Responsible Investment Policy

Invesco Environmental Climate Opportunities Bond Fund

October 2021

Executive Summary

Contents

02 Executive Summary
- The climate objective

04 Five stage investment process
- Macroeconomic assessment
- Identify issuers with strong climate characteristics
- Credit analysis
- Portfolio construction and risk management
- Carbon monitoring and Invesco's ESG Team oversight

13 Environmental, Social and Governance (ESG) integration in the general investment process
- Common principles
- Resources
- Engagement

The Invesco Environmental Climate Opportunities Bond Fund (the Fund) is an actively managed fixed income fund that invests in corporate and government bonds from issuers globally. The Fund has both a financial and a non-financial objective; these are: i) to provide income and growth; and ii) to support the transition to a low carbon economy.

In order to achieve these two objectives, the investment team employs a five-stage investment process which incorporates a traditional financial and credit research-based methodology alongside a climate-based framework to select corporate and government bond issuers.

The traditional financial and credit research process emphasises active fund management based on in-depth macroeconomic and credit research.

The climate-based framework combines sector exclusions, sector-specific parameters and the selection of issuers with stronger climate characteristics compared to their sector peers. 'Climate characteristics' means a range of data which reveals how carbon intensive companies are, how quickly they are decarbonising and other factors such as management's approach to climate risk in their business planing. The Fund seeks to achieve its objective of supporting the transition to a low carbon economy through investing in bonds of issuer's who meet one or more of the following five key criteria:

- Companies that have a low carbon footprint, or are making significant progress in reducing their carbon footprint
- Companies that have carbon reducing projects financed via green bonds, transition bonds and sustainability-linked bonds
- Green companies (those directly involved with activities that result in a low carbon economy which do not issue green bonds)
- Companies that have made commitments, and are, or are expected to be, on a Net Zero pathway
- Governments that have demonstrated strong environmental and social credentials

The Fund strategically invests across the fixed interest credit risk spectrum depending on investment opportunities.

The Fund is actively managed and is measured against the 75% ICE BofA Global Corporate Bond Index (USD Hedged) and 25% ICE BofA Global High Yield Index (USD Hedged) for performance purposes.

The climate objective: Transition to a Low Carbon Economy

Climate change represents one of the greatest risks and challenges to humankind over the coming decades.

The science of climate change is complex and nuanced. However, there is now an overwhelming weight of scientific evidence to support the view that not only is the world heating at an ever quicker pace, but also that human-generated emissions are primarily responsible for this heating.

A key breakthrough in the politics of climate change occurred in 2015 when the world's governments accepted the findings of the International Panel on Climate Change (IPCC) which stated that in order to avoid potentially severe consequences of climate change, humankind had to limit the increases in temperature to below 2 degrees. Most of the world's governments have ratified the Paris Agreement on Climate Change which commits them to setting national targets and producing policies designed to reduce carbon emissions.

The limiting of temperature rises represents a huge undertaking. To meet the objective set out by the IPCC, the world will have to undergo a decarbonisation of economic and social activity on an unprecedented scale.

The financing requirements for this process are huge. The IPCC estimates that annual investments in clean energy and energy efficiency would have to increase by a factor of 6 by 2050 compared with 2015 levels to limit warming to 1.5 degrees.[1]

We believe that the fund management industry has an important role to play in supporting this objective through a combination of engagement with issuers, advocacy and the channelling of capital away from carbon intensive activities towards green energy and low carbon goods and services.

The Invesco Environmental Climate Opportunities Bond Fund is part of that effort.

It is important to stress that whilst the fund will invest in companies that have made a Net Zero commitment, it will not be restricted to this specific criteria. The Fund will also invest in companies that demonstrate strong climate characteristics relative to their peers, green and sustainability-linked bonds and companies producing goods and services that directly contribute to decarbonisation.

The Fund will support the transition to a low carbon economy by funding companies in high carbon emitting sectors that show progress towards lowering their carbon footprint as well as low carbon sectors. We believe funding such companies is an effective way of influencing such trends rather than simply excluding the sectors from the portfolio.

1 Financing the Low-Carbon Future, Climate Finance Leadership Initiative, September 2019.

Five stage investment process

The investment team employs a five-stage investment process, combining a traditional investment research alongside a climate focused selection process.

1	**Macroeconomic assessment**	• Top down macroeconomic assessment, conducted by the team's economist macro specialists • Fund managers develop their views on the general direction of yields and credit spreads
2	**Identify issuers with strong climate characteristics**	• Non-sustainable exclusions applied • 'Climate Comparator' output • Fundamental climate analysis
3	**Credit analysis**	• Bottom up credit research conducted by the team's 11 dedicated corporate credit analysts • Absolute and relative value analysis incorporated • Green bond assessment
4	**Portfolio construction and risk management**	• Fund manager responsibility – not tied to an index • Risk continuously managed according to market conditions • Strong risk monitoring infrastructure
5	**Climate monitoring and ESG team oversight**	• Portfolio measured and compared against the Climate Comparator using a range of indicators • Periodic reviews with Invesco's ESG team

In the Macroeconomic assessment stage, 'credit spread' refers to the extra yield earned from a corporate bond, over a government bond of the same maturity.

Stage 1: Macroeconomic assessment

The starting point for the investment team's work is an appreciation of the key macroeconomic inputs that influence government and corporate bond markets.

There is no 'house view' to which the team must adhere and the fund managers form their own opinions about key macroeconomic trends as they remain ultimately responsible for the Fund's risk profile and performance.

Specifically, the aim of the team's macroeconomic work is for the team's fund managers to develop a view of the general direction and structure of interest rates and future trends in the general pricing of credit risk, rather than make point estimates of specific economic variables. To a large extent these broader views help influence the fund managers' overall appetite for credit and interest rate risk.

To assist the fund managers, the team has a dedicated economist and several macroeconomic analysts who produce and share research and facilitate team discussions. Team members assess a range of primary data sources, as well as engaging with independent economic research providers and investment bank economists. The team also benefits from the research produced by Invesco's Group Chief Economist's department.

High frequency economic and survey data are assessed continuously either informally or more formally at the team's daily morning meetings. In addition, more in-depth economic research is produced and discussed at dedicated meetings or more formally at the monthly investment department meeting or the fixed income team's asset allocation group meeting.

Five stage investment process

Stage 2: Identify issuers with strong climate characteristics

The identification of companies with strong climate characteristics is what gives this strategy its unique characteristic. The team considers those companies and governments that are leading the way towards a low carbon world through a combination of public policies and strategies designed to encourage or compel decarbonising activities, or by providing low carbon energy, goods and services.

1. Exclusions

The Fund's ethos results in certain minimum standards both in terms of climate and general sustainable activities. Therefore, the first step is to screen the universe of global corporate bonds based on the exclusions outlined below.

Climate-based exclusions	Revenue thresholds for exclusion[2]
Thermal coal extraction	>=5% of revenue
Arctic oil & gas exploitation, oil sands extraction, shale energy extraction	Each >=5% of revenue
Oil & gas exploration, production, refining, transportation and/or storage[3]	>=25% of revenue
Non-climate-based exclusions	
Controversial weapons	>=0% of revenue
Tobacco – products production Tobacco related products and services	>=5% of revenue >=5% of revenue
U.N. Global Compact Status	Companies not compliant with the Ten Principles of the UN Global Compact Initiative
The manufacturer and sale of nuclear weapons to countries that have not signed the Nuclear Non-Proliferation Treaty	>=0% of revenue
Recreational cannabis	>=5% of revenue

The climate-based exclusions have been applied with reference to each fossil fuel's climate warming potential, set against the practical reliance that we still have on fossil fuels in the medium term.

Fossil fuel type	Kg CO_2 emitted per million British thermal units (Btu)
Coal	93-103 depending on variety
Diesel	73
Gasoline	71
Propane Gas	63
Natural Gas	53

We believe that supporting the transition to a low carbon economy necessitates the almost total exclusion of thermal coal. Thermal coal is not only the most polluting of fossil fuels, but in addition, the global economy in aggregate is no longer dependent on it as other forms of energy have become more prevalent.

The revenue threshold for thermal coal is set at 5% rather than 0% to allow companies with very modest legacy coal assets to be eligible. For example, a number of mining and steel companies have legacy thermal coal operations but play an important role in climate transition through the supply of raw materials required for electrification. As a result, their inclusion in the Fund is supportive of the transition objective. Furthermore, the Fund has no restrictions on coking coal which is used for steel production.

The oil and gas sector is more nuanced. On the one hand, oil and gas represent the overwhelming majority of CO_2 emissions. According to the US Energy Information Administration, in 2018 fossil fuel combustion was responsible for 93% of all anthropogenic CO_2 emissions in the US. However, both are cleaner fuels than coal (natural gas produces 43% less CO_2) and both are deeply embedded in the global energy supply chain. For example, oil and gas still accounts for 75% of the UK's primary energy (power, transport and heating). The team believes that in the medium term, gas in particular is a vital and relatively clean component of global energy supplies.

2 Companies which derive more than this level of revenue from the activities listed above will be excluded from the Fund.

3 The Fund is permitted to buy green bonds, subject to an analysis of their suitability, from companies whose revenues from oil and gas are greater than 25% and whose revenues from unconventional oil and gas exploration are greater than 5%.

Five stage investment process

Nonetheless, we acknowledge that it would be inappropriate for a climate fund to have no restrictions on funding the major sources of CO_2 emissions and as a result, we place a 25% revenue threshold for mainstream oil and gas production. This rule effectively excludes companies whose core activities are oil and gas related. The reason for permitting up to 25% of revenue from oil and gas operations, rather than a complete exclusion, is because whilst we don't wish to finance major sources of carbon emissions, we think we should be able to finance diversified energy companies and support their efforts to increase clean energy production.

We also recognise that whilst oil and gas companies are major sources of emissions, there are increasing efforts amongst many of these companies to diversify into renewable energy. Critically, many of the global oil and gas energy groups have the financial and technical resources necessary to make that shift. As a result, the Fund also permits investment in companies whose revenues from oil and gas activities are greater than 25% in cases where it can finance specific green energy projects via green bonds.

Another important sector in a climate context is utilities, given the extent of emissions created during power generation. Here, rather than the Fund adopting specific exclusions based on thermal coal, we analyse the amount of CO_2 emissions per unit of energy generated, ensuring that only the least carbon intensive generators are selected.

The issue of nuclear energy is also sensitive. On the one hand, nuclear energy remains controversial with the challenge of waste and the environmental risk that it poses a genuine concern. Yet we recognise that nuclear power also provides consistent, reliable, and importantly for a climate-oriented fund, zero-carbon energy. As a result, we believe that permitting nuclear power is on balance appropriate for a sustainable product of this type.

The Fund also adopts a number of baseline exclusions (shown in the table above as "Non-climate based exclusions") determined by Invesco, based in part on its assessment of the market's expectation of what constitutes unsustainable activities.

The exclusion filter uses Sustainalytics data on company revenues attributed to particular activities such as tobacco or thermal coal which is then fed into Invesco's pre-trade compliance system.

To ensure a minimum standard of governance amongst investee companies, the Fund will avoid investing in those that have a governance score of 5 as measured by our proprietary ESG scoring tool, which scores companies 1-5 (with 1 being the best) against 18 governance-specific indicators.

The Fund is also permitted to have up to 30% of its assets (such as cash) and long exposure to derivatives (such as index CDS), which do not conform to the climate methodology.

The next step is to identify companies that are performing well versus their peers from a carbon perspective and therefore could be suitable potential investments for the Fund.

2. Investment selection process: Climate Comparator

To help in this assessment, the team uses an Invesco-developed proprietary sector-based Climate Comparator which incorporates data from over 2,000 corporate bond issuers, incorporating a wide range of climate and specifically carbon-oriented indicators.

Examples of indicators include the percentage change in a company's carbon emissions, different measures of carbon intensity, the percentage change in a company's intensity and measures of carbon emissions relative to an output such as power.

Each company's performance in each indicator is converted to a sector-relative 1-5 score (1 being the best). The indicator scores are then summed to produce an overall sector-based 1-5 rating. In cases where data is missing, those indicators are excluded from a company's overall score.

The weights applied to each indicator are determined by its importance based on the team's judgement. The weights of each indicator can also be tailored to individual sectors. For example, the CO_2 / kwh indicator is given a 60% weighting for the electric utility sector but is not included in other sectors.

Below is an example of how an electric utility company is scored based on the indicators that are applied to that sector. This company scores particularly well on its low use of thermal coal and its assessment by the Transition Pathway Initiative, a climate-focused organisation that assesses companies on the basis of their carbon intensity and management's approach to dealing with climate change.

Five stage investment process

Electric utility sector indicators	Weighting	Data	Score
CO_2mt per MWH	60%	0.32mt	2
CDP Grade[4]	15%	A-	2
Transition Pathway Initiative Assessment[5]	15%	4	1
MSCI Low Carbon Transition Management Score[6]	10%	6.60	1
Overall score			**1.8**

The Fund will typically invest in companies which have better scores than their peers. Although the Fund is permitted to invest in lower scoring companies, the fund managers must justify their inclusion in the portfolio.

In instances in which the investment team judges that the quality of the data for certain indicators in specific industries is poor, those indicators can be excluded. A good example of this is banks' scope 3 emissions. In this case, banks' efforts to calculate their funded emissions are in their nascency and comparative data is not yet available. Instead, the focus is on banks' willingness to engage with industry initiatives, a qualitative assessment of their policies towards funding emissions intensive sectors and other qualitative assessments.

Considerations of a Climate Comparator – Data limitations and our input

It is important to recognise where a quantitative approach has limitations. These include both limitations with each individual metric, the lack of data and in some instances, data which may be misleading.

For example, a company's absolute emissions may be affected by corporate actions, or by its general operational performance rather than efforts to reduce emissions. The extent to which a company owns its supply chain (upstream raw material sourcing and downstream distribution) can significantly affect how a company calculates its emissions. The quantitative approach also struggles to judge diverse sectors or diversified companies. It is also has a tendency to look backwards and miss companies about to undergo change. Private companies are a feature of fixed income markets, a group of companies where data is often sparse.

Therefore, whilst the output of the Climate Comparator is a vital component, it is not the sole determinant of which companies qualify for the universe of potential investment candidates. When identifying companies with strong climate characteristics, understanding and contextualising data is critical and as a result, the team uses a combination of research resources including the team's credit analysts, its dedicated ESG research analyst and Invesco's 13 strong Global ESG Team which consists of specialist research analysts.

We permit investment in companies which are not in the Climate Comparator in instances that we can justify, either because we have sufficient climate-related data on the company from other sources, or where a company's core activity is supporting transition.

Nonetheless, we believe there are numerous advantages of using a Climate Comparator approach to analyse companies in a systematic and thorough way. It is an efficient way of identifying the broad trends in a sector, it can help us understand which companies are leading and lagging in the drive towards decarbonisation, and identify those companies whose record is mixed and may warrant further investigation. The Climate Comparator will evolve to accommodate advances in data reporting and also facilitates the comparison between the Fund and the benchmark.

In addition, at the portfolio level, the Fund is expected to achieve a lower (better) Climate Comparator score than the Fund's benchmark by a minimum of 10% although this is not a fund target or a constraint and the Fund is actively managed.

3. Fundamental Research: Invesco's ESG team

In addition to the Climate Comparator, the investment team also benefits from the fundamental research capability of not only the team's credit analysts but also Invesco's Global ESG team.

Invesco's Global ESG team consists of 13 specialists (as at 14 October 2021), who conduct fundamental research
in co-ordination with Invesco's investment teams. Fundamental climate and carbon research is directed towards those issuers for which the investment team judge that further investigation is warranted, for example where data is sparse, or inconclusive, or where the investment team believe that the historic data does not properly capture the investment opportunity to support future carbon reduction.

Research involves an assessment and contextualisation of the carbon data, understanding an issuer's carbon reduction strategy, their objectives and success to date. The views of the ESG team analysts and investment analyst are then considered by the fund managers

4 CDP rates companies based on their environmental disclosure and environmental risk management.
5 Transition Pathway Initiative Assessment assesses companies' preparedness and management of climate risk as well as their carbon performance.
6 MSCI proprietary measure of how well a company manages risk and opportunities related to the Low Carbon Transition.

Five stage investment process

who are able to make an informed judgement about the appropriateness of a security.

4. Green, sustainability-linked, and transition bonds

The Fund will also invest in a range of green bonds where an investment opportunity is identified and, given the rapid growth and development of this market, there is no upper limit to how many green bonds will be held in the Fund.

Supply of green bonds has grown rapidly in recent years as issuers have sought to benefit from the rise in demand from socially responsible investors. A key challenge in the development of the green bond market has been to develop common standards as to what constitutes a green bond. To counteract the threat of greenwashing, the use of external reviews of green bonds has become widespread. External reviews can take the form of second party opinions, verifications and ratings. These reviews confirm (or otherwise) alignment with green bond principles and verify that the use of proceeds conforms to standards as set out in the Green Bond Principles.

The development of the market was boosted by the introduction of Green Bond Principles from the International Capital Markets Association (ICMA) in 2014 and the Climate Bond Initiative Standards and Certification Scheme which set out to provide a framework in which green financing could develop.

The investment team assesses green bonds to ensure they meet acceptable standards. To do this, the team follows the International Capital Markets Association criteria.

Bonds are scored on four criteria: the use of proceeds, management of proceeds, reporting, and external verification.

A green bond can score 1 – 10 and the investment team will invest in green bonds that score 4 or more.

	Score	Definition
Use of proceeds	0 – 4	Are qualifying projects clearly identified? Is refinancing permitted, if so for how long? Is there committee oversight?
Management of proceeds	0 – 2	Are proceeds held in a separate account? Is there a timeline for distribution of proceeds?
Reporting score	0 – 3	Is there regular reporting on the project? Is the report published? Is the project audited?
External verification	0 – 1	Is the bond verified by an external party?
Total	**/10**	

5. Net zero emissions alignment

The Fund will also invest in bonds issued by companies that have made net zero pledges.

The Carbon Trust, a well known authority on climate change, defines 'net zero' as 'achieving a state in which the activities within the value-chain of an organisation result in no net impact on the climate from greenhouse gas emissions.'

Companies and governments often set 2050 as their 'net zero' goal to align with the IPC's own global goal of carbon neutrality. However, with such a long time frame it is important that issuers set out a clear roadmap with interim targets.

In this regard, Science Based Targets (SBT, a leading climate-focused not for profit organisation that works with companies who are reducing their carbon emissions) is at the forefront of defining how companies can achieve net zero status.

SBT states that there are three key elements to the definition of a net zero emissions company:

1. The company will set and pursue an ambitious 1.5°C aligned science-based target for its full value chain emissions
2. The boundary must be global scopes 1, 2 and 3 for the organisation
3. Any remaining hard-to-decarbonise emissions can be compensated with certified greenhouse gas removals (GGR). These should be restricted to only certified methods of GGR, to increase confidence that the carbon is permanently sequestered. Importantly, the company or organisation should make sure that only truly 'hard-to-decarbonise' emissions may be compensated.

Five stage investment process

Net zero also differs from 'carbon neutrality' in a number of ways. The Carbon Trust states:

1. Whereas the boundary of a net zero target includes global scope 1, 2 and 3 emissions of the organisation, carbon neutrality for an organisation only requires scope 1 and 2, with scope 3 emissions encouraged but not mandatory.
2. The boundary of a carbon neutral claim can refer to a specific product or service instead of encompassing the whole organisation in the case of net zero.
3. The reduction in reported emissions required differs. Net zero targets must align to a 1.5°C science-based target, whereas the level of ambition of a carbon management plan for carbon neutrality is not specified.
4. The approach to residual emissions differs, with specific greenhouse gas removals required for net zero targets, whereas carbon offsets are accepted for carbon neutrality.

At this stage, the number of companies making a pledge to achieve net zero status is small but growing.

The Fund has not set a minimum level of exposure to net zero issuers as its process is already designed to seek out those companies with strong climate characteristics, some of which are likely to be aligned to the temperature reduction goals even without making a formal commitment. However, it is likely that through the Fund's climate objective and the increasing number of companies making net zero commitments, the Fund's exposure to net zero aligned companies will grow over time.

6. Climate risk assessment for government debt

The Fund can invest in both developed market and emerging market sovereign debt as part of its investment strategy and the team also applies a quantitative and qualitative assessment to determine the most appropriate issuers from a climate perspective.

The starting point is Invesco's ESG quantitative tool, ESGIntel, which scores sovereign issuers on 23 indicators, of which 7 are environmental (including 3 focused on climate change), 8 social and 8 governance-focused. These indicators assess governments on a range of topics including carbon emissions, air quality, life expectancy, education and health.

Data is sourced from a number of intergovernmental organisations such as the UN and World Bank as well as specialists such as the International Energy Agency. Governments are scored relative to 5 separate groups: overall, IMF REO regions, (Europe, Asia, Middle East and Central Asia etc), IMF Economy (advanced, low income emerging market etc), Developed/Emerging Market and GDP cohort.

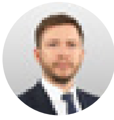
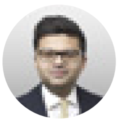
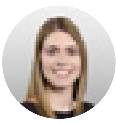
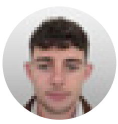
Data is converted to a scale (1-5 with 1 the best) and quintiled.

The team assesses the government scores. The Fund will not invest in governments scoring 4 and 5.

Five stage investment process

Stage 3: Credit analysis

Once an issuer has been judged as being suitable for inclusion from a carbon perspective, the investment team then assesses individual financial corporate credit risk. The team has 10 credit analysts who are organised by industry on a global basis.

		Years in team	Industry experience	
	**Asad Bhatti** CFA Charterholder	19 years	21 years	Emerging Markets
	**Rhys Davies** CFA Charterholder	18 years	19 years	Autos, Gaming, Rental, Distressed
	**Julien Eberhardt** CFA Charterholder	13 years	16 years	Banks: US, Europe, Japan
	**Edward Craven** Fellowship Chartered Accountant	10 years	18 years	Telecom, Media, Technology, Leisure
	**Tom Hemmant** Associate Chartered Accountant	10 years	19 years	Utilities, Energy, Infrastructure, Paper & Packaging
	**Jessica Svantesson** MA International Business	7 years	15 years	Infrastructure, Transport, Technology, Services, Leisure
	**Thomas Moore** CFA Charterholder	5 years	22 years	Retails, Consumer, Food
	**Samir Patel** CFA Level III Candidate	3 years	15 years	Banks (UK, Ireland, Nordics, Netherlands, Belgium, Spain, Portugal), Insurance
	**Sarah Williams** CFA Charterholder	2 years	7 years	General
	**Ellie Mainwaring** CFA Charterholder	1 year	6 years	General
	**Matt Cottingham**	<1 year	17 years	Chemicals, Metals & Mining, Building Materials, Construction
	**Eoin Strutt**	<1 year	2 years	ESG

Given the investment team's active approach and benchmark agnosticism, there are no predetermined rules that govern which credits analysts review, although given the size of the team's assets under management, smaller issuers are less likely to be attractive. Instead, it is the responsibility of both the fund managers and the credit analysts to generate investment ideas for review which can result from a range of different factors including a change in outlook, a change in price or new bond issues.

Five stage investment process

Although the research approach taken by the team's credit analysts will vary according to circumstance, when assessing a new issuer, the process begins with an understanding of the Offer of Memorandum which states the objectives, risks and terms of a bond issue. This is followed by a review of credit rating agencies reviews (where the issuer is already rated but not yet covered by the analyst) and attendance at a presentation given by the issuing company's management.

Given the size of the team's assets under management, the credit analysts are typically able to secure additional time with the issuer's management if needed.

The team's credit analysis encompasses a range of inputs that are presented in the table below.

Credit ratings	Moody's, S&P, Fitch
Operational	Management, competitive position, business outlook
Balance sheet	Capital structure, leverage, equity, cash, debt mix/maturity
Cashflow	EBITDA, capital expenditure, working capital, interest coverage
Protection	Covenants, asset value, franchise, banks

It is the role of the analyst to understand for each bond which of these considerations are the most important and warrant focus. The emphasis of the analyst's work is on understanding the evolution of credit metrics rather than on the numerical value of the ratios at a point in time. Moreover, the analyst needs to place both the risks of the company and the value of the bond in some context. How does this issuer compare to others in the sector? How much value does the bond offer relative to others from the same or similar issuers?

The credit analysts have the flexibility to work and present their assessment in a way that best suits the circumstances and the team does not employ a template model. Once the research is complete, analysts present their work to the fund managers, providing an informed opinion on which the fund managers can decide the attractiveness of the bond.

Value assessment

Once a deep and informed credit risk opinion has been established about a corporate borrower, absolute and relative risk and value judgements can be made.

The fund managers are ultimately responsible for determining which bond issues are selected for the portfolio. Bonds are not selected with reference to an index, but rather on merit of their value assessment and the balance of risk and reward according to the fund manager's judgement.

The investment team constantly seeks to understand why an investment opportunity may exist, including factors such as:

- The team's different assessment of a company's outlook to that of the market
- Market overreaction to one aspect of a company's situation
- The effects of ratings changes, such as moving between investment grade and non investment grade
- Issuance patterns of the company such as the frequency and size of supply
- Mispricing of covenant protection (investors mis-interpreting particular protections awarded to bondholders or lack thereof)

In keeping with an absolute risk and return mentality, the investment team also considers the risk/return profile of a bond in relation to cash and government bonds. This aspect can be particularly important in periods in which the credit market as a whole can appear attractively or unattractively valued.

An appreciation of relative value enables the investment team to select the best value corporate bonds given pre-determined variables such as maturity, sector and credit rating. This also helps the team to identify credit trends and pricing anomalies.

Five stage investment process

Stage 4: Portfolio construction and risk management

The investment team employs a multi-faceted approach to oversight and risk management with processes bolstered and overseen by several independent controls. It is an integral part of the investment process and is the product of the following factors:

- Fund manager understanding: the fund managers effectively control bond-specific risk by ensuring the portfolio is always appropriately diversified. Continuous analysis of all holdings gives the fund managers a comprehensive understanding of the financial risks associated with any bond.

  The team manages portfolio risk from the perspective of:
  - Market risk
  - Currency exchange risk
  - Investing in assets traded on non-eligible markets
  - Use of financial derivative instruments
  - Counterparty risk
  - Use of warrants
  - Market liquidity risk
  - Interest rate risk
  - Issuer risk
  - ESG and climate risk
- Continuous monitoring: At the portfolio level, monthly performance and risk reports are produced by the Investment Oversight team, ensuring that the fund managers adhere to investment objectives, guidelines and parameters.
- Chief Investment Officer (CIO) Challenge process: Invesco's essential belief is that fund management is a skill and the inherent risks taken in managing investments are those made by the fund managers themselves. Thus, no unnecessary restrictions exist that limit a fund manager's freedom to back his/her own convictions. A periodic meeting is held between the CIO and the individual fund managers which seeks to ensure that the fund managers are managing money in a way that adds value and that the risks taken in respect of the Fund are understood and are considered appropriate. The Investment Oversight team provides reports to facilitate this process.
- In addition to the risk management procedures within the team and the investment centre, risk management is also conducted on an EMEA-wide level by the Operational Risk and Investment Risk Oversight teams.

Stage 5: Carbon monitoring and Invesco's Global ESG Team oversight

The Fund is monitored from a performance perspective and to ensure that it meets its climate objectives.

The Fund's benchmark for performance comparison purposes is a composite index consisting of 75% ICE BofA Global Corporate Bond Index (USD Hedged) and 25% ICE BofA Global High Yield Index (USD Hedged). While the composite benchmark is not consistent with the ESG characteristics of the Fund, it is a suitable proxy for the wider investment and therefore it is likely that the majority of issuers in the Fund are also components of the composite benchmark. As an actively managed fund, this overlap will change and this statement may be updated from time to time. The Investment Manager has broad discretion over portfolio construction and therefore it is expected that over time the risk return characteristics of the Fund may diverge materially to the benchmark.

For some Share classes, the benchmark may not be representative and another version of the benchmark may be used or no benchmark at all where a suitable comparator does not exist. Such details are available in the KIID of the relevant Share class.

The Fund's benchmark for climate comparison (not performance) purposes is the Climate Comparator which consists of companies drawn from the ICE BoAML Global Corporate Index (G0BC) and the ICE BoAML Global High Yield Index (HW0C).

The Fund is expected to achieve a lower (better) score than the Climate Comparator by a minimum of 10% however, this is not a Fund target or a constraint and the Fund is actively managed.

The portfolio is also compared to the Climate Comparator for a range of metrics such as carbon emissions, carbon intensity, as well as a number of sector specific indicators.

The proportion of the Fund in green and sustainability-linked bonds and companies that have made Net Zero commitments will also be calculated.

Invesco's Global ESG team's Oversight
The investment team also benefits from the advice and expertise of Invesco's Global ESG Team which meets periodically to review the portfolio and ensure that it is meeting its climate objectives, discuss upgrades to the Climate Comparator and investment process and co-ordinate on engagement with the management of companies relevant to the Fund.

ESG integration into the general investment process at Invesco Henley Fixed Income

ESG overview

The Henley Fixed Income (HFI) team's investment approach is centred on macroeconomic and corporate credit research and focuses on fundamental valuation to support the active management of portfolios. HFI has always incorporated ESG analysis into its investment research because it believes that non-financial risks can have a material impact on credit risk and by identifying those risks it can improve its credit risk assessment and produce better risk-adjusted returns in portfolios.

The core objective of HFI's ESG approach is to assess issuers' performance across environmental, social and governance factors and to determine where those risks are potentially material or mispriced.

The fixed income universe is broad and varied. Geographical, structural and regulatory differences mean that data availability, ESG awareness and management engagement levels can vary greatly. As a result, while the investment team's commitment to ESG risk assessment is constant, the path to arriving at an ESG-based assessment necessarily differs to account for the constraints and challenges of different circumstances.

Common Principles for ESG Research

The team's approach to ESG is based on a belief that incorporating material environmental, social and governance risks into a broader risk assessment, leads to better long-term risk-adjusted returns. In order to do this, the team considers **materiality** and **momentum**.

- Issuers may have myriad ESG considerations, but **materiality** means focussing on those particular ESG risk factors that have the potential to impact an issuer's credit risk profile.
- **Momentum** means understanding the evolution of ESG risks. As with all risk, we look to identify positive and negative momentum in ESG risks and assess the potential for those trends to affect creditworthiness. As a firm we encourage positive momentum by engaging with companies. We work with Invesco's Global ESG team which engages with the management of companies and provide views on matters such as corporate strategy, transparency, capital allocation and ESG concerns.

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ESG analysis for corporate bonds

HFI's credit analysts are responsible for understanding and assessing ESG risks for the companies under their coverage alongside financial credit risk. Corporate credit research is organised around global industrial sectors, allowing the analysts to develop a comprehensive understanding of not only the ESG risks pertinent to each issuer under their coverage but also those risks prevalent in a sector.

This approach of incorporating ESG risk into the broader assessment is undertaken for all issuers of corporate bonds, for both developed or emerging market countries.

External ESG resources
Invesco has a range of third-party research and data available as an input to support the analysts in their ESG risk assessment.

Examples:

- MSCI E, S & G Scores, industry percentiles and weights
- CDP carbon and scoring data
- Sustainalytics Risk scores and category summary data
- Global Compact compliance or violation fields (MSCI and Sustainalytics)
- ISS Climate Solutions – Scope 1 to 3 emissions and science-based emission targets
- Controversies – MSCI & Sustainalytics data feeds

Invesco's ESG resources
Invesco's 13-strong Global ESG team has resources in research, portfolio analytics and management engagement.

Furthermore, Invesco's own proprietary developed ESG tool provides ESG insights, metrics, data points and momentum scores from over 50 data points and metrics. Sector differences are accommodated with each having its own tailor-made framework.

The tool provides a holistic view on how a company's value chain is impacted in different ways by various ESG metrics, and ratings are produced both at the overall company and indicator levels to facilitate a focus on higher risk company-specific issues. In addition, momentum indicators highlight a company's trajectory using 5 years of data history (longer back data in database).

While disclosure levels vary greatly by the company due to sector, size and regional factors, these data dashboards can provide a comprehensive picture of each issuer's performance.

The importance of fundamental ESG analysis
At the issuer level, data availability, disclosure rules and management engagement levels can vary across each global sector. Raw ESG data can sometimes present a partial or even misleading picture. When placed alongside the fact that issuers themselves have unique features in terms of business models, the weighting of ESG factors in each issuer assessment must be interpreted and understood in a broader context.

In our research process, the qualitative judgment of the credit analyst is therefore central to determining whether an ESG factor is evolving in a manner that may compromise an issuer's financial indicators and ultimately, its creditworthiness.

ESG in credit selection

Once a credit analyst has undertaken their credit assessment, including that of the materiality and momentum of ESG risks, then credit research is presented to fund managers.

The fund managers need to assess the type and materiality of any ESG risk and set that against the potential investment return in the context of the Fund's objectives.

Other than the exclusions for the Invesco Environmental Climate Opportunities Bond Fund, there are no pre-determined rules on how securities are selected in light of any ESG risks. Each investment case is likely to have its own unique set of risks. The investment team's credit selection emphasises fund manager judgement and each case is considered on its own merits. The ESG risks being considered will not be those relating to an issuer's negative impact on climate change as, in particular, polluting companies would have already been screened out.

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ESG portfolio monitoring

Dedicated ESG-focused portfolio reviews are in place to complement the existing risk-return portfolio review process. Invesco's Global ESG team leads each review meeting which is attended by HFI fund managers and credit research analysts.

The review meetings cover portfolios with ESG objectives such as the Invesco Environmental Climate Opportunities Bond Fund and portfolios without explicit ESG objectives. Portfolios are reviewed on the basis of a wide range of ESG metrics on an absolute basis and also relative to benchmarks where appropriate.

Engagement with issuers
Invesco engages directly with companies to better understand their positions and their future intentions and lobby for change where Invesco believe it is necessary. Although engagement as pure debt investors can be challenging, Invesco's ownership of both equity and debt can often be used to increase our voice as a stakeholder. Engagement is carried out on a case by case basis by relevant analysts and strategically with co-ordination through Invesco's Global ESG team.

Investment teams at Invesco are supported on many ESG engagement activities by a centralised team of ESG professionals. Invesco's Global ESG team is led by the Global Head of ESG. Reporting to the Global Head of ESG is the Director of ESG Research, who leads the ESG analyst team who focus on this ESG company engagement activity.

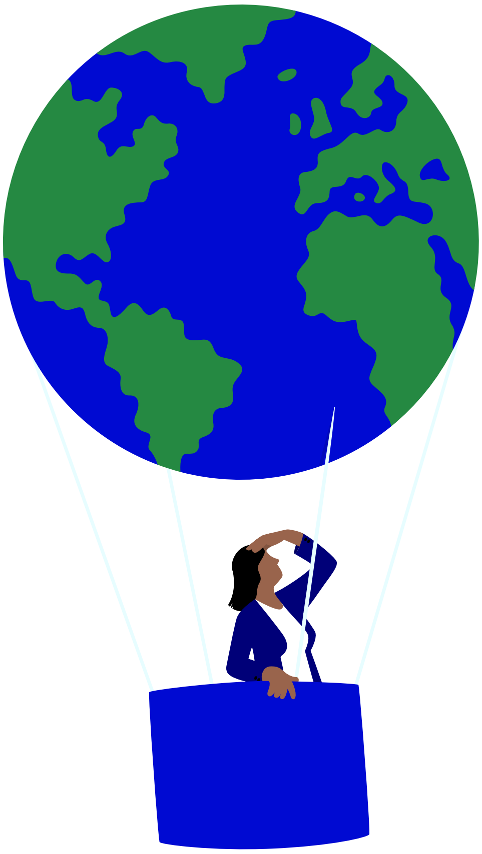
Invesco has established a global process to ensure that our ESG-targeted engagements are a collaboration between the ESG team and the investment teams across Invesco who may have interest in the issuer:

i. **Internal assessment and coordination**
The ESG team consults with the investment teams and reviews the ESG Engagement focus list and decides whether to: (a) gather feedback on a topic and provide that feedback to an issuer, (b) schedule a call with the issuer if it is deemed to be necessary; or (c) engage directly with the issuer and serve as a liaison. Invesco's ESG team will arrange contact between the relevant investment teams and issuers when and if it is deemed necessary. Any ESG engagement meeting is added to a centralised calendar that investment teams can access.

ii. **Research and follow up**
The ESG research team conducts in-depth ESG research in preparation for these meetings and discusses with the relevant investment teams across Invesco to ensure that companies are questioned on the key ESG topics. The ESG team produces an Engagement Report for these meetings which is shared via the Bloomberg platform for all relevant investment teams to access.

Invesco is also a member of several organisations that facilitate collective dialogue with companies and continues to assess other collective engagements that we would like to work more closely with in the future:

- Invesco is a signatory to Climate Action 100+ and is taking a leading investor role on one company and a participative role on at least 6 other companies.
- Invesco joined the Investor Tailings Initiative when it was first launched in 2019. Invesco signed letters that were sent to over 600 companies and actively participated in meetings with companies and governments to ensure the development of higher standards and to evolve the tools to assess companies.
- Invesco signed the Investor statement on Covid-19, to encourage the business community to take what steps they can to mitigate the social impacts caused by the pandemic. Some of these steps include providing paid leave, prioritizing health and safety, maintaining employment and maintaining supplier relationships. Invesco has engaged with companies on these topics as part of its ongoing one-to-one ESG engagements.



Fund Facts

Invesco Environmental Climate Opportunities Bond Fund

Investment Centre	Invesco Asset Management - Henley Fixed Income
Fund Manager	Mike Matthews Tom Hemmant
Contracted Vehicle Type	SICAV
Domicile Country	Luxembourg
Launch Date	10 March 1992
Fund volume	USD 77.7 m

Source: Invesco as at 14 October 2021.