

# Responsible Investment Policy

**Invesco Quantitative Strategies**

Invesco Sustainable US Structured Equity Fund

October 2021



# Executive Summary

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The Invesco Sustainable US Structured Equity Fund (the fund) follows an ESG integrated multi-factor Low Volatility strategy. While strict ESG filters are applied, the investment team aims at earning factor premiums, using their proven multi-factor investment approach which considers Momentum, Quality and Value. Furthermore, the team's low volatility optimization targets to achieve reduced volatility compared to a market cap weighted benchmark, the S&P 500. The fund invests in US listed equities. The consideration of sustainability criteria is an integral part of every step of our investment process.

The investment process of the fund is based on three building blocks: ESG Policy, Security Selection and Proxy Voting and Engagement.

01

## ESG Approach

- Using integrated ESG screening combined with additional ESG criteria.
- Implement ESG criteria using the V.E (Vigeo Eiris) data.

02

## Security Selection

- Multi-factor low volatility selection process focused on equities using a proprietary multi-factor investment approach which exploits premiums using proprietary factor definitions for Momentum, Quality and Value.

03

## Proxy Voting & Engagement

- Voting in line with a dedicated proxy voting policy promoting ESG themes.
- Entering into an active dialogue with companies that have weaknesses in the field of ESG.

## Combination of appealing characteristics

- Implementing holistic **ESG criteria** in investment process
- Extra return potential from **Multi-Factor Model**
- **Low volatility objective** for more stable return pattern
- Achieving **measurable improvement** of ESG characteristics



# Holistic ESG consideration in the investment process

The Invesco Quantitative Strategies (IQS) team applies an integrated ESG (environmental, social, governance) investment approach and has been managing customised sustainable investment solutions for more than 20 years. With many years of experience, the team offers different approaches to integrate ESG criteria into the portfolio at different stages of the investment process across all asset classes.

The investment team follows an integrated ESG approach. The team takes ESG factors into account at several levels of their management process:

- Explicit and implicit consideration of key ESG aspects in the multi-factor optimization process
- Active dialogue with companies through engagement programs and investor-oriented proxy voting with Invesco's proprietary proxy voting platform
- Offering optionality to implement additional, customized ESG criteria

## Holistic ESG consideration in our investment process

### Integrating key aspects of ESG

We **consider ESG at several layers** in our investment process:

- Standardized explicit and implicit incorporation of ESG key aspects into our investment process
- Active dialogue with companies and investor-driven proxy voting using Invesco's proprietary Proxy Voting Platform
- Offering optionality to implement additional, customized ESG criteria tailored towards the client's needs
- ESG fully embedded in research processes and analytics and documented in every research note



Source: Invesco. For illustrative purposes only.

## Holistic ESG consideration in the investment process

The IQS team's investment process is built on the factors Momentum, Quality and Valuation, which can explain the long-term risk and return characteristics of equities. The team has identified that some signals within the Quality factor show positive correlation to governance factors. The calculation of these Quality signals is part of the daily factor score production and the multi-factor investment process. These Quality signals prefer companies with a high balance sheet quality which, for example, buy back shares and do not show disproportionate balance sheet growth. Governance factors also prefer companies in which management acts in the interests of shareholders and does not pursue unprofitable business projects.

Besides the implicit integration via the Quality factor, the team also explicitly uses its measures Adverse ESG Momentum and ESG Exposure Control. The team uses these measures to manage the risks which are associated with weakly scoring companies or portfolios.

For the Adverse ESG Momentum, the investment universe is screened daily for significant ESG downgrades. The team's research has shown that companies that experienced severe downgrades tend to underperform their peers in the following months. Therefore, the investment in companies which suffered severe downgrades would be restricted.

Additionally, the team uses the ESG Exposure Control. During the regular rebalancing the ESG exposure of the equity portfolio is managed against the exposure of the fund's equity benchmark, hence the S&P 500 index. The team targets an exposure that is approximately at or above benchmark level. The key point is guarding against a risk that historically has been small but is expected to be material in the future.

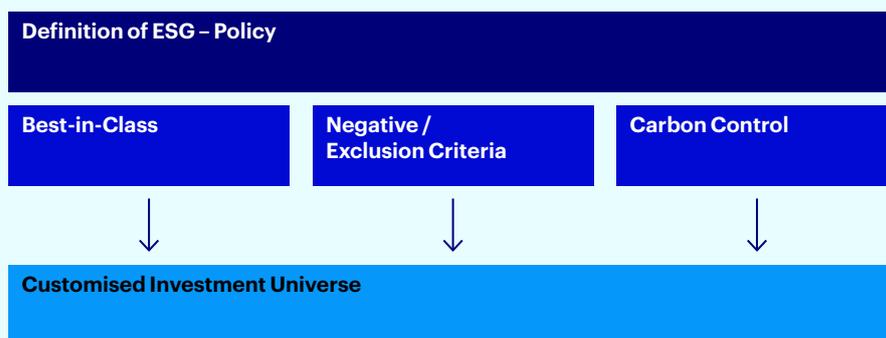
## Customised ESG

In addition to the standard ESG integration, IQS implements further individual ESG requirements in numerous respects:

### ESG screening for equities

Environmental, social and governance focus

- Flexible use through an individual client specific definition of over 250 ESG criteria
- Global universe of over 6,000 companies



Source: Invesco. For illustrative purposes only.

**Best-in-Class criteria:** By applying best-in-class criteria, companies are identified that display excellence in sustainable management and sustainable products or processes. They fulfil ecological and social requirements particularly well, ranging from climate efficiency and low water consumption to labour safety and satisfaction.

### Exclusion and negative criteria:

By applying these criteria, companies, sectors or countries are excluded from the investment universe which fail to fulfil certain ESG criteria or that violate international norms and standards according to the definitions of the International Labour Organisation (ILO), the OECD or the United Nations.

Using a wide range of data fields provided by V.E, the investment team is able to define a set of ESG criteria. Exclusion criteria and negative criteria can be used to eliminate companies that fail to meet certain ESG criteria, while with positive criteria, companies can be identified, which are particularly characterised by sustainable economic development, positive products or processes.

With the integrated best-in-class approach, the investment team also focuses on the best performing companies in their sector with respect to the company's ability to transition into a low carbon economy.

## Holistic ESG consideration in the investment process

The Invesco Sustainable US Structured Equity Fund uses the following exclusion criteria:

	<b>Controversial Activities</b>	<b>Excluded if</b>
<b>Coal</b>	Turnover derived from thermal coal mining	<b>&gt;=5%</b>
	Turnover derived from burning coal for power generation	<b>&gt;=5%</b>
	Proportion in electricity generation fuel mix from coal	<b>&gt;=10%</b>
	Structural increase of thermal coal activities over 3 years	<b>Yes</b>
<b>Unconventional oil &amp; gas</b>	Revenues that come from projects or the extraction of tar sands and oil shale, as well as the proportion of reserves in tar sands or oil shale	<b>0%</b>
	Involvement in fracking activities	<b>Yes</b>
	Involvement in arctic drilling activities	<b>Yes</b>
<b>Fossil fuel industry</b>	Revenues are derived from fossil fuel industries including upstream (exploration and production), midstream (processing and transport) and power generation from fossil sources	<b>&gt;=5%</b>
	Structural increase of fossil activities over 3 years	<b>Yes</b>
<b>Environmental strategy</b>	Company's commitment to define clear objectives and appropriate measures to ensure management of the environmental impacts of products and services	<b>Insufficient environmental strategy</b>
<b>Chemicals of concern</b>	Production of restricted chemicals	<b>0%</b>
<b>Bio-diversity</b>	Controversies in the field of endangering biodiversity	<b>Yes</b>
<b>Pollution</b>	Controversies in the field of preventing and managing of accidental pollution or soil pollution	<b>Yes</b>
<b>Community involvement</b>	Controversies in the field of community involvement (including e.g. impact of operations on the local economy, responsible tax strategy, transfer of technology and skills)	<b>Yes</b>
<b>Nuclear power</b>	Turnover from nuclear power	<b>&gt;=5%</b>
	Proportion in electricity generation fuel mix from nuclear power	<b>&gt;=5%</b>
<b>Civilian Firearms</b>	Manufacture or sale of civilian firearms or related products	<b>&gt;=10%</b>
	Manufacture of civilian firearms or related products	<b>&gt;=5%</b>
<b>Military</b>	Sales that are related to military sales including key parts or services for conventional weapons	<b>&gt;= 5%</b>
	Controversial weapons & financing of cluster munition or anti-personnel landmines	<b>0%</b>
<b>Tobacco</b>	Turnover from production and distribution	<b>&gt;=10%</b>
	Turnover from production	<b>&gt;=5%</b>

# Holistic ESG consideration in the investment process

	Controversial Activities	Excluded if
<b>UN Global Compact</b>	Fail to pass the global compact screening	<b>Yes</b>
<b>Human Rights</b>	Controversies in Labour Rights including the supply chain, forced or child labour and discrimination	<b>Yes</b>
<b>Water</b>	Controversies in Pollution or lack of protection of water resources	<b>Yes</b>
<b>Recreational Cannabis</b>	Involvement in recreational cannabis	<b>Yes</b>

For the low carbon best-in-class approach the Invesco Quantitative Strategies Team uses the Energy Transition score from V.E. The score seeks to inform on a company's strategic approach to reducing their emissions and to adapt their business model to address the risks and opportunities tied to the transition to a low carbon economy. During the construction of the portfolio, the fund aims to reduce the aggregated Scope 1 and 2 greenhouse gas emission intensity by at least 30% compared to the market cap weighted benchmark.

As a result of these ESG guidelines for screening, it is expected that the size of

the investment universe of the Fund will be reduced by about 40 to 50% in terms of number of issuers.

Derivatives, which are utilized to gain exposure to capital markets have to fulfil the ESG criteria on a constituent's level. This includes derivatives used for efficient portfolio management. The product does not use any derivatives on agricultural commodities.

The product does not structurally invest into Fixed Income securities neither issued by states nor by corporates.

## Proxy Voting

Invesco's Proxy Voting approach is governed by the Global Proxy Voting Policy,<sup>1</sup> which is premised on respecting the fund manager's freedom to vote in what they believe is the best interests of the investors in the relevant fund or portfolio in order to achieve positive outcomes for clients.

To this effect, Invesco maintains a proprietary global proxy administration platform, known as "PROXYintel". The platform streamlines the proxy voting and ballot reconciliation processes, as well as related functions, such as share blocking and managing conflicts of interest issues. This enables fund managers to vote in an efficient manner, increase transparency, share knowledge and effectively influence corporate practices and behaviours.



Source: Invesco. For illustrative purposes only.

Invesco adopts and applies a dedicated ESG voting policy across managed funds, portfolios and mandates. Besides the support of shareholder proposals through Invesco's proprietary "PROXYintel" Fund Manager Portal, specific voting decisions on the following ESG topics are taken if applicable:

- Gender Pay Gap Proposals
- Political contribution disclosure/political lobbying
- Disclosure/political activities and action data security
- Privacy and internet issues
- Report on Climate Change/climate change action and
- Gender Diversity on public boards.

<sup>1</sup> <https://www.invesco.com/corporate/dam/jcr:a1f25695-b417-4701-b399-5e6ec31929c8/Global%20Proxy%20Policy%20-%20Effective%20January%202021%20-%20FINAL.pdf>

# Holistic ESG consideration in the investment process

## Engagement

IQS enters regularly into dialogue with carefully selected target companies via the Global Engagement Service of V.E. The potential target companies are selected by IQS and a final selection of the companies to be engaged with is then agreed with V.E. In general, the team look to engage on topics related to the IQS Priority ESG Themes, which are Climate Change, Human Rights, Supply Chain Management, Water and Bribery/Corruption.

IQS selects investee companies which are at a size and stage making them likely to be influenceable. The objective is to identify weaknesses in the company's sustainability management and discuss these with management to enable the companies to achieve a better ESG performance in the medium to long term. Discussions can take place via telephone calls, personal meetings and written communication. Engagements are followed through over a period of years where necessary.

## Direct dialogue with companies



- Address ESG risks and weaknesses
- Enhance ESG performance of companies
- Pooling of interest of different asset managers

### IQS Engagement ESG themes

- Climate change
- Water management
- Bribery & corruption
- Supply Chain labour standards
- Human rights
- Global norms & conventions

### Joint Engagement with Invesco ESG areas

- Good governance
- Climate change
- Social Equity
- Climate Action 100+

Source: Invesco Quantitative Strategies, Vigeo Eiris. For illustrative purposes only.

## IQS' engagement priorities follow two methods:

- Theme-based engagement, which aims to encourage companies to expose and reduce systemic risks in areas such as bribery reporting; climate change; human rights management systems; supply chain labour policy and water scarcity.
- Controversy-led engagement, which aims to prompt companies to observe internationally-recognized standards and conventions and correspondingly improve their company guidelines.

V.E undertakes a detailed assessment of the themes for each company that the IQS team has selected. This is based upon a long established and rigorous methodology and involves assessing the level of risk that a company is exposed to in any one area and then analysing how the company mitigates these risks.

IQS also leverages on the firm-level engagement and actively supports the Climate Action 100+ initiative.

# Investment Process

## Investment universe

The investment universe comprises US listed equities that meet the defined sustainability criteria using exclusions as well as Best-in-Class criteria. Risk management is an integral part of each investment step.

The investment team relies on its factor-based selection model, which seeks to capture the factors of Quality, Momentum and Valuation. In addition, the IQS team implements specific ESG criteria. Following in-depth factor research, IQS uses proprietary factor definitions that are expected to deliver results in excess of standard factor definitions.

**In the first step**, the whole investable US stocks universe (around 1200 stocks) is screened for ESG criteria to define the eligible ESG universe. The eligible number of stocks of the ESG universe varies depending on the ESG criteria. At this stage the adverse ESG momentum is applied, which leads to exclusion of companies which face severe downgrades in their ESG score. Afterwards the stocks are ranked according to each stock's attractiveness with respect to the above-mentioned factors. To achieve comparability, these rankings are done within industry groups within regions, i.e. on an industry-neutral basis by region.

**In step two**, these factor rankings are weighted in order to obtain an overall multi-factor measure of a stock's attractiveness, a weighted multi-factor score. The weightings of the factors are determined with a view through the cycle, i.e. with the intention to establish highly attractive long-term risk-adjusted return expectations. This overall multi-factor attractiveness score is based on stock characteristics that have historically proven to differentiate successful from unsuccessful stocks, it is a measure of a stock's relative attractiveness within its regional peer group.

**Step three** determines a corresponding risk forecast for each stock in the universe by using a proprietary risk model that uses the same multi-factor building blocks as the return forecasting in order to assure alignment of return and risk view.

**Step four** constructs a Low Volatility tilted anchor portfolio. This portfolio is constructed using an optimization approach by reducing the ex-ante volatility of the portfolio. The ESG criteria as well as the greenhouse gas intensity reduction targets are incorporated in this step.

**In the final step**, the portfolio construction/optimisation establishes factor weightings aiming at high sensitivities of the overall portfolio with respect to the factors applied while rigorously managing risks and neutralising non-rewarded risks. This explicitly includes consideration of transaction costs.

Factors Balanced, time-tested	Momentum		Quality	Value
	Earnings Momentum	Price Momentum		
Proprietary signals Quantifiable, predictive, complementary	<ul style="list-style-type: none"> <li>Earnings momentum</li> <li>Earnings/sales revisions</li> <li>Revisions against trend</li> <li>Cash flow surprise</li> </ul>	<ul style="list-style-type: none"> <li>Specific momentum</li> <li>Risk-adjusted momentum</li> <li>Event momentum</li> <li>Short interest</li> </ul>	<ul style="list-style-type: none"> <li>Net external financing</li> <li>Net asset growth</li> <li>Profitability &amp; operating efficiency</li> <li>Fundamental health</li> <li>Accounting integrity</li> </ul>	<ul style="list-style-type: none"> <li>Cash flow yield</li> <li>Gross profit yield</li> <li>Earnings yield</li> <li>Book yield</li> <li>Dividend yield</li> </ul>

Source: Invesco, as of 30 September 2021. For illustrative purposes only. Not all signals are used in all regions and sub-models. Signals often have subcomponents. Additional signals are used in specific sub-models and definitions may vary across regions

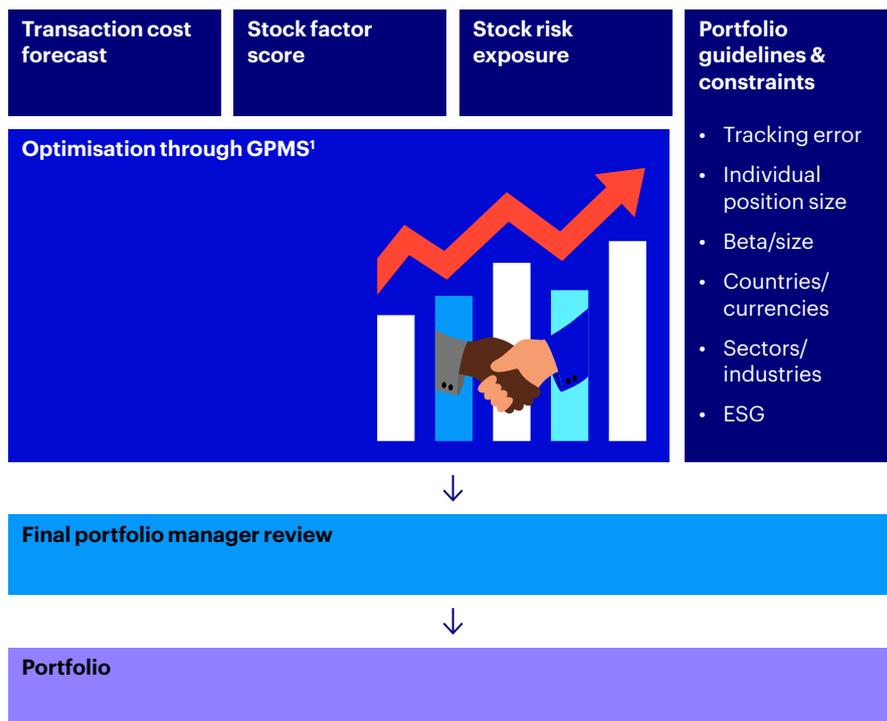
# Investment Process

The resulting ESG equity portfolio will establish broadly diversified factor exposures towards stock characteristics we like, seeking to capture the long-term positive premiums of these factors deemed rewarding while reducing volatility compared to a capitalisation weighted index.

Finally, before the portfolio is implemented a member of the IQS Portfolio Management team manually checks the optimisation results and the suggested trades for data consistency. The portfolio manager

does not have a discretionary right to overrule the optimisation results. However, if the portfolio manager finds data inconsistencies for a stock, e.g. due to a last-minute profit warning, the IQS team has defined procedures for how to deal with a stock in such a case. After the correction of the data, the optimisation is run again to reflect all important information. Subsequently to the sign-off of the optimisation result, the portfolio adjustments will be implemented into the portfolio.

## How we build the optimal equity portfolio



Source: Invesco. For illustrative purposes only. <sup>1</sup> Global Portfolio Management System.

# Fund Facts

## Invesco Sustainable US Structured Equity Fund

Investment Centre	Invesco Quantitative Strategies
Fund Manager	Alexander Uhlmann Alexander Tavernaro, CFA
Contracted Vehicle Type	SICAV
Domicile Country	Luxembourg
Launch Date	28 June 2002
Fund volume	USD 35.1 m

Source: Invesco as at 31 March 2021.

