



BEST PRACTICES FOR RESPONSIBLE INVESTING

Portfolio management, research, ownership
and collaboration

May 2018

ABSTRACT

In the coming years, Responsible Investing will be routine. Understanding how Environment, Social and Governance (ESG) factors impact security prices and portfolio structure will be integrated across the entire industry. Russell Investments has embraced this and has developed – and continues to develop – best practices for our process, portfolios and clients.

From policy and beliefs to practice — a summary

Russell Investments' responsible investing practices incorporate decisions from across the business and are drawn from our beliefs and policy.

Policy	Russell Investments' policy is to incorporate responsible investing in our investment manager evaluation process, our portfolio management, our advisory services, and through implementing proprietary solutions as desired by clients.			
Beliefs	ESG factors impact security prices. These factors can vary by company, industry, and region through time.	A deep understanding of how ESG factors impact security prices is value-adding to a skillful investment process.	Embedding ESG into a firm's culture and processes improves the likelihood of prolonged and successful investing.	Active ownership of securities is an effective tool for improving investment outcomes.
Practices	Portfolio management Manager ranks: on our sub-advisers on ESG integration Surveys: sub-advisers to get a pulse on the market Manager selection: our portfolio managers select products with knowledge ESG ranks and metrics	ESG Research & metrics Products: ESG products and product enhancements Research: research metrics & universes Reporting: report our sub-advisor ranks and all relevant metrics for listed assets (including bonds)	Culture & processes Corporate ESG: global teams integrate ESG across organisation Sustainable work practices: keep our internal practices in check Diversity and inclusion (D&I): support associates across the globe	Active ownership Proxy voting: vote proxies and incorporate ESG into our policy Engagement: join other shareholders to influence the companies we own Sustainable development goals (SDG): considering SDGs as part of our active ownership practices

Source: Russell Investments, April 2018

Belief 1: ESG factors impact security prices. These factors can vary by company, industry, and region and their importance can vary through time.

Belief 2: A deep understanding of how ESG factors impact security prices is value-adding to a skillful investment process.

These two beliefs are the foundation of our responsible investing practice. We incorporate ESG awareness into our active manager evaluation and have developed proprietary metrics for our direct investing capabilities. This includes our **Decarbonisation 2.0** technology and reporting.

ESG ranks — a qualitative assessment of our managers

In 2014 we added an assessment of ESG integration into our manager evaluation process. Through a combination of interviews, surveys and a quantitative review of their portfolios, Russell Investments' analysts rank managers on their ESG integration. Note that we believe ESG awareness and integration is not about restricting securities, targeting ESG or climate-related metrics of any sort, or even intentionally investing in securities with better environment, social or governance practices. But rather, such awareness and integration is about understanding how E, S and G impact a firm, and will impact the future direction of a security's price.

Ranking active managers on their ESG integration



The manager demonstrates **strong awareness** of the potential risk and return of ESG issues on individual holdings and the portfolio structure.

The manager can **clearly demonstrate** how portfolio positioning reflects the management of relevant ESG risks and/or how ESG exposures can add value.

The breadth of perspective and analytical **inputs on ESG issues** are superior to peers.

The manager demonstrates **adequate awareness** of the potential risk and return impacts of ESG issues on individual holdings and the portfolio structure.

The manager's perspective and **analytical inputs on ESG issues** is **undifferentiated** from peers.

The manager **does not demonstrate awareness** of the potential risk and return impacts of ESG issues on individual holdings/ portfolio structure.

Meaningful discrepancies have been found between the target ESG guidelines and holdings in the portfolio.

The manager's perspective and analytical **inputs on the ESG issues** lack rigor.

ESG metrics — a material score for companies

Russell Investments has developed and introduced a new metric for companies called the **Material ESG score**. We have mapped the characteristics identified by SASB as 'material' to firm profitability alongside Sustainalytics disaggregated data. With this more targeted collection of underlying data, we then apply an industry-specific weighting scheme to roll the data up into ESG scores. As our ESG integration is refined, we expect these Material ESG scores to become more typical in our reporting, products and analysis — possibly replacing the standard ESG scores currently used.

Belief 3: Embedding ESG considerations into a firm's culture and processes improves the likelihood of prolonged and successful investing.

As a part of Belief 3, firms' organisational dynamics, cultural values and actions are assessed. A diversity and inclusion disaggregated rank is also included as part of our manager assessment.

We believe that firms who do the following are more likely to achieve prolonged investment success:

- » Attract and retain the right people
- » Offer a supportive environment for their investment teams
- » Provide fair remunerations and incentives
- » Bestow a level of autonomy to make good investment decisions
- » Deliver adequate resources to do a good job

Consistent with Belief 3 is also our own active role in sustainability and responsible investing. We do this through industry memberships with organisations such as the **Principles for Responsible Investments (PRI)** and the Institutional Investors Group on Climate Change (IIGCC).

Belief 4: Active ownership of securities is an effective tool for improving investment outcomes.

Russell Investments actively works to increase shareholder value as we support and foster positive change – whether that's through the proxy voting process, engaging directly with companies or collaborating with industry leaders.

Proxy voting

Russell Investments has built a robust proxy voting and governance process over the last 30 years. The Proxy Committee and Proxy Voting Guideline Subcommittee meet regularly to ensure that our Proxy Voting Guidelines are aligned with current best practices. The professionals who make up these committees not only stay on top of current issues and topics that are important to investors today, but work to analyse the risk and reward merits of these topics.

Proxy voting statistics 2017



Figures are as at 31 December 2017

Engagement

Being an engaged shareholder is another important component of Russell Investments' active ownership responsibilities. This includes engaging with the investment managers that sub-advise our portfolios, as well as engaging directly with management teams of companies we own.

As part of becoming a PRI signatory, Russell Investments has built a more explicit and organised engagement effort. For example, we directly engage with companies on a host of topics via our Corporate Engagement Committee. We are also actively considering how to incorporate the United Nations Sustainable Development Goals into our engagement practices. To this end, we have defined our specific engagement focus areas for 2018 as: Compensation, Accountability, Diversity, Sustainability and Shareholder Outreach.

Best practices for responsible investing – looking forward

As we further develop our approach to responsible investing, we endeavor to lead the investment community in integrating investing best practices with responsible investing best practices. Ultimately, we expect these two to be one and the same.

FOR MORE INFORMATION

Call Russell Investments on **+64 09 357 6633** or visit russellinvestments.co.nz

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