Aegon Asset Management

DEFINING SUSTAINABILITY WITHIN CORPORATE CREDITS

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We believe companies that have products and services aligned with long term sustainability megatrends may provide the dual benefit of generating better returns while contributing to a more sustainable world. Alternatively, companies who choose to ignore sustainability may be more exposed to business model risk, and eventually balance sheet risk, as the inability to obtain more sustainable economies and markets will likely result in increased environmental and social risks for these companies.

Sustainability at a corporate credit level is initially determined by assessing the amount of a company's revenues/assets that are tied to sustainable initiatives. The United Nation's Sustainable Development Goals (SDGs) provide a comprehensive framework for determining sustainability. Since these goals and associated targets are a blueprint for countries and governments to promote prosperity while protecting the planet, they are not always directly applicable for determining the sustainability of a company's products and services.

Given this disconnect between corporates and governments, Aegon Asset Management has defined six sustainability pillars that categorize broad sustainable investment opportunities. There are a multitude of investible areas within the corporate credit universe that are aligned with these pillars and offer an opportunity to create a sustainable fixed income portfolio.

Our process

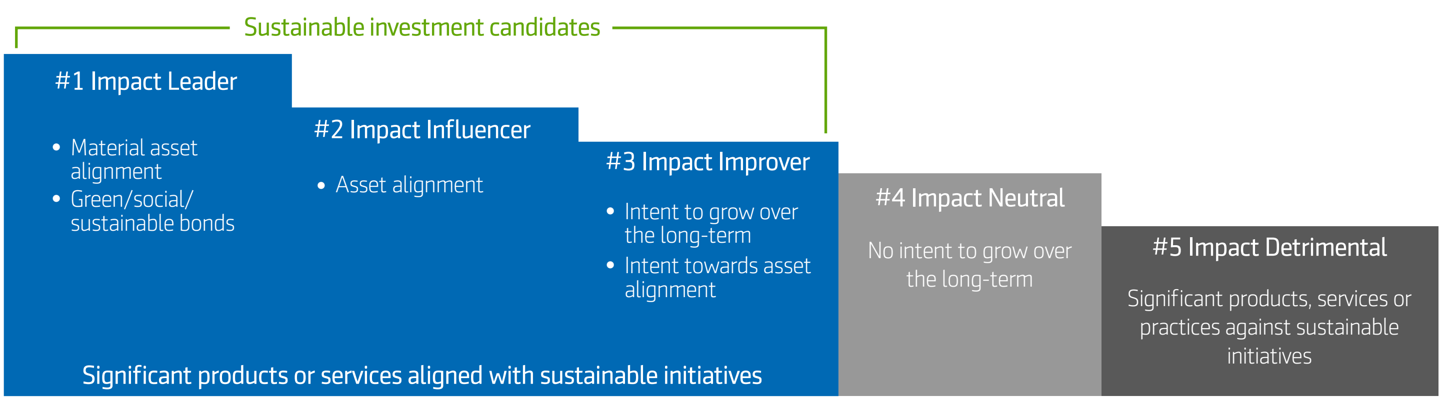
Aegon Asset Management's corporate credit research team utilizes its deep knowledge of the products and services that companies and industries offer to determine the amount of a company's revenues that are aligned with each of the UN SDGs. Through company filings, discussions with management teams, sustainability reports and third party environmental, social and governance (ESG) research providers, analysts assess whether a company's products or services are consistent with our view of sustainability.

In our experience, the answer is not always clear cut. Consider a company that has developed a product that has been instrumental in reducing nitrogen oxide emissions from diesel engines, which aligns with our health & well-being sustainability pillar. However, the company also sources a large portion of revenue from its nitrogen fertilizer business, which has been known to be detrimental to the environment. Namely, the dead zones found in large bodies of water due to the excess application of nitrogen fertilizer and associated runoff as well as the carbon intensive nature of producing and distributing nitrogen fertilizers. While on one hand, this company is reducing nitrogen oxides emissions, their business involvement in nitrogen fertilizer is not consistent with our resource efficiency sustainability pillar. Therefore, the company is not an eligible investment for the sustainable fixed income strategy.

After the initial revenue assessment has been done and any potential misalignment with our sustainability pillars has been evaluated, the credit is presented to the Sustainable Investment Committee (SIC). The SIC is comprised of four individuals with deep expertise in research, responsible investing and portfolio management. This committee provides a final determination of whether the credit will be included in the sustainable investment universe. As part of this discussion, the SIC will also consider qualitative information regarding sustainable business practices. In addition to the inclusion/exclusion decision, the SIC assigns an impact category to each company (Exhibit 1).

Green, social and sustainability bonds are also eligible for the corporate universe in the sustainable fixed income strategy. The green/social/sustainability attributes of the bond are assessed by the SIC to ensure they are consistent with the sustainability pillars of the strategy. In some cases, it may be determined that these elements of the bond are not robust enough for inclusion in the strategy. If these attributes are deemed robust enough, the bond is classified as an impact leader. Even if a company does not meet the SIC's criteria for sustainability, a green/social/sustainability bond issued by it can be included in the sustainable fixed income strategy.

Exhibit 1: Impact category spectrum



Source: Aegon Asset Management US.

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Aegon Asset Management's dedicated responsible investing (RI) team[1] is a valued contributor to the process as it helps the research analysts and SIC make better informed decisions on determining sustainability for corporate credits. In addition, the RI team engages with companies. From a sustainability perspective, engagement allows us to encourage companies to provide better disclosure on their sustainability efforts. We can also urge companies to grow their sustainability efforts by providing financing to them via green, social or sustainability bonds.

[1]Refer to important disclosures at the end of this information regarding the global research platform and responsible investment team.

ESG corporate credit case studies

The following case studies illustrate our credit analysis and how certain qualifiers are accounted for in the process of determining whether a company is suitable to be included in the sustainable fixed income strategy.

Case Study #1 – Impact Leader	
Company description	Global biopharmaceutical company engaged in the discovery, development and commercialization of innovative therapies designed to treat cancer, blood diseases, immune-inflammatory diseases and bone health
Sustainability analysis	The company's products treat various diseases and related issues such as neutropenia, lung cancer, anemia, arthritis, spondylitis and heart failure, which collectively inflict millions of people globally
SDG alignment	UN SDG #3: Good Health & Wellbeing
Sustainability pillar alignment	Health & Wellbeing
Impact category	Impact Leader

Case Study #2 – Impact Influencer	
Company description	A self-administered real estate investment trust (REIT) that develops, manages, leases and acquires suburban office and industrial properties throughout the Southeastern and Midwestern United States
Sustainability analysis	The company's link to sustainability is primarily driven by its green building activities with ~70% of their properties having achieved Energy Star® certifications and 100% of their development projects since 2013 having achieved LEED certification
SDG alignment	UN SDG #11: Sustainable Cities and Communities
Sustainability pillar alignment	Climate Change
Impact category	Impact Influencer

Case Study #3 – Impact Detrimental	
Company description	A producer and distributor of chicken, beef, pork, prepared foods and related allied products whose major customers include grocery retailers and wholesalers, meat distributors and industrial food processing companies
Sustainability analysis	While the company's products primarily represent basic, healthy food, concerns around severe product recalls, water stress, labor unrest, non-traceable place of origin for palm oil and animal welfare issues all point to a lack of focus on sustainability
SDG alignment	Against UN SDG #3: Good Health & Wellbeing, UN SDG #8: Decent Work & Economic Growth, UN SDG #12: Responsible Production & Consumption
Sustainability pillar alignment	Against Climate Change, Resource Efficiency, Health & Wellbeing, Inclusion
Impact category	Impact Detrimental: Significant Products, services or practices against sustainable initiatives

Related literature

The Secular Sustainability Shift
Enhancing ESG Integration: The Value of an Independent Research Assessment
Three Reasons to Invest Responsibly
Electric Power Sector to Drive Success of Electric Vehicles
Global Emissions Standards Driving Hybrid and Electric Vehicle Growth
A Solution to the Plastic Problem Presents Risks to the Chemical Industry
How we Incorporate ESG

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