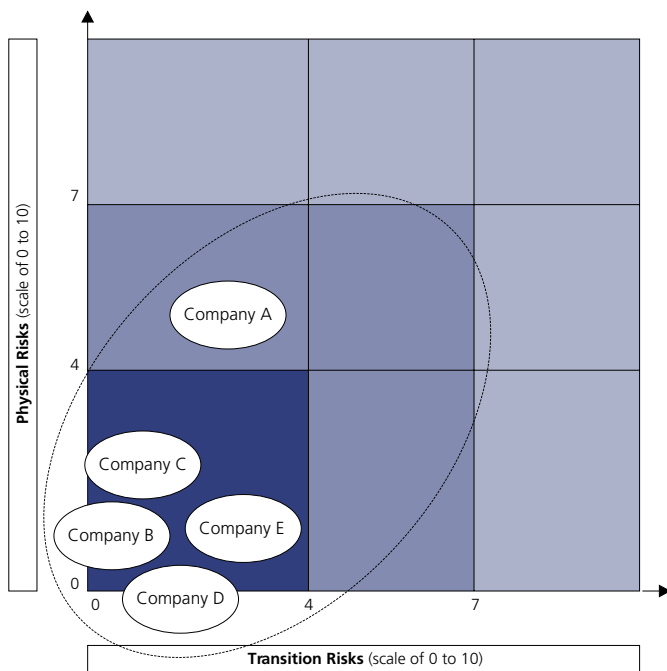
During due diligence we focus on confirming the benefit of the solution in delivering better outcomes than the alternatives. In the case of an education business that improves learning, we look at independent studies confirming the uplift in graduation rates and test scores across different socio-economic groups of constituents. We then look at unit economics for schools to understand affordability, particularly for districts in the lowest income communities. Once the investment is made, we track metrics that capture scalability and impact value creation, such as number of school districts and the number of students enrolled.

Private debt

Climate action within private debt

In line with other LGT CP initiatives on climate change described in this report, we have enhanced the way we manage climate change risk in our private debt portfolio. Our new approach is designed to address the rising expectations of investors and regulators, as well as mitigate intrinsic climate-related business risks. It emphasizes climate risk analysis for asset selection and systematic CO₂ footprint monitoring post investment, in line with the recommendations of the Task Force for Climate-related Financial Disclosures (TCFD).

Figure 16: Physical and transition risks of the portfolio so far



Source: LGT CP

With our climate risk analysis, we systematically consider climate-change induced risks, while assessing the materiality of those risks for any given business. Towards this end, we developed a framework for analyzing climate resilience in terms of physical risks (related to climate change itself) and transition risks (related to the transition to a lower carbon economy), as recommended by the TCFD. On the back of our analysis, we rate the materiality of such risks, which allows for informed asset selection based on climate change considerations and monitoring of the portfolio's composition according to the risks identified. This rating process now forms an integral part of the investment due diligence process carried out on each prospective portfolio company, and the climate resilience rating informs the discussions of the investment committee.

Figure 16 shows the five companies that have been rated so far within the framework, in terms of their physical and transition risks. Scores of 4 and below are considered to be low risk, while a score in the 4-7 range is deemed a medium risk, which would entail further scrutiny from the investment committee. Companies rated 7-10 would invite still more scrutiny, and the investment committee has committed to limiting such companies to less than 20% of portfolio assets.

Examples of climate resilience considerations

Physical risks often include considerations relating to operations and supply chain. Take the example of a mid-sized company that produces goods, while relying on a single centralized facility or a complex single-stream supply chain. The investment team will scrutinize the manufacturer's exposure to climate change-related events, as well as the company's back-up and recovery processes. Each issue will be assigned a materiality score on a scale of 0 to 2, where 0 indicates no anticipated risk, 1 signals a possible risk with moderate materiality, and 2 flags high risk with high materiality. The scores will be aggregated into an overall physical risk assessment as shown in Figure 17.

Figure 17: Assessing physical risks

Physical risks assessment		
Item	Potential impact example	Materiality score
1. Operations	Facility integrity & production capacity	1
2. Supply chain	Raw materials, transportation, access to energy	2
3. Workforce	Health, safety & absenteeism	0
4. End-user environment	End-user behavior changes	0
5. GHG emissions	Direct emissions	1
Total		4

Source: LGT CP

Transition risks may be slightly less intuitive, since they relate to more indirect overall business environment changes triggered by the transition to a lower carbon economy. The increasingly material considerations in this respect are often related to regulatory developments, changing stakeholder expectations or shifting end-user preferences, as shown in Figure 18.

Figure 18: Assessing transition risks

Transition risks assessment		
Item	Potential impact example	Materiality score
1. Technology	Substitution to new tech offerings	0
2. End-market	Shifting end-user preferences	1
3. Supply chain	Health, safety & absenteeism	1
4. Regulatory	GHG emissions pricing & compliance	1
5. Reputation	Negative stakeholder perception	0
Total		3

Source: LGT CP

In one recent example, the team turned down an opportunity to invest in an industrial company that is a global leader in its field. The company produces greenhouse gas (GHG) emissions at several plants globally, but derives much of its leadership position from the high margins it generates from one plant in a low-regulation country, where there are few constraints on carbon emissions and other environmental impacts. The team felt that a business strategy premised on lax regulations is not sustainable, as the regulatory regime in that country could tighten in the face of mounting environmental degradation from climate change. Furthermore, the company's customers could start to shy away from the reputational risk associated with a low-regulation jurisdiction. In either case, the team determined that the transition risk for this company was too high, notwithstanding the otherwise attractive fundamentals.

Portfolio company KPIs

In addition to our work on climate change this year, we have also tracked our usual range of ESG KPIs on the companies in our private debt portfolio. These provide us with insights on how companies are responding to the full set of ESG challenges and opportunities. The portfolio is comprised of small and mid-sized European companies, with a tilt towards those in the service, technology and light industrial sectors. In Figure 19, we aggregate a selection of KPIs across our portfolio of 42 companies to provide a snapshot of how our private debt portfolio overall is performing on ESG.³

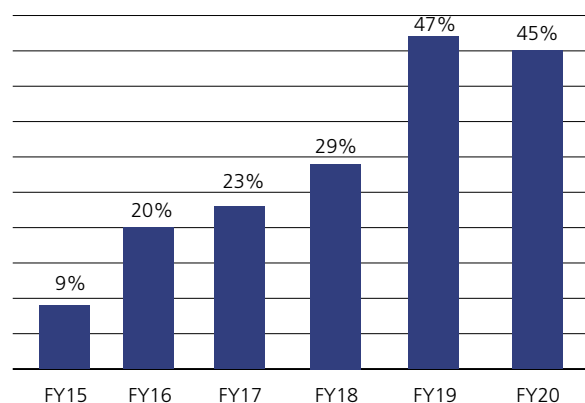
Figure 19: ESG KPIs

	ESG metric	Portfolio score
General	Implemented an ESG policy	57%
	Track ESG initiatives with KPIs and reports	64%
	No ESG-related litigation	93%
Environment	Implemented an environmental policy	48%
	Assess carbon footprint	45%
	Track water or energy consumption	62%
	Track waste volumes, cost and % recycled	40%
Social	Net job creation	55%
	Provide training opportunities	90%
	Company-wide profit sharing	45%
Governance	One or more independent board member(s)	48%
	Proportion of women in executive management committees	25%
	Average number of board meetings per year	9
	Adhere to a corporate code of ethics	67%
	Established independent board committees (management, audit, remuneration, etc.)	67%

Source: LGT CP

For one key indicator, assessing carbon emissions, we observe a positive long-term trend (Figure 20), as the proportion of companies disclosing this information has grown significantly since 2015. Currently, 45% of portfolio companies report on CO₂ emissions, which is broadly in line with last year, accounting for a small change in the sample size. It shows that nearly half of the companies in the portfolio recognize the importance of climate change within business operations.

Figure 20: Proportion of companies assessing their carbon emissions



Source: LGT CP

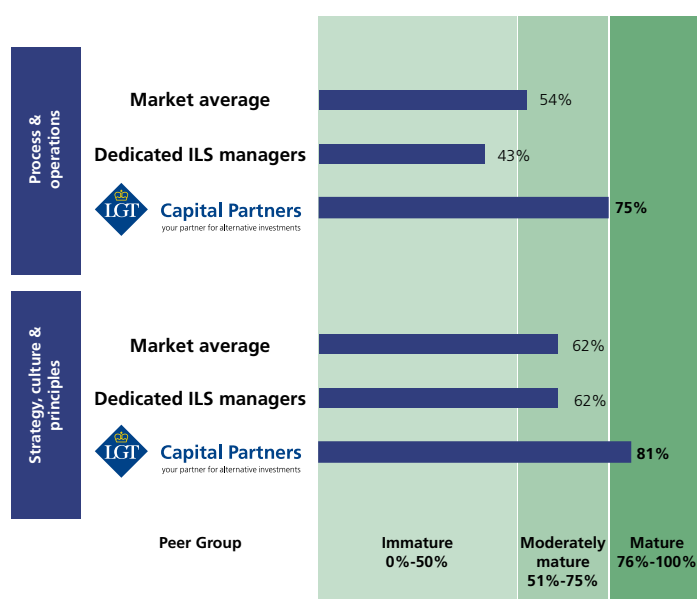
³ Based on our survey of LGT CP private debt portfolio companies as of 31 December 2020, featuring a selection of key items.

Insurance-linked strategies (ILS)

The state of ESG practice in ILS

Many investors agree that ILS solutions are well aligned with the goals of sustainable investing, as the risk capital provided by investors may ultimately be used to rebuild homes and infrastructures after natural disasters. However, this top-down view does not capture the full ESG potential of ILS as an asset class, since much depends on how a manager implements ESG. The global business consultant Synpulse recently sought to assess the state of ESG practice in ILS through a survey of market participants. The consultant surveyed 41 leading insurers and reinsurers, institutional investors and ILS fund managers in North America, Europe/Middle East and Asia-Pacific, asking them a wide range of questions on how they incorporate ESG into their strategies and operations. Based on the responses, Synpulse assessed the organizations on how advanced they are on ESG integration, ranging from not very advanced (“immature”) to very advanced (“mature”).

Figure 21: How LGT CP’s ILS offering compares to its peers



Source: Synpulse, select “Factual” indicators, data as of November 2020

While the majority of respondents thought that integrating ESG is a key factor of long-term success, very few appear to have the processes and necessary resources already in place. We are pleased to share that LGT CP compares favorably to our peers in the maturity of our ESG framework, as shown in Figure 21.

LGT CP scored significantly higher than the market average (all 41 respondents) and dedicated ILS managers in two key areas of ESG, “Strategy, culture & principles” within our firm and integrating ESG into our investment “Processes & operations.” On both measures, the survey found LGT CP’s approach to ESG to be “mature”, while the rest of the market ranged from “immature” to “moderately mature.”

Seamless integration of ESG criteria into our investment process

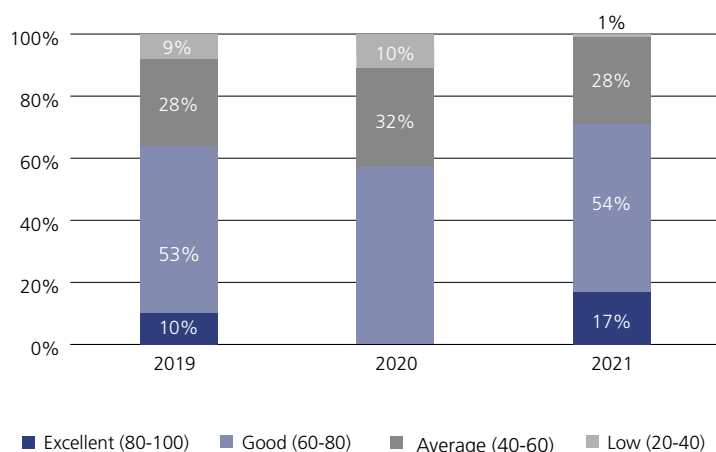
In last year’s ESG report, we outlined our approach for integrating ESG factors into our ILS investment process. We focus on analyzing individual reinsurance counterparties (“cedents”), rather than individual investment positions. With the help of LGT CP’s proprietary ESG screening and scoring tool, the ESG Cockpit, we assess the ESG profile of insurance and reinsurance companies along a clearly defined set of KPIs. The tool draws on publicly available ESG data from a variety of well-established information providers, such as Refinitiv, RepRisk and Inrate, to generate ESG scores for insurance and reinsurance companies. It does so by assessing the companies on the ESG attributes of their operations, products and services, as well as how they impact the SDGs. We believe that the integration of ESG criteria into the qualitative analysis of our reinsurance counterparties has the potential to create value for investors, as it helps to identify and mitigate potential business and reputational risks.

Positive ESG trend within our portfolio

Since our first assessment of ILS counterparties in 2019, we have observed a positive trend within the ratings of our counterparty panel of 95 firms. The average ESG Cockpit rating has increased from 61.5 to 66.4 (out of 100). Compared to two years ago, we now also write a significantly larger portion (71%) of our business with companies rated “excellent” (80-100) and “good” (60-80)

than two years ago. While this change is partially attributable to an increasing number of companies captured in the ESG Cockpit, it also reflects our commitment to improve the overall ESG profile of our ILS business over time.

Figure 22: ESG rating distribution of ILS counterparties



Source: LGT ILS Partners; based on limit written

European companies outperform those domiciled in the US or Asia, both in terms of average rating as well as share of rated companies. This outcome reflects the underlying composition of our cedent panel in the corresponding regions. For example, our European panel of reinsurance counterparties consists mostly of large, multi-national, publicly listed companies. On the other hand, our US panel consists of nationwide counterparties, as well as locally active carriers and government-related entities. In the majority of cases, local players have an ESG framework in place, but have less incentive to commit to the same level of public disclosure than companies that are accountable to a variety of stakeholders (i.e. public and private equity investors, NGOs, etc.).

Figure 23: Rating by counterparty domicile

Counterparty domicile	Average rating (out of 100)
Europe	70.9
USA/Canada	63.8
Asia	60.2
Total	66.4

Source: LGT ILS Partners; based on individual counterparties

The insurers and reinsurers play an active role in reducing carbon emissions

The vast majority of our counterparties (Figure 22), 71%, have ESG ratings of “excellent” or “good” in our proprietary rating framework, so we could continue to focus our engagement efforts on our smaller US-based counterparties. Overall, we see that the insurance and reinsurance sector as a whole is taking an active role promoting positive action on climate change, given the industry’s significant exposure to rising sea levels, extreme weather events and other climate-related effects. The following examples highlight the efforts of some of LGT CP’s top ILS counterparties on climate change:

- Swiss Re has implemented new guidelines on the oil and gas industry, excluding support for the most carbon-intensive companies
- AXA has tightened its coal policy, restricting investments in electric utilities that have a coal-based energy mix of over 30% and/or coal power expansion plans of over 300MW
- Allianz does not offer insurance for coal power plants or mines and requires all companies in its proprietary investment portfolio to phase out coal by 2040

The high loss burden from natural disasters of 2020, in combination with the financial impact of COVID-19 on insurer balance sheets, has led to a “flight to quality” effect within the industry. Insurers are even more selective in choosing providers for their reinsurance purchase. At the same time, high-quality sellers of reinsurance capacity are showing a greater preference for insurance and reinsurance carriers that adhere to high ESG standards and play a key role in fulfilling the climate action goals. This is creating a virtuous circle with ever-greater commercial rewards for companies that take their climate change responsibilities seriously.

Hedge funds

Over the last two years, LGT CP has continued to enhance the way we assess our hedge fund managers on ESG. Last year we built upon our existing framework, which focused on assessing managers on their overall approaches to ESG, by incorporating a bottom-up ESG assessment of the publicly listed assets in our portfolios, allowing for a more comprehensive ESG evaluation. The enhanced approach captures both the ESG practices of managers and the results of their efforts in terms of the assets managed for us. We show the results of this year’s assessments in the latter part of this section.

Over the last 12 months, we have taken the framework a step further by extending it to consider how certain hedge fund trading strategies can positively or negatively affect the carbon footprint of a portfolio. We have also started to bring our hedge fund portfolios in line with the emissions targets of the Paris Agreement (limit global warming to well below 2° Celsius compared to pre-industrial times), using an approach we describe in detail in the section “Public equity and fixed income”. All the while, the managers we partner with have continued to do good work on ESG, as seen in the case of Crake, an equity long/short manager that we highlight in this section.

Making an impact through short selling

An important part of assessing the carbon footprint of a hedge fund portfolio is understanding its treatment of derivatives (both listed and over the counter) and short selling with respect to GHG emissions. While shorting a stock does not reduce overall GHG emissions (just as investing in a stock does not directly increase them), it does have an impact on the companies’ cost of capital. In our view, shorting a stock is a more powerful way to increase the cost of capital of high GHG emitters than simply not holding the

stock. In addition, as can be seen in Figure 24, to properly account for each company’s emissions and avoid double counting, a short investor should subtract its share of emissions from the portfolio.⁴ Based on this rationale, we support “negative carbon emissions accounting,” an approach that is embraced by a number of other large investors and is well articulated in a whitepaper by the global quantitative investment manager AQR Capital Management.⁵ This is the approach we are using to calculate the alignment of our long/short portfolios with the Paris Agreement. We look forward to the day when it is integrated into industry standards promoted by sustainable investment organizations like the Principles for Responsible Investment (PRI) as well as regulators.

Figure 24: Carbon footprint before and after a short sale

	Before a Short Sale		After a Short Sale	
	Shares Held	Carbon Footprint	Shares Held	Carbon Footprint
Investor A	100	100	100	100
Investor B (Short Seller)	0	0	-1	-1
Investor C	0	0	1	1
Aggregate Across All Market Participants	100	100	100	100

Hypothetical example with a stock with 100 shares outstanding, no debt, and the total carbon footprint of 100. Initially, Investor A holds all 100 shares. Next, Investor B borrows a share from Investor A and sells it short to Investor C. For illustrative purpose only.

Source: AQR Capital Management

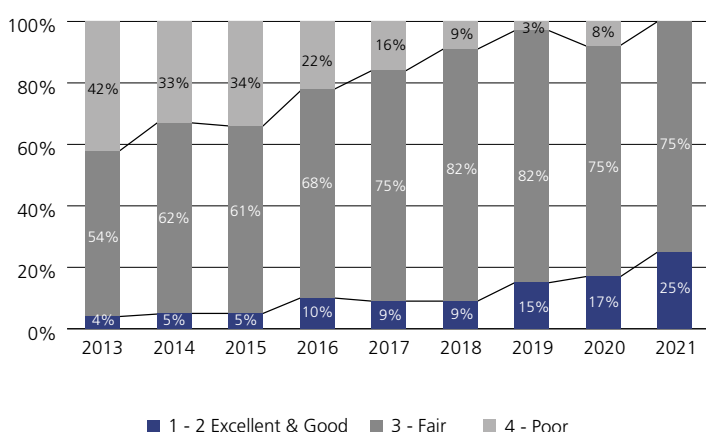
⁴ A similar rationale could be used for derivatives, however in this case we took the conservative approach to account GHG emissions for OTC derivatives as we fear that the brokers’ counterparties will not account for the shares that they hold for hedging purposes, while we excluded listed derivatives where no counterparty is typically holding the physical stock/index.

⁵ “(Car)Bon Voyage: The Road to Low Carbon Investment Portfolios”, AQR, 2020

Current ratings and the long-term ESG development of our hedge fund universe

Our assessment of hedge fund managers shows continued improvement in ESG practices across the portfolio as a whole. We find (Figure 25) that 25% of our managers achieved the top ESG ratings of 1 or 2 this year, compared with 17% last year.⁶

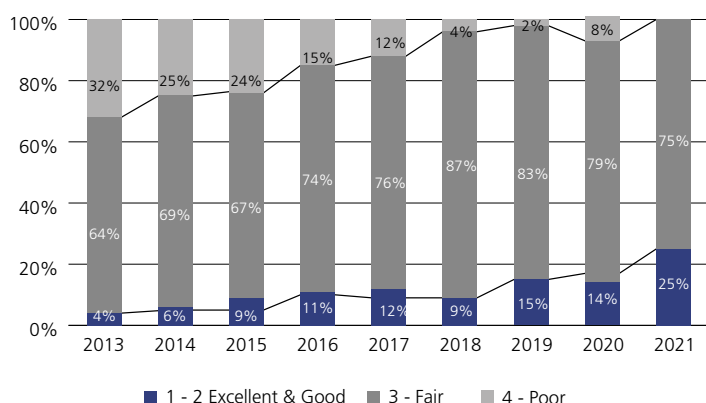
Figure 25: ESG ratings by number of managers



Source: LGT CP

The assets invested with these managers (Figure 26) have also increased to 25%, compared to 14% last year.

Figure 26: ESG ratings by AuM



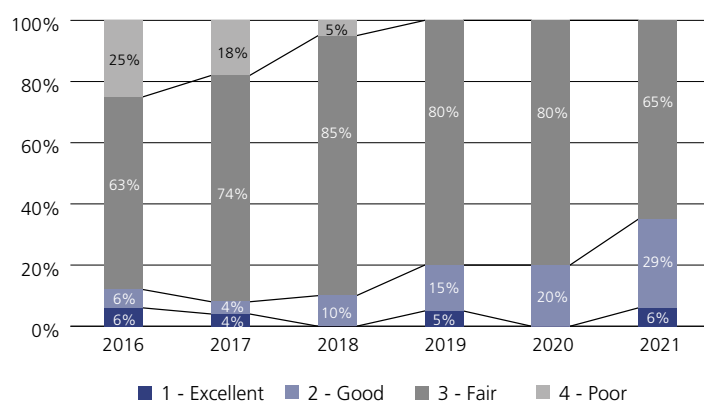
Source: LGT CP

Similar to last year, a large majority (75%) of our hedge fund managers have a rating of 3, and we also invest 75% of our assets with such managers (versus 79% last year).

Following last year's decision to divest from all investments with a rating of 4, we no longer have exposure to managers with poor ESG ratings. We are pleased to report that this achievement was the result of a considerable engagement with these managers during the last year, resulting in the managers enhancing their ESG efforts in order to meet our minimum standards. There was only one case, a relative value manager, where we were forced to redeem the position because our ESG concerns could not be addressed.

Within the equity-related strategies (event driven and long/short), various managers made further improvements in the integration of ESG aspects within the investment process, and now 35% achieved a top ESG rating of 1 or 2. The remaining 65% of managers are rated 3 (versus 80% last year).

Figure 27: ESG ratings of equity long/short and event driven managers



Source: LGT CP

⁶ Based on this year's ESG assessment of 36 managers in our hedge fund portfolios managed for the LGT endowment.

Relative value and CTA/global macro: ESG share classes

As we mentioned in last year's ESG Report, in 2019 we made fund investments with a number of new managers that pursue strategies driven by artificial intelligence (AI), which initially did not meet our expectations for a 3 rating. Although these managers are actively researching the integration of ESG factors into the investment processes of their funds, the findings do not always lead to clear results in terms of ESG and performance correlation. As a near-term solution, managers who are working hard to address our ESG expectations have been able to address our concerns by creating an ESG share class specifically for portfolios managed by LGT CP. Within this share class, they apply our exclusion of controversial weapons and control the carbon footprint of our position to align with the Paris Agreement. Although the ESG impact of this approach is limited only to our portion of the portfolio, its positive effects could compound as more ESG-oriented investors switch to the new share class.

Overall, the breakdown of ESG ratings for our CTA/global macro and relative value managers improved since last year, with 16% currently rated 2, up from 14% in 2020. The remaining 84% are rated 3, as all of the previously 4-rated managers either improved their approach to ESG, earning them higher marks, or they were redeemed.

Case study: Hedge fund with comprehensive framework for assessing and monitoring ESG



Crake Asset Management (Crake) is a hedge fund manager established by former Nevsky Capital founder, Martin Taylor, in 2018. It launched its debut fund in Q3 of 2019 with a global long/short approach across stocks and underlying commodities, which forms part of LGT CP's broader long/short equity strategy. Crake adheres to an ESG policy designed to deliver on their commitment to responsible corporate citizenship, while taking a pragmatic, effective approach to portfolio management. The manager partners with the ESG consultant, ISS, to regularly review the companies in the portfolio, so that it can engage on material ESG issues and, if necessary, adjust the portfolio holdings.

Crake's ESG assessment is a core part of the manager's investment process, which has a strong focus on companies with solid ESG performance. The manager will, however, make exceptions for companies with lower ESG scores, where there is clear evidence the companies are on an improving path, with management teams that are taking real actions to address ESG weaknesses.

With the ISS ratings, Crake assigns a "traffic light" system to monitoring and engaging companies on their adherence to international norms on human rights, labor standards, environmental protection and anti-corruption, where:

- Green indicates the company has no material issues
- Amber indicates the company is under observation due to issues of concern
- Red indicates the company is in violation of a recognized international norm

Of the 43 ISS-rated companies in Crake's current portfolio, 60% are rated Green, 33% are rated Amber, and 7% (three companies) are rated Red.⁷ Of the three Red-rated companies, two are taking active measures to address the environmental issues that have resulted in the low rating, so Crake will continue to monitor their progress. The third represented a very small long position (0.1% of NAV) in a pharma company facing controversies about the possible negative environmental impacts of a chemical it produces. The controversy is the subject of some disagreement within the scientific community, as a number of credible researchers disagree that the chemical is harmful. Crake closed its position in the company after year end, as it cannot ultimately judge an essentially scientific disagreement.

In addition, Crake leverages ISS' ESG ratings to get a detailed assessment of a company's ESG performance based on approximately 100 different criteria. Companies are given decile rankings from 1 (best) to 10 (lowest) within their respective industries. Of the 43 ISS-rated companies in Crake's current portfolio, 81% are ranked in the top-three deciles for ESG performance within their industries, while 9% (four companies) are ranked in the bottom half of their sectors. Among the latter, two have been clearly improving their ESG scores over time, while the remaining two are being carefully monitored for signs of improvement. Failure to do so will result in divestment.

⁷ Portfolio as of 31 December 2020

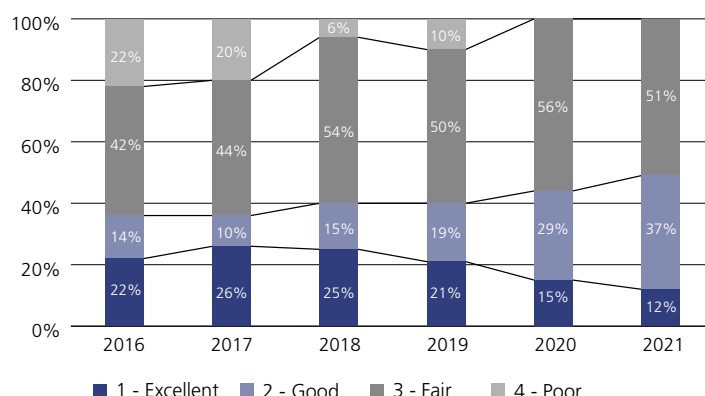
Long-only managers

The positive ESG trend continues across our long-only portfolios, as now almost half of these long-only managers are rated 1 or 2 (vs 44% last year).⁸ Within this cohort, the proportion of managers with the highest rating of 1 has decreased further, as a result of our more stringent approach to assessing managers, which we introduced in 2019. Since then, we have complemented our usual evaluation of manager ESG processes with an in-depth ESG analysis of portfolio companies in the portfolio. This has resulted in a continuous raising of the bar on ESG expectations, making it harder for managers to achieve the top ratings.

We further expect our approach to be validated by new ESG rules and regulations that will ultimately be adopted within the European Union on the back of the European Green Finance Act. As a result, we anticipate an increasing number of managers in the region to adopt practices that align with our ESG standards. Our continuous engagement with a large number of global firms shows that many managers outside of Europe are already moving in this direction, so the proportion of top-rated managers in our portfolios is expected to increase over time.

Beyond our annual assessment of long-only managers, we have been working with them to bring the portfolios they manage for us in line with the emissions targets of the Paris Agreement (using an approach described in the next section, “Public equity and fixed income”). One such manager is State Street Global Advisors (SSGA), who manages LGT CP’s Minimum Volatility mandate and is highlighted in this section.

Figure 28: ESG ratings of long-only managers



Source: LGT CP

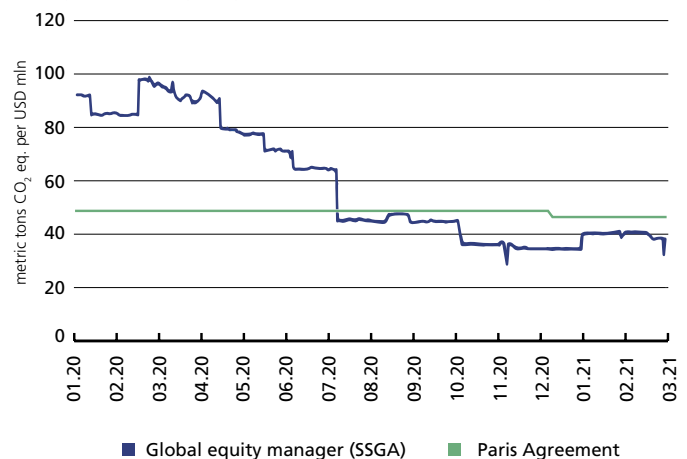
⁸Based on this year's ESG assessment of 41 managers in our long-only portfolios managed for the LGT endowment.

Case Study: Aligning portfolio with the Paris Agreement

STATE STREET GLOBAL ADVISORS

Adapting the mandates of our external managers to our Paris-aligned emissions framework has been a complex process, in which we have used different approaches depending on the type of strategy. For example, LGT CP's Minimum Volatility mandate is managed by State Street Global Advisors (SSGA), a systematic manager with strong ESG credentials and significant experience with low carbon portfolios. Nevertheless, retooling the portfolio to meet the requirements of LGT CP's "well below 2° Celsius" emissions framework entailed a multi-month project to research and think through implementation. The solution had to integrate the emissions target, while optimizing risk, return and trading costs. Over the course of last year, the team developed an approach that achieved the carbon reduction objective (Figure 29) without a material impact on the overall strategy's risk-return profile.

Figure 29: Aligning SSGA portfolio with Paris Agreement



Source: LGT CP

Public equity and fixed income

Assessing alignment of portfolios with the Paris Agreement

LGT CP supports the Paris Agreement to limit global warming to well below 2° Celsius compared to pre-industrial times. The agreement was signed by over 190 countries in 2015 and was subsequently articulated into a formal emissions framework by the Intergovernmental Panel on Climate Change (IPCC). To help achieve the Paris goals, we have been actively managing the carbon footprint for a number of years now and have achieved substantially lower carbon emissions than respective broad market benchmarks, both for equity and fixed income investments. Now we have added a framework to directly assess if our portfolios are aligned with the goals of the Paris Agreement.

The average global temperature is directly linked to the concentration of GHGs in the atmosphere. Given this, we assess the alignment of a portfolio to a temperature increase by measuring the portfolio's emissions and comparing the result to a carbon budget derived from an appropriate climate scenario. We specifically use the "Beyond 2°C Scenario" (B2DS), developed by the International Energy Agency (IEA).⁹

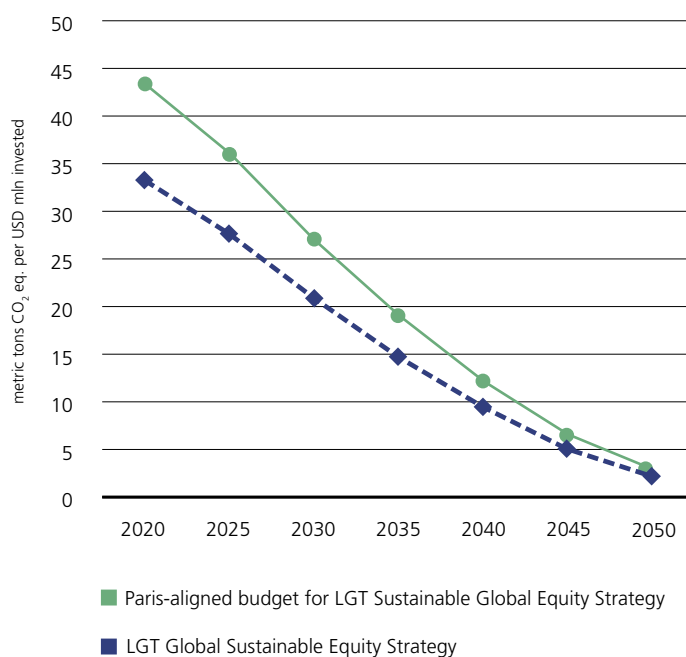
Portfolio emissions are compared to the budget based on the B2DS, with two possible outcomes:

- Portfolio emissions are below or at the B2DS budget: the portfolio is aligned with the Paris Agreement
- Portfolio emissions are above the B2DS budget: the portfolio is not aligned with the Paris Agreement

Paris alignment in practice: LGT Global Sustainable Equity Strategy

Below we show the results of an analysis for our Global Sustainable Equity strategy.¹⁰ The chart shows the derived budget as well as the actual emission level, both measured in tons of CO₂ equivalent per USD million invested. We also project the evolution of the budget out to 2050. The steep decline in budgeted emissions underlines how strongly the decarbonization of the global economy has to proceed, if we want to reach the goals of the Paris Agreement.

Figure 30: Projected decarbonization of the LGT Sustainable Global Equity Strategy over time



Source: LGT CP

The portfolio is well below its current budget, and therefore it is aligned with the goals of the Paris Agreement.

⁹ The B2DS explores how technology improvements and deployment are pushed to their maximum practicable limits across the energy system in order to achieve net zero emissions by 2060 and to stay net zero or below thereafter. This scenario is consistent with a 50% chance of limiting average future temperature increases to 1.75° Celsius by 2100. The B2DS falls within the Paris Agreement range of ambition.

¹⁰ The analysis assumes that portfolio emission levels will remain below the budget, and the portfolio composition remains unchanged, until the two converge to zero in 2050.

How we calculate portfolio emissions

Portfolio emissions are calculated based on the Scope 1 and Scope 2 greenhouse gases of each company in the portfolio. The emissions attributed to the portfolio are determined by the ownership share of the individual companies in the portfolio (size of the portfolio position relative to the enterprise value, including cash, of the respective company) and the company emissions. The results are then aggregated to arrive at the overall portfolio emissions, as shown in the simple example in Figure 31.

The budget for the portfolio is calculated by combining two different approaches. As some industries like electric power generation, steel, or cement production, have homogenous business activities with very high carbon emissions, climate scenarios like the B2DS allocate specific emission budgets to these activities, related to a typical measure of economic activity. These specific models are called Sector Decarbonization Approaches (SDAs).

Figure 31: Calculating portfolio emissions

Company	Portfolio position (mln USD)	Company EV (mln USD)	Ownership share	Company emissions (1,000 t CO ₂ e)	Portfolio emissions (t CO ₂ e)
Company A	10	71,938	0,0139%	34,700	4,820
Company B	25	246,380	0.0101%	7,610	770
Total	35				5,590

Source: LGT CP

For all other lower emitting or heterogeneous business activities, which typically comprise less than 25% of the carbon emissions of economic activity, the so-called “Value Added” approach is used. It determines a company’s emissions budget for a given year by considering the amount of CO₂ allowed per dollar of gross profit, according to the global emissions budget, and multiplying it by the company’s gross profit for that year.

The benefits of carbon budgeting

With the framework described above, we adopted broadly accepted concepts with sound quantitative grounding and made them applicable to our investments. One of the benefits of using SDAs for specific industries is that this explicitly takes into account the different levels of “carbon emission allowances” from Paris-aligned climate scenarios for certain economic activities. A portfolio can be Paris aligned and at the same time have exposure to critical industries, which allows for a diversified investment portfolio. In addition, the concept of Paris-aligned portfolios reaches much farther than only investing into industries with low emissions.

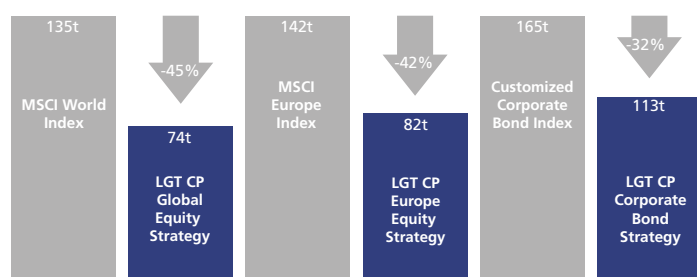
We have started to use our framework for listed equity portfolios, as relevant data is widely available. At the same time, we are working to expand this to an overall multi-asset portfolio, taking into account various other asset classes. The challenges that remain are not only conceptual, with the assessment of government debt being the most obvious, but also consist of applying the concepts to asset classes with very limited data available, such as private markets.

Substantially lower level of carbon emissions than the benchmark

The current carbon footprint of an investment portfolio, or the absolute level of GHG emissions, is a key metric for many investors, so we measure this for all Sustainable Investment Strategies, and report on it below for selected strategies. We also compare the footprints of the various strategies with those of their respective benchmark indices, so our investors can better understand the impact of our investment decisions in terms of relative carbon intensities.

The chart shows the aggregated normalized GHG emissions for three different strategies against their respective benchmarks, with carbon footprints that are 32–45% lower than the benchmarks. As an example, the portfolio companies of our Global Equity Strategy generate 74 metric tons of carbon emissions per year, while the corresponding benchmark figure is 135 metric tons, a difference of 61 tons.

Figure 32: Carbon emissions of select LGT CP strategies relative to their benchmarks (Metric tons CO₂ equivalent/USD million company sales)



Source: Refinitiv, LGT Capital Partners. All data in metric tons CO₂ equiv./USD 1 million company sales per calendar year. Data as of 28 February 2021

State-of-the-art framework for analyzing the impact of fixed income portfolios on the SDGs

Mapping a broad fixed income portfolio to the SDGs is a complex task, so LGT CP has established a holistic framework to meet the challenge. Such portfolios typically contain bonds from many different types of issuers, such as sovereigns, supranationals, corporates and organizations specializing in green, social, sustainable and sustainability-linked bonds. With the emergence of the SDGs as a common framework for targeting sustainable outcomes, asset managers and investors share a common interest in measuring the impact of portfolios on the SDGs, whether in absolute terms or relative to a benchmark. Given the wide variety of issuers and bond types, measuring the impact of a broad fixed income portfolio on the SDGs requires a sophisticated framework that can assess each bond on its own merits. At LGT CP, we have developed such a framework, as we describe below.

Figure 33 shows how our flagship LGT Sustainable Bond Global Strategy impacts the SDGs relative to its benchmark, using our framework, which is based on a wide range of metrics linked to key characteristics of the sovereign and corporate borrowers in our portfolio. The chart shows that the LGT portfolio outperforms the benchmark on 15 of the 17 SDGs, and by a wide margin on several measures, including SDG 7 (Affordable and Clean Energy), SDG 10 (Reduced Inequality) and SDG 13 (Climate Action).

Figure 33: LGT Sustainable Bond Global Strategy impact on the SDGs relative to its benchmark



Sources: LGT CP/CMA High-level mapping tool

How LGT CP measures SDG impact in a bond portfolio

Each of the four major types of bonds in our portfolio has its own characteristics and challenges in assessing them for their SDG impact. Our framework addresses these various challenges as described below.

Sovereigns

The largest part of a global aggregate fixed income portfolio typically consists of sovereign bonds. For these bonds, we analyze the institutional framework of the country, as well as a set of social and environmental KPIs. For assessing the SDG contributions, we use a framework from the Bertelsmann Foundation, which draws upon UN-recommended KPIs for measuring a country's level of achievement of the SDGs. While countries like Sweden and Switzerland stick out as very positive examples with high positive contributions to many SDGs, even the high performers show some negative contributions, like contribution to SDG 14 Life Below Water in the case of Sweden and SDG 12 Responsible Consumption and Production for Switzerland.

Supranationals

Analyzing the SDG impact of bonds from supranational issuers requires a different methodology, which considers the governance score of the institution and an assessment of the project being financed. Investors might assume that supranationals generally score well on positive SDG impact, given the typical mission orientation of these organizations, but our assessment approach results in a surprisingly diverse range of scores. We find that many supranationals finance controversial projects, have mediocre governance or even corruption issues, which can have a very detrimental effect on the issuer's evaluation. One example of this is an international development bank, which has an SDG impact close to zero because the positive impact from lending activities is counterbalanced by negative impacts, especially on SDG 11 (Sustainable Cities and Communities) and SDG 15 (Life on Land). One institution that has managed to avoid such shortcomings is the African Development Bank, which has one of the highest scores, driven mostly by contributions to SDG 1 (No Poverty) and SDG 7 (Affordable and Clean Energy).

Corporates

We apply still a different process to corporate issuers, where we map their impact in two ways. First, we analyze the impact of the companies' products and services on the SDGs, using LGT CP's proprietary ESG Cockpit, and then we analyze the impact of their operations. Assessing the impact of a given business activity is not always straightforward, as different aspects of the business can

touch the SDGs in different ways. For example, burning natural gas is less carbon intensive than coal, but it still contributes to global emissions. Similarly, industrial automation can increase resource efficiency and reduce injuries, while also disrupting segments of the labor market. In short, there are often several orders of impact associated with a given business activity, but there are also areas for debate or further consideration. This is why LGT CP looks at a wide range of factors across a company's products, services and operations to triangulate a final impact score.

Green, social and sustainable (GSS) bonds

GSS bonds issued by corporates, sovereigns and supranationals require yet another approach, as they typically explicitly target one or more of the issues addressed by the SDGs. Many societal priorities have been brought to the forefront during the COVID-19 pandemic, such as lack of economic opportunity and access to basic services in health, sanitation, education, energy and financial inclusion. Until recently, mainly niche investors like microfinance institutions focused on these challenges, but now a broad range of issuers are active in this space. To evaluate them on their impact on the SDGs, we first check whether the issuers' project is in line with the recommendations of the ICMA Green Bond Principles. We then categorize the use of proceeds and map them to the relevant SDGs, using a matrix developed by Moody's. Finally, we use any additional information such as the secondary opinion and external analyst views for verification of our assessment.

Looking ahead

The ongoing evolution of sustainable financing and its product innovations will demand a constant assessment and adjustment of our internal ESG-related bond analysis tools. We are currently finalizing a new process to score sustainability-linked bonds and detect potential greenwashing in our portfolios. Also, engagement is becoming an ever more important element of our analysis, especially when it comes to the evaluation of public controversies that weigh negatively on the SDG contribution. Finally, it is highly likely that regulatory frameworks like the EU Taxonomy will increasingly influence or even dictate the methodological process.

The LGT endowment

The multi-asset perspective

We leverage our expertise across the firm to integrate ESG into the LGT endowment, a USD 15 billion dollar portfolio that we manage for the Princely Family of Liechtenstein and clients who invest alongside them. The ESG approach we take with this globally invested multi-asset strategy spans our entire firm and includes all of our specialized investment teams, processes and decision-making. 2020 marked the first time in more than 20 years that the mandate of the LGT endowment was amended, adding sustainability as an explicit target, in addition to its long-term performance goals.

The ESG processes we use to screen, select and interact with both our direct investee companies and our external managers are covered throughout this report. In this section, however, we focus on the vital first step for any multi-asset investor, namely the strategic asset allocation. Our approach integrates ESG risks and opportunities into our scenario-based strategic asset allocation framework. From this framework, we also set priorities for our climate action strategy, which aims to decarbonize the portfolio to align with the Paris Agreement and enhance the overall climate resilience of the portfolio.

Scenario-based strategic asset allocation framework

At LGT CP, a forward-looking scenario approach provides the basis for long-term asset allocation decisions. Current scenarios include, for example, “reflationary expansion”, “global protectionism” and “competitive prosperity”. Each of our eight scenarios, while macro-economic in nature, include top-level ESG considerations such as:

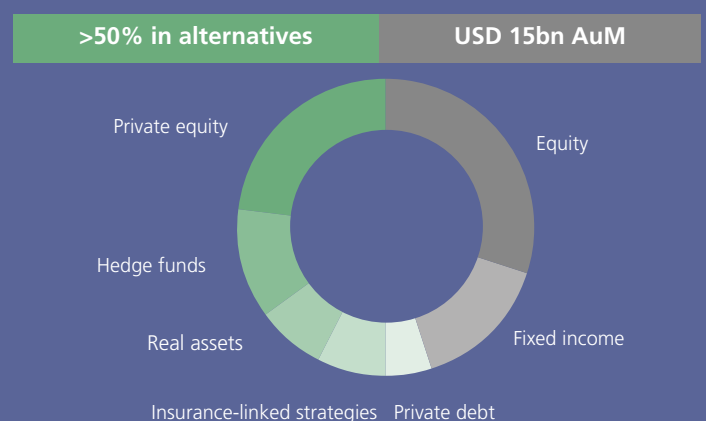
- E – Stress-testing the financial implications of climate change and the transition to a carbon neutral economy, in particular related physical and transition costs
- S – Rising wealth and income inequality, populism and protectionism, data privacy issues, loss of confidence in institutions
- G – Standards of corporate and state governance in emerging markets, monopolistic behavior of large companies (“Big Tech”) and policy reaction

These considerations also take into account positive developments. For example, in the “reflationary expansion” scenario, we expect strong fiscal investment programs (e.g. European Green Deal) to support green innovation. This could provide significant opportunities in the form of new business models, products and services, which can revive productivity and economic growth.

The LGT endowment at a glance

LGT CP has been managing and investing a combined portfolio of traditional and alternative investments, the LGT endowment, for over 20 years. Today, this strategy has USD 15 billion of assets under management, including a significant investment of more than USD 3 billion by our shareholder, the Princely Family of Liechtenstein. Its investment mandate is to achieve long-term asset growth with moderate volatility and a strong focus on sustainability. It is a broadly diversified multi-asset portfolio with an emphasis on alternatives, similar to that of US Endowments funds, combining the entire investment platform of LGT CP.

Figure 34: Strategic asset allocation of the LGT endowment



Source: LGT CP

Additionally, as the importance and threat of climate change continues to increase, 2021 saw the introduction of a dedicated “climate distortions scenario” in our framework. Instead of focusing only on very long-term and gradual impacts (on an annual basis), we incorporated an outlier and stress-test like scenario, which allows for realistic sentiment shocks and sudden repricing of financial assets. The scenario consists of a series of extreme weather events, starting with physical damage, subsequently followed by the introduction of strong policy measures, such as carbon pricing and strict environmental regulation.

In this scenario, both physical and transition costs are likely to be a major drag on the economy and on asset performance, particularly in carbon intensive industries and growth-sensitive segments such as equities. Emerging market assets are likely to be more negatively affected than developed markets, due to a higher carbon-intensity of their industry mix and a higher vulnerability to adverse weather outcomes. With respect to fixed income, inflation-linked bonds are expected to outperform nominal bonds due to rising inflation expectations. Potential winners in this scenario are technology and volume leaders in renewables and companies with products and services that positively impact climate change.

In our view, early and stringent decarbonization of investment holdings seems to be the best path forward for improving portfolio resilience and helping to mitigate devastating climate change.

Climate action approach of the LGT endowment

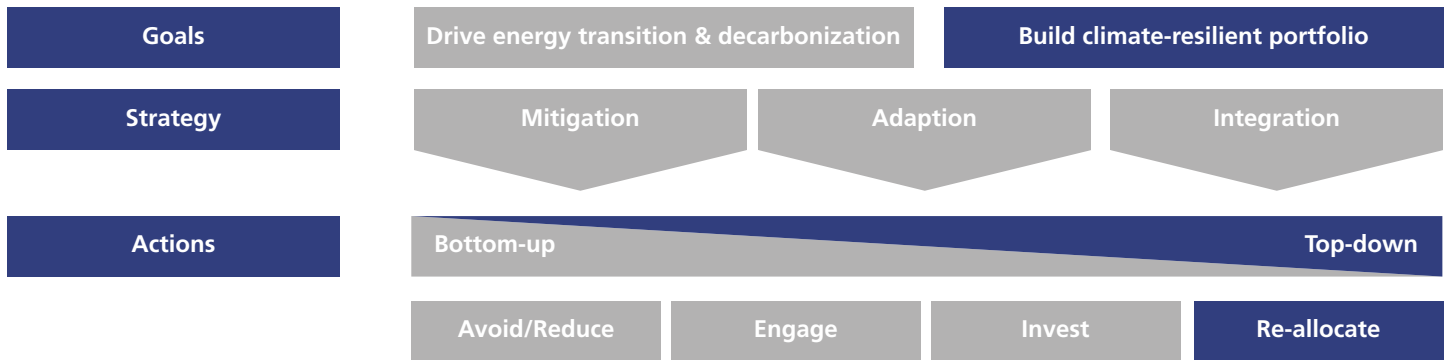
Based on our scenario framework, we found that carbon-intensive investments pose a significant risk for both the environment and the portfolio. In response, we set two core objectives for the LGT endowment’s climate action plan:

1. Contributing to the energy transition of the global economy and decarbonizing the portfolio
2. Building a climate-resilient portfolio

The latter entails identifying critical drivers and potential vulnerabilities and, if necessary, reducing allocations to exposed segments, as well as avoiding concentrated exposures to climate risk. In order to set an ambitious and measureable goal, we committed to aligning the LGT endowment with the Paris Agreement. This entails both immediate portfolio actions and continuous future efforts to ensure alignment with net zero emissions.

Our climate action strategy is built on the three dimensions of impact, with 1) “mitigation” aimed at tackling the causes and minimizing the possible impacts of climate change, (2) “adaption” focused on taking advantage of any opportunities that arise and, (3) “integration” considering climate-related factors across decision levels.

Figure 35: Climate action framework



Source: LGT CP

We can take concrete actions either bottom-up through stringent security selection or top-down through reallocation of capital between asset classes. Some of the actions that we have taken in the LGT endowment over the last three years include:

- Avoiding/reducing exposures to single companies or entire sectors, especially those whose emission pathways are fundamentally inconsistent with the goals of the Paris Agreement. For example, we have excluded from our investment universe all companies that are involved in thermal coal production
- Engaging with our managers has been and will remain a priority. We were able to significantly reduce the carbon intensity of many managers' portfolios through intensive collaboration and the setting of carbon budgets (see example of State Street Global Advisors described earlier in the report)
- Investing into climate solutions. For example, we have constantly increased our allocation to green bonds and the renewable infrastructure segment. Furthermore, our investment teams are called upon to continue identifying investments that can make a positive contribution to mitigating climate change
- Reallocating capital away from concentrated transition and physical risks (including the risk of stranded assets) into strategies and sectors that are much richer in sustainable and climate-related opportunities. For example, we shifted our dedicated allocations from conventional energy infrastructure and natural resource equities (i. e. extractive industries) into private equity, which offers a broad range of opportunities in low carbon intensive industries in the technology and service sectors

We continue to work on these dimensions as we progress towards our aim of aligning the entire portfolio with the emission pathway of the "Beyond 2°C Scenario" of the Paris Agreement. With this approach, we aim to make a meaningful contribution to mitigating the damaging effects of climate change, while also enabling investors to benefit from attractive opportunities that arise from the ensuing changes to the global economy.

Net Zero Asset Managers initiative

LGT CP recently joined the Net Zero Asset Managers initiative, which aims to galvanize the asset management industry to commit to a goal of net zero emissions.



As per March 2021, the Net Zero Asset Managers initiative had a total of 73 signatories representing USD 32 trillion in assets under management. The initiative was originally launched in December 2020 as a commitment to support the goal of net zero GHG emissions by 2050 or sooner, in line with global efforts to limit warming to 1.5°C.

To ensure real world progress ahead of 2050, the asset manager signatories have committed to set interim targets for 2030, consistent with a fair share of the 50% global reduction in GHG identified by the Intergovernmental Panel on Climate Change (IPCC) to halt global warming at 1.5°C. Supporting the acceleration of action, signatories will submit an interim target, within a year of joining the initiative, for the proportion of assets to be managed in line with reaching net zero emissions by 2050 or sooner.

Asset managers joining the initiative commit to transparent and rigorous accountability. Signatories will annually report progress against the TCFD recommendations, including setting out a climate action plan and submitting this for review by peers. This will ensure the approach applied is based on a robust methodology, consistent with the Race to Zero criteria, and action is being taken in line with the commitments.

Diversity and inclusion at LGT Capital Partners

At LGT CP, we value the diversity of our staff members by gender, race, nationality, sexual orientation and religion. We believe that diverse organizations attract and retain higher quality talent, while also improving decision-making that ultimately benefits our investors. We are also convinced that diversity is an integral component of being a long-term oriented, sustainable investor, which offers equal opportunities to people from underrepresented backgrounds.

We are in the early stages of a long-term diversity and inclusion (D&I) journey, but we are making progress. We have established a D&I Committee comprised of senior team members and focused on promoting initiatives internally. Furthermore, LGT CP's Executive Management Team has adopted D&I as one of its key initiatives. Highlights of what we have achieved so far are:

- more than 25% of senior promotions in 2020 were diverse individuals who have been with LGT CP for an average of nine years
- 30% of new hires in 2020 were female
- from 2017 to 2020 we increased the proportion of senior female team members from 6% to 10%
- D&I engagement with our private markets, hedge fund and long-only managers, where 47% currently have D&I policies in place

Talent recruiting and retention

A top priority for LGT CP over the last couple of years has been to recruit a more diverse workforce. A first step in achieving this has been to broaden the application pool to attract and recruit diverse talent. One example of this is a partnership with the University of St. Gallen in Switzerland. Twice a year, we host events for female students on campus and at our office to introduce them to our firm and asset management as an industry. In 2020, this included hosting two virtual events to keep the momentum going.

We also set clear expectations with the recruitment agents we work with to present a broader pool of talent, while working with a wide range of external organizations to broaden the group of applicants. Our 2020 recruitment results, where 30% of new hires were female, show that these efforts are bearing fruit. Equally important is the development and retention of diverse talent within the firm. Only by ensuring an inclusive culture, where all employees are given the same opportunities, will we be able to retain a diversified workforce. A positive result from our staff development and retention efforts is evident in our 2020 staff appraisal cycle, where women and people from diverse backgrounds accounted for over 20% of the promotions to partner/principal. We are committed to increasing this ratio over the next couple of years.

Partnering for D&I success

In 2020, we increased our participation in industry organizations focused on D&I in order to collaborate with peers and to help raise awareness in our industry. This has included joining a number of new organizations:

- Out Investors – a global initiative aimed at making the investment industry more welcoming for LGBTQ+ individuals
- Level 20 – an organization dedicated to increasing the number of women in the private equity industry, with the target of 20% of senior roles to be held by women. Senior LGT CP team members actively participate by serving as mentor to young female professionals within the firm
- Private Equity Women Investor Network (PEWIN) – an invitation-only organization, with the mission of fostering and growing relationships globally, professionally and personally, among senior women in private equity
- Women in Secondaries network – seeks to empower, promote and support women working in the private equity secondaries industry
- ILPA Diversity in Action – an initiative that brings together limited partners and general partners who share a commitment to advancing diversity, equity and inclusion in the private equity industry

Meanwhile, in Switzerland, we continue to support Advance Gender Equality in Business, which we joined in 2017 and have participated in both as mentor and mentee for high potential female staff members in senior management. We look forward to further expanding our active participation in organizations related to D&I.



About us

LGT Capital Partners is a leading alternative investment specialist with USD 75 billion in assets under management and more than 550 institutional clients in 41 countries.¹¹ An international team of over 600 professionals is responsible for managing a wide range of investment programs focusing on private markets, liquid alternatives and multi-asset class solutions. Headquartered in Pfaffikon (SZ), Switzerland, the firm has offices in New York, Dublin, Frankfurt, London, Paris, Vaduz, Dubai, Beijing, Hong Kong, Tokyo and Sydney.

LGT CP has a long-held commitment to incorporating ESG considerations into its client programs and its business overall. Since 2003, many of our programs have had a responsible investment clause written into their governing documents, authorizing us to exclude investments that are substantially exposed to arms-related activities, violations of human rights, irresponsible treatment of the natural environment or other non-ethical conduct of business. Consideration of ESG issues is an

integral part of our investment process, as our investment teams are responsible for taking into account ESG considerations when performing due diligence on investments. Any opportunity that is pursued will have been vetted for such issues.

LGT CP has been a signatory to the Principles for Responsible Investment (PRI) since 2008. In 2018, Tycho Sneyers, a managing partner and chairman of the firm's ESG Committee, was elected to the the board of directors of PRI, where he helps to provide strategic direction to the global body of asset owners and asset managers. LGT CP also participates in the Carbon Disclosure Project (CDP) and the European Sustainable Investment Forum (Eurosif), the Montreal Carbon Pledge, the Institutional Investors Group on Climate Change (IIGCC) and Climate Action 100+.

In 2020, the PRI awarded LGT CP scores of A or A+ across all modules evaluated in its annual RI Assessment Report.



¹¹ Data as of 31 March 2021. AuM data is estimated and subject to change. Private market assets are stated in terms of committed capital.

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ESG disclosures

The impact strategy mentioned in this document is considered to meet the criteria of an Art. 9 strategy under EU 2019/2088. Investors should note that, relative to the expectations of the Autorité des Marchés Financiers, this strategy presents disproportionate communication on the consideration of non-financial criteria in its investment policy. Further, it is considered that the name of this strategy is disproportionate to the AMF's consideration of non-financial criteria. The sustainable long-only equity and bond strategies as well as the most recent private debt strategy mentioned in this document, are considered to meet the criteria of an Art. 8 strategy under EU 2019/2088. Investors should note that, relative to the expectations of the Autorité des Marchés Financiers, these strategies present proportionate

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