

ESG Methodology

Lupus alpha Sustainable Convertible Bonds

Target

Lupus alpha's corporate culture as an independent, owner-managed / partnership-based asset manager is clearly focused on sustainability. With *Lupus alpha Sustainable Convertible Bonds*, we are responding to the growing demand for investment strategies with a sustainable focus. With this fund, investors who put emphasis on sustainable investments, benefit from the advantages of the convertible bond asset class. Thanks to their hybrid character of bonds and equities, this asset class offers convexity, which means a stronger participation in rising than in falling equity markets, a low interest rate sensitivity and advantages in diversification, while at the same time taking comprehensive ESG criteria into account.

Responsible investing makes an important contribution to making capital investments sustainable. As an investor with a fiduciary mandate from our clients, we therefore want to make our contribution and only invest in companies that pay sufficient attention to certain sustainability criteria.

For this fund, the responsible portfolio managers conduct numerous company meetings as part of the fundamental investment process. Sustainability topics, especially governance, are an integral part of the company analysis.

We review the appropriateness of our ESG methodology in an annual review process. Changes to the methodology are documented internally.

Methodology

All investable companies¹ are classified according to environmental, social, ethical and governance criteria. The analysis includes, among others, social standards, environmental management, product portfolio and corporate governance. A comprehensive negative screening process excludes investments that do not meet certain minimum standards.

In doing so, the PAB (Paris-aligned benchmark) criteria² developed by the EU, which are in line with the Paris Climate Agreement, are taken into account. This means that an investment is excluded if at least one of the following criteria applies:

- Activities related to **controversial weapons**
- Cultivation and production of **tobacco**
- Violations of the Organisation for Economic Cooperation and Development (**OECD**) Guidelines for Multinational Enterprises. This audit continues to comprise:
 - Violations of UN Global Compact (**UNGC**)
 - Violations of **ILO** core labour standards in the company and the supply chain and inadequate response/appraisal of the company

¹ If issuer and underlying equity do not match, both are analysed in the negative screening process.

² The PAB criteria are applied to the entirety of the fund's assets. A description of the criteria can be found in Art. 12(1)(a)-(g) of the Commission Delegated Regulation (EU) 2020/1818 of 17 July 2020 (eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32020R1818).

- Violations of UN Guiding Principles on Business and Human Rights (**UNGPR**)
- Exploration, mining, extraction, distribution or refining of **hard coal and lignite** $\geq 1\%$ revenue
- Exploration, extraction, distribution or refining of **oil fuels** $\geq 10\%$ revenue
- Exploration, extraction, manufacturing or distribution of **gaseous fuels** $\geq 50\%$ revenue
- Electricity generation with a GHG intensity of more than 100 g CO₂ e/kWh

In addition, the following exclusion criteria are considered for all securities and money market instruments:

Environment:

- Revenue from energy production from thermal coal $> 0\%$
- Revenue from production and distribution of nuclear electricity $> 0\%$
- Revenue from products and services for the nuclear electricity industry $> 3\%$
- Revenue from uranium mining $> 0\%$
- Revenue from conventional extraction and production of oil & gas $> 5\%$
- Revenue from unconventional extraction and production of oil & gas (incl. oil sands, oil shale & fracking) $> 0\%$
- Revenue from products and services for extraction and production of oil & gas $> 5\%$
- Revenue from energy production from oil & gas $> 0\%$
- Revenue from genetically modifying organisms (GMOs) for agricultural use or human consumption $> 5\%$

Social / Ethics:

- Activities related to nuclear weapons
- Revenue from production of military goods and related services (e.g., research) $> 5\%$
- Revenue from production or sale of firearms and ammunition for civilian use $> 5\%$
- Revenue from production of alcohol $> 5\%$
- Revenue from distribution of alcohol $> 33\%$
- Revenue from distribution of tobacco $> 33\%$
- Animal testing for non-medical purposes (without tolerance limit)
- Commercial/industrial (intensive) animal farming for the purpose of food production or fur farming (without tolerance limit)
- Production of fur (without tolerance limit)
- Revenue from production and distribution of pornographic content $> 3\%$
- Production or development of products that are used as abortifacients (without tolerance limit)
- Stem cell research with human embryos (without tolerance limit)
- Revenue from gambling $> 5\%$

Governance:

- Very severe, ongoing controversies for which the company is directly responsible
- Very severe, partially concluded controversies for which the company is directly responsible

- Violations of international corruption conventions and poor response/appraisal of the company

Consideration of Principal Adverse Impacts on Sustainability Factors (PAIs)

In addition to the aforementioned criteria the following principal adverse impacts on sustainability factors are material and binding for all securities and money market instruments:

Environment:

- **Carbon footprint & carbon intensity**
- Activities negatively affecting **biodiversity**-sensitive areas

Social:

- Violations of **UN Global Compact** principles and Organisation for Economic Cooperation and Development (**OECD**) Guidelines for Multinational Enterprises
- Exposure to **controversial weapons** (anti-personnel mines, cluster munitions, chemical weapons and biological weapons)

Governance:

- **Board gender diversity** (no female board members)
- Cases of insufficient action taken to address **breaches of standards of anti-corruption and anti-bribery**

If an investee company has principal adverse impacts on the sustainability factors mentioned, this generally leads to exclusion. However, in order to offer companies the opportunity to improve on certain factors over time ("transition") we start an engagement process with companies concerning

- **Carbon footprint & carbon intensity** (if both metrics are in the bottom decile of corresponding IVA-industry)

or

- Insufficient **board gender diversity** (no female board members).

We can only invest in the investee company if there are comprehensible plans for improving on these PAIs or if plans can be agreed on with the company in a direct dialogue. For these companies, we document the plans as well as the desired and implemented changes. If the desired targets are not met or if the company does not show the agreed willingness towards change, the position is sold as a last resort after several escalation levels.

The engagement process described above can only be applied to carbon-related PAIs or to board gender diversity. If an investee company requires engagement in both areas mentioned, we refrain from making an investment.

Additional criteria for explicitly sustainable investments

In addition to the standards, revenue limits and consideration of PAIs, we commit to invest **at least 51% of the fund's assets** in convertible bonds that qualify as **sustainable investments**. For this, we examine three criteria:

- 1. Positive contribution to an environmental or social objective:** We consider an investment/a company to be sustainable if its products or its operational behaviour are aligned or strongly aligned with at least one of the 17 Sustainable Development Goals (SDGs)³, and at the same time its products and operational behaviour are not misaligned or strongly misaligned with any of the other SDGs.⁴
- 2. Do No Significant Harm (DNSH):** Investments/companies must adhere to the principle of causing no significant harm. For this assessment, we analyse all relevant PAIs and define specific criteria and thresholds. If a company violates at least two of these criteria or thresholds, it cannot be classified as sustainable. Due to the still insufficient data quality, non-sustainability is only determined after two violations. This minimizes the risk of excluding investments due to potential data errors. However, for PAIs that we classify as particularly critical (e.g., involvement in controversial weapons), a more detailed examination is carried out in advance to ensure exclusion in the event of a breach (see above).

We consider the following ten mandatory PAIs for companies. For numerical PAIs, we calculate the percentile within the IVA industry of the respective company.

PAI	criteria/ threshold
PAI 2: Carbon footprint	90%-percentile
PAI 3: GHG intensity of investee companies	90%-percentile
PAI 4: Exposure to companies active in the fossil fuel sector	Yes
PAI 5: Share of non-renewable energy consumption and production	90%-percentile
PAI 6: Energy consumption intensity per high impact climate sector	90%-percentile
PAI 7: Activities negatively affecting biodiversity-sensitive areas	Yes
PAI 9: Hazardous waste and radioactive waste ratio	90%-percentile
PAI 10: Violations of UN Global Compact principles and Organisation for Economic Cooperation and Development (OECD) Guidelines for Multinational Enterprises	Yes
PAI 13: Board gender diversity	0%
PAI 14: Exposure to controversial weapons (anti-personal mines, cluster munitions, chemical weapons and biological weapons)	Yes

When determining the relevant PAIs, we take potential overlaps (e.g., between PAI 1 and PAI 2) into account, as well as the general availability of data for a given PAI. The goal is to avoid disadvantaging issuers that provide data. However, data availability is continuously monitored and evaluated so that our approach can be promptly adjusted in response to changes.

³ www.un.org/sustainabledevelopment

⁴ We apply MSCI ESG methodology when considering contribution to the SDGs (Sustainable Impact Metrics: <https://www.msci.com/our-solutions/esg-investing/impact-solutions>).

As this is a pure convertible bond fund, PAIs for sovereigns and supranationals as well as real estate assets are not included.

- 3. Good governance:** Companies must have a minimum ESG rating of BB to ensure good corporate governance.

If an investment fulfils all three criteria, it can be rated as a sustainable investment according to its share of the fund's assets.

The aforementioned revenue limits, norm-based violations / controversies, the consideration of PAIs, ESG ratings as well as the SDG alignment are analysed and checked with data of our external research provider MSCI. Companies for which MSCI has not previously provided analysis are reviewed internally. Information provided by MSCI is also reviewed internally, as portfolio management usually has direct access to the management of the companies under review and can critically review this information.

Developer of the strategy, users and data used

The strategy / methodology described above was developed by Lupus alpha. The portfolio management team is responsible for security selection in the global convertible bond segment and compliance with ESG criteria. As part of the detailed ESG analysis, external specialised data providers (in particular MSCI) are also used for sustainability research:

<https://www.msci.com/our-solutions/sustainable-investing>

Exemptions & Selling Discipline

In justified and documented individual cases, there may be exceptions to the methodology described above. However, these are to be avoided by the portfolio management.

If there is a change in an investment which means that the criteria / thresholds described above are no longer met in the medium term, the corresponding financial asset will be sold in compliance with legal requirements after the portfolio management has taken notice.

For more information on the topic of sustainability at Lupus alpha, please visit

<https://www.lupusalpha.com/esg/>.

Date	Version	Description
25.10.2021	1.0	Start of versioning
01.08.2022	1.01	Inclusion of PAIs; addition of a footnote ('GMOs'); editorial changes
31.12.2022	1.02	Editorial changes
11.10.2023	1.03	Adding of carbon intensity and possibility of engagement in PAI consideration
12.07.2024	1.04	Inclusion of OECD screening outside the PAI screening; editorial changes
13.05.2024	1.05	<ul style="list-style-type: none"> - Inclusion of the PAB criteria as well as further exclusion criteria - Introduction of a minimum proportion of sustainable investments (51%) - Integration of the positive selection process into the methodology for evaluating sustainable investments - Editorial changes

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