HEALTH WEALTH CAREER

MERCER DELEGATED SOLUTIONS EUROPE

SUSTAINABLE INVESTMENT POLICY

MAY 2019

MAKE TOMORROW, TODAY

MERCER

POLICY SCOPE AND KEY PRINCIPLES

Mercer Delegated Solutions in Europe (Mercer DSE)[1] provides services to a broad range of institutional investors, including pension funds endowments, foundations and other investors.

This policy sets out how Mercer DSE will implement its beliefs on sustainable investment within the multi-client Mercer Funds[2] it manages. Mercer does not directly select investments; instead, it selects and combines specialist sub-investment managers into portfolios. The following key principles underpin this policy:

- **Clear communication** to sub-investment managers of Mercer DSE's environmental, social and corporate governance (ESG) expectations
- **Active monitoring** of sub-investment manager ESG and stewardship activities
- **Engagement** with sub-investment managers to improve ESG practices over time
- **Transparency** on the implementation of this policy to the investors in the Mercer Funds

Please refer to this policy for Mercer DSE's key principles and general approach to ESG factors; sustainability trends; climate change; stewardship (voting and engagement) and screening or exclusions.

[1] Mercer DSE is delivered by Mercer Limited, registered in England No. 984275, whose registered office is at 1 Tower Place West, Tower Place, London EC3R 5BU and Mercer Global Investments Europe Limited, registered in Ireland, No 416688, whose registered office is at Charlotte House, Charlemont Street, Dublin 2, Ireland.

[2] "Mercer Funds" are any collective investment scheme, including investment companies, common contractual funds, unit trusts and limited partnerships, for which Mercer Global Investments Europe Limited or any affiliate serves as discretionary investment manager.

OUR APPROACH

Mercer, through its global investment consulting business, has advised investors on all aspects of responsible investment (RI) since 2004, and this experience informs the approach taken by Mercer DSE. Mercer DSE is supported by European-based and global members of Mercer's RI team.

Mercer articulates its approach in its global investments beliefs. These beliefs support Mercer's commitment to the Principles for Responsible Investment (PRI) and recognise the international and regional guidance on stewardship, such as the UK Stewardship Code. Mercer's *Investing in a Time of Climate Change* report (and the 2019 Sequel), the Paris Agreement on Climate Change; and frameworks such as the Financial Stability Board's Task Force on Climate-related Financial Disclosures (TCFD) and the United Nations' Sustainable Development Goals inform Mercer's investment beliefs and approach.

Mercer believes a sustainable investment approach is more likely to create and preserve long-term investment capital and, more specifically, that:

1. **ESG** factors can have a material impact on long-term risk and return outcomes and should be integrated into the investment process.
2. **Taking a broader and longer-term perspective on risk**, including identifying sustainability themes and trends, is likely to lead to improved risk management and new investment opportunities.
3. **Climate change poses a systemic risk**, and investors should consider the potential financial impacts of both the associated transition to a low-carbon economy and the physical impacts of different climate outcomes.
4. **Stewardship** (or active ownership) supports the realisation of long-term shareholder value by providing investors with an opportunity to enhance the value of companies and markets.

Consequently, Mercer DSE believes that a sustainable investment approach that considers these risks and opportunities is in the best interests of our clients.

ESG INTEGRATION

Mercer DSE expects all its sub-investment managers to assess and reflect ESG risks and opportunities in security selection and portfolio construction. Examples of ESG factors include:

Table 1. ESG Factors

ENVIRONMENTAL	SOCIAL	GOVERNANCE
Climate change	Health and safety	Board structure and diversity
Water	Demographics/consumption	Remuneration
Waste and pollution	Supply-chain labour issues	Accounting and audit quality

Selection and monitoring processes for potential and appointed sub-investment managers include Mercer's ESG Ratings and associated commentary from the Manager Research team (see Appendix for further detail). ESG Ratings are reviewed during quarterly monitoring processes, with a more comprehensive review performed annually — which seeks evidence of positive momentum on ESG integration. Expectations are set as ESG3 or above, where practicable and relevant to the strategy (with ESG1 being the highest rating and ESG4 being the lowest). Comparisons are also made with the appropriate universe of strategies in Mercer's global database.

SUSTAINABILITY THEMES

Mercer DSE believes that including some exposure to sub-investment managers that identify longer-term environmental and social themes and trends is likely to lead to improved risk management and new investment opportunities.

In addition to "pure-play" allocations to clean energy, water, timber or agriculture, this can include "broad sustainability" allocations to companies providing sustainable goods and services solutions in environmental matters or social areas, such as health and education. Selection and monitoring processes for potential and appointed sub-investment managers increasingly consider these exposures in portfolio construction decisions.

APPLICABLE ASSET CLASSES — ESG AND SUSTAINABILITY

Mercer DSE believes that ESG factors can be applied across asset classes — including listed equities (active and passive), sovereign and corporate bonds, property and unlisted assets. However, we acknowledge that the degree of relevance, or materiality, varies across asset classes, as does the current state of integration by strategies within asset classes. Sustainability-themed strategies are more prevalent in equities and real assets (infrastructure, timber, agriculture) and less so in other asset classes. These considerations, summarised in Table 2, inform our expectations for sub-investment managers in Mercer DSE's selection and monitoring processes.[3]

Table 2. ESG and Sustainability by Asset Class

	Manager progress on ESG integration*	Availability of sustainability themed strategies**
Public equity (active)	Medium/high	Low/medium
Fixed income	Low/medium	Low
Real estate	Medium/high	Low
Private equity and debt	Medium	Low/medium
Infrastructure	High	Medium/high
Natural resources***	Medium	Medium/high
Hedge funds	Low	Low

NB: Low: <5%; low/medium: 5%–10%; medium: 11%–20%; medium/high: 21%–40%; high: >40% (As at Dec 2018)

* Refers to the percent distribution of ESG1- and ESG2-rated strategies in Mercer's Global Investment Manager Database (GIMD), where available.

** Refers to percent distribution of ESG1- and ESG2-rated strategies compared to mainstream by asset class — noting equities is a large universe so the low relative number is not actually a low absolute number.

*** Conservate view — research updates in this asset class may result in a more favourable view than is currently held.

[3] At the time of adoption of this policy, Mercer does not assign ESG ratings to passive fixed income strategies. Thus, MGI has no expectations of passive fixed income subadvisors as it relates to this policy.

CLIMATE CHANGE

Mercer DSE believes climate change poses a systemic risk, with financial impacts driven by two key sources of change. The first is the physical damages expected from an increase in average global temperatures and the second is the associated transition to a low-carbon economy, required to mitigate the likelihood and severity of physical damages. Each of these changes presents both risks and opportunities to investors, as outlined in Mercer's *Investing in a Time of Climate Change* reports.

Mercer DSE considers these potential financial impacts at a client portfolio level, in portfolio construction within asset classes and in sub-investment manager selection and monitoring processes. Together with ongoing research, the potential financial impacts of climate change are included in Mercer's modelling estimates under multiple climate scenarios for physical damage and transition risk factors (as per the *Investing in a Time of Climate Change* report). At the sub-investment manager level, Mercer DSE's expectation is that climate change risk assessment and risk reduction are integrated within a manager's approach to ESG, stewardship activities and sustainability themes.

Mercer DSE believes that limiting global average temperature increases this century to "well below two degrees Celsius", as per the 2015 Paris Agreement, is aligned with the best economic outcome for long-term diversified investors. Mercer DSE therefore participates in collaborative industry engagements to support this end goal and will seek to increasingly align portfolios with that objective, where consistent, with meeting stated investment objectives.

Mercer DSE's approach to climate-related financial risks and opportunities is summarised below, consistent with the framework recommended in 2017 by the Financial Stability Board's TCFD. Disclosure consistent with the TCFD recommendations are also expected of appointed sub-investment managers.

In summary, Mercer DSE takes the following approach to the TCFD framework's four elements for managing climate-related financial risks:

Governance: Nominated members of the board and the management team have oversight of the Mercer DSE approach to climate-related risks and opportunities, with support provided by Mercer's RI team. The board oversees Mercer DSE's compliance with this policy through annual reporting from management to the board.

Strategy: Climate-related scenario analysis is undertaken as part of strategy reviews on multi-asset class portfolios. Portfolio construction within asset classes is undertaken with a consideration of climate-related risks and opportunities under different climate scenarios.

Risk management: Consideration is given to risk-reduction strategies to decarbonise the portfolio and identify new low-carbon opportunities, including adding exposure to sustainability-themed sub-investment managers and reviewing passively managed index exposures. In addition, Mercer DSE participates in industry-wide engagement activity to encourage successful implementation of the Paris Agreement in an effort to minimise future systemic risk associated with climate change. We also review sub-investment managers' individual voting activity in regards to key climate-related resolutions and engage with these managers where deemed appropriate.

Targets/metrics: Metrics, such as carbon footprinting, are employed to review carbon policy risk relative to benchmark for listed equities exposures and to engage with sub-investment managers on the results. Mercer DSE expects metrics and targets to evolve across asset classes as data becomes increasingly available and reliable.

A stand-alone report on how this policy is being implemented, including example analysis on strategy and targets/metrics, will be available in Q3 2019.

APPLICABLE ASSET CLASSES

As per the systemic risk comments above and Mercer's *Investing in a Time of Climate Change* reports, Mercer DSE's current view is that climate change risks are applicable, to varying degrees, across all asset classes. Initial activity has focused on listed equities, active and passive, and sustainability-themed private markets investments; however, all asset classes are being reviewed. As climate change expertise continues to evolve, we will review and update our views and approaches accordingly.

STEWARDSHIP — SHARE VOTING AND ENGAGEMENT

Mercer DSE believes stewardship (or active ownership) helps the realisation of long-term shareholder value by providing investors with an opportunity to enhance the value of companies and markets in a manner more consistent with long-term investor timeframes; for example, voting on resolutions at company AGMs and writing to or meeting with company management on particular issues.

This policy represents Mercer DSE's commitment to industry standards of good governance and stewardship. Mercer DSE's Irish-domiciled investment management business also supports the UK Stewardship Code as universal good practice and has made a voluntary statement of commitment on its approach to each of the Code's seven underlying principles.

Mercer Funds, managed by Mercer DSE, are long-term institutional investors and consider investment governance and active ownership to be of particular importance. Active/engaged shareholders have a greater chance of ensuring company management acts in ways that are aligned with shareholder interests. Stewardship can also provide investors with an opportunity to enhance the value of companies and markets and to acquire additional information, which can enhance the investment decision process.

Mercer DSE expects sub-investment managers of the Mercer Funds that invest directly in listed equities to comply with this policy. For pooled investment vehicles, Mercer DSE will engage with the sub-investment managers, with the aim of improving the managers' ESG practices in line with this policy.

Mercer DSE's approach has four main components and principles:

SHARE VOTING

All shares are to be voted by sub-investment managers in a manner deemed most likely to protect and enhance the long-term value for investors.

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All votes are to be evaluated and voted on, unless there is a valid reason to prevent this (see Voting Exceptions on page 8).

TRANSPARENCY

Voting and engagement activities of sub-investment managers appointed by Mercer DSE are to be reviewed regularly, including voting records and statistics, along with engagement examples, reported on at least an annual basis.

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Reporting will be provided to investors in the form of an annual policy and voting and engagement activity review. (see Monitoring Voting and Engagement on page 9).

CORPORATE ENGAGEMENT

Mercer DSE expects sub-investment managers appointed to Mercer Funds to adopt clear guidelines on their engagement activities and escalation processes and to report on these activities and outcomes.

PUBLIC POLICY PARTICIPATION

Engagement with regulators, and sometimes governments, to recommend changes or express views on proposed changes to regulatory regimes may be required where this is deemed important to protect the rights and enhance the interests of shareholders.

APPLICABLE CORPORATE GOVERNANCE PRINCIPLES

Mercer DSE's monitoring focus on voting resolutions and engagement is informed by a range of principles and codes, including the corporate governance guidance and principles published by the Organisation for Economic Co-operation and Development (OECD) and the International Corporate Governance Network (ICGN), along with the 2012 EU Commission Action Plan on European company law and corporate governance, the Central Bank of Ireland Corporate Governance Code and the 2018 UK Corporate Governance Code. These principles are grouped as follows:

1. **Shareholder rights:** Shareholders have basic rights that should be upheld. In particular, shareholders should be able to share in company profits, participate in major decisions and exercise their "voices" (for example, through proxy voting or direct company engagement).
2. **Role and responsibilities of the board:** The board is central to the exercise of good corporate governance within companies. It is accountable to shareholders and must act in their best interests as well as those of the company. History has shown that effective boards are likely to enhance long-term corporate value, thereby creating value for shareholders.
3. **Risk and audit:** The board of the investee company plays a central role in supporting a corporate culture of integrity and ethical standards (which applies equally to the conduct of the board itself). Directors should consider what the European Commission refers to as "the entire range of risks" faced by their company — in this, we would include ESG risks — and ensure that sufficient information on the most important (and potentially material) of these risks is disclosed.
4. **Disclosure and transparency:** Information on a company's challenges, achievements and failures should be provided to shareholders (and other stakeholders). Company disclosures should be timely and relevant and use appropriate and high-quality reporting frameworks (such as international accounting standards). Shareholders increasingly expect information on relevant and potentially material ESG issues in addition to standard financial disclosures — for example, a company's access to and management of non-renewable resources and its carbon emissions.
5. **Remuneration and incentives** — The rewards and incentives provided to company executives should align their interests with those of shareholders — the ultimate owners of the company. The fundamental purpose of companies from the perspective of shareholders is to create long-term value. Remuneration policies have an important role to play in supporting this purpose — in particular, by focusing the minds of executives on long-term rather than short-term value creation.

VOTING EXCEPTIONS

Mercer DSE's objective is for its sub-investment managers to vote on all listed equities in which the Mercer Funds invest, with the following qualifications and exceptions:

Conflicts of interest: As part of its review and appointment process, Mercer DSE assesses whether selected sub-investment managers have policies and procedures that are designed to manage conflicts in relation to stewardship. Sub-investment managers are required to report on any conflicts of interest and demonstrate that they have adhered to their conflicts policy and reported any breaches.

Power of attorney (PoA) markets: Some global markets allow voting to be carried out only by in-person attendance. The rules on PoA vary by market, apply for different periods of time and have various cost implications. Mercer DSE expects the sub-investment managers to have PoAs in place for larger markets but accepts that a cost/benefit view on smaller markets is required, and shares may not be voted where that is prohibitive.

Share-blocking markets: Some markets place regulatory barriers on voting, usually in the form of limitations on trading of shares if a vote is enacted. Mercer DSE's objective is to vote in these markets but accepts that, on occasion, not all votes will be cast by sub-investment managers.

Stock lending: Mercer's stock lending program is a fully collateralised solution and indemnified solution, managed and implemented by an external Securities Lending Agent (SLA). Collateral posted by borrowers is held in a segregated account by a Triparty Collateral Manager appointed by the SLA. The SLA has established processes to recall shares on loan for voting purposes ahead of an AGM, and Mercer expects that this will not affect our objective for sub-investment managers to vote on all listed equities. The SLA also implements exclusions on acceptable collateral, with Mercer's current exclusions outlined in the Screening section of this policy on the following pages.

Where sub-investment managers have not voted, Mercer DSE expects rationale to be provided, which typically includes references to PoA or share-blocking. Mercer DSE periodically reviews the percentage of "no votes" and the rationale provided and may engage with the sub-investment manager if these reviews raise questions or concerns.

MONITORING VOTING AND ENGAGEMENT

Mercer DSE expects its selected sub-investment managers to monitor investee companies and to report on stewardship activities and outcomes.

Mercer DSE also monitors stewardship explicitly for the Mercer Funds by seeking disclosure from the sub-investment managers on two annual stewardship information requests:

1. A policy review that applies the UK Stewardship Code principles framework: Monitoring confirms that managers have achieved, are making reasonable progress towards or can reasonably explain why they do not anticipate meeting the requirements of the Code.
2. A voting and engagement activity review that covers the following areas:

Voting Execution: The Broadridge voting system is used to obtain voting statistics to monitor execution and consider vote percentages.

Voting Rationale: Brief commentary, based on sub-investment-manager-disclosed information, covers votes cast in four parts: a) votes against management; b) votes against proxy advisor policy (where applicable); c) abstentions and d) no votes.

Engagement: Brief commentary, based on sub-investment manager-disclosed information, captures examples of instances where the sub-investment manager has exchanged views with companies — for example, a) number of companies engaged; b) engagement examples by topic; c) engagement examples that are collaborative and d) any voting activity that is an escalation connected to engagement.

Mercer DSE accepts that sub-investment managers may have detailed knowledge of both the governance and the operations of the investee companies and has therefore enabled sub-investment managers to vote based on their own proxy-voting execution policy. Leveraging sub-investment manager knowledge to benefit the voting process may result in “split votes”, where Mercer DSE’s sub-investment managers vote differently on a resolution. Mercer DSE regards explanations from sub-investment managers as critical, and these explanations, particularly where there are split votes, are part of the monitoring process.

SCREENING

Mercer DSE undertakes screening with two key objectives in mind, to identify:

1. High-severity breaches of the UN Global Compact (UNGC) Principles that relate to human rights, environmental and corruption issues, as identified by MSCI's ESG Research. In response to identified breaches, Mercer DSE will engage with the sub-investment managers owning those companies and seek their views on the risk, return and reputation implications. If, over a meaningful period of time, the company has not rectified the breach and the sub-investment manager still owns the company, Mercer DSE may direct this to be sold.
2. Investment activities nominated for exclusion. Mercer DSE believes that exclusions are driven by clients and a requirement to avoid profiting from investment activities that don't align with stakeholder values and expectations. When considering exclusions, Mercer has developed an Investment Exclusions Framework in which multiple risk, return and reputation criteria are considered.

For Mercer DSE's actively managed multi-client equity and fixed income funds, and selectively for some passively managed multi-client equity funds, companies that manufacture whole weapons systems, components or delivery platforms, or components that were developed or are significantly modified for exclusive use in cluster munitions, anti-personnel landmines, biological, chemical or nuclear weapons are excluded. Mercer utilises MSCI ESG Research to inform the sub-investment managers of the list of companies to be excluded each quarter.

Mercer DSE also manages a number of Mercer Funds for which, in order to meet client expectations, the appointed sub-investment managers have additional screens or exclusions to those above included in their investment guidelines, and these are documented separately for clients. In these cases, Mercer DSE identifies the activity to be excluded, and the sub-investment managers are responsible for stock-level implementation. Screening examples include restrictions on companies earning a percentage of revenue from tobacco, gambling, alcohol, adult entertainment or fossil fuel reserves.

POLICY IMPLEMENTATION

Table 3 describes how Mercer DSE will implement the commitments set out in this policy across the different asset classes.

Table 3

Asset class	Listed equities	Fixed income	Liquid alternatives (hedge funds)
Monitoring	• Assess manager's ESG capabilities using Mercer's ESG Ratings and Stewardship Assessments, including for passive and quantitative strategies. • Monitor voting and engagement activity. • Monitor portfolio holdings for ESG issues, including climate-change-sensitive sectors. • Monitor turnover frequency of company holdings by strategy and seek exposure to some low turnover strategies.	• Assess manager's ESG capabilities using Mercer's ESG Ratings. • Monitor for ESG in the context of country and credit decisions and positioning for long-term, thematic-driven views. • Monitor portfolio holdings for ESG issues, including climate-change-sensitive sectors.	• Assess manager's ESG capabilities using Mercer's ESG Ratings.
Engagement	• Engage with managers on areas of weakness based on outputs of monitoring of ESG and stewardship activities. • Request information on the views of managers on material ESG issues (for example, climate change) and how they are considering these issues in investment analysis and portfolio construction.	• Engage with managers on areas identified for improvement during reviews and monitoring.	• Engage with managers on areas identified for improvement during reviews and monitoring.
Transparency	• Reporting is to be provided annually to investors on our progress against the above commitments.		
Supporting industry initiatives	In addition, Mercer and Mercer DSE will participate where possible in collaborative industry initiatives on responsible and sustainable investment. Mercer currently supports the following key initiatives globally and within Europe: • Carbon Disclosure Project (CDP) • Global Impact Investing Initiative (GIIN) • United Nations Principles for Responsible Investment (PRI) • UK and European Sustainable Investment and Finance Association (UKSIF and Eurosif) • Institutional Investors Group on Climate Change (IIGCC) • Task Force on Climate-related Financial Disclosures (TCFD)		

APPLICATION TO DIFFERENT INVESTMENT ARRANGEMENTS

Appointment of sub-investment managers may be by either segregated mandates or investments in pooled vehicles, or by a combination of both. Mercer DSE will actively monitor its appointed sub-investment managers on ESG integration, consistent with this Sustainable Investment Policy; however, application may vary depending on the degree of discretion available (which is expected to be higher in segregated mandates relative to pooled vehicles) in which the Mercer Funds invest.

POLICY GOVERNANCE

Mercer DSE is the owner of this policy. Mercer's RI team supports and reports to Mercer DSE on those topics covered by the policy and will be accountable for guiding the implementation of the policy, reviewing the policy annually and recommending amendments as necessary.

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APPENDIX — MERCER ESG RATINGS

Mercer's ESG Ratings represent the Mercer Manager Research team's assessment of the degree to which ESG factors are incorporated within a strategy's investment process. Four factors are considered and documented within the research commentary and an overall rating assigned, where ESG1 = highest possible rating and ESG4 = lowest possible rating. The research is stored within Mercer's Global Investment Manager Database (GIMD).

MERCER'S FOUR FACTORS

IDEA GENERATION

- Efforts to identify and integrate ESG factors into active fund positions as a source of added value
- Identification of material ESG factors — skill of team members, data sourcing

IMPLEMENTATION

- Engagement and proxy voting activities (where applicable) with investee companies
- Does the investment horizon align with the ability to effectively implement ESG views?

PORTFOLIO CONSTRUCTION

- Efforts to integrate ESG-driven views into the portfolio's construction

BUSINESS MANAGEMENT

- Firm-level support for ESG integration, engagement activities and transparency

ESG1	ESG2	ESG3	ESG4
Leading approach to integration, where ESG is **embedded in investment philosophy**; strong on stewardship, which is a core part of the process	**Consistent and repeatable** process to ESG integration; well-developed evidence of stewardship	**Well-developed focus on G factors; less consistency in E&S;** stewardship process is ad hoc, but an indication of progress	**Little or no integration of ESG factors** or stewardship into core processes and no indication of future change

For passive equity ratings, the overall framework is the same, but the focus is primarily concerned with stewardship activities.

MERCER'S FOUR FACTORS — PASSIVE EQUITIES

VOTING AND ENGAGEMENT

- Policy, process and prioritisation
- Quality of engagements

RESOURCES AND IMPLEMENTATION

- Skill set of resources
- Effectiveness of engagement outcomes

ESG INTEGRATION AND INITIATIVES

- Data analysis to enhance active ownership

FIRMWIDE COMMITMENT

- Collaborative initiatives and engagement with regulators and policymakers

ESGp1	ESGp2	ESGp3	ESGp4
Leaders in voting and engagement (V&E) **across ESG**; stewardship activities and ESG initiatives undertaken consistently at a **global level; clear link between V&E actions**	**Strong approach** to V&E across ESG topics, and initiatives at a regional level, with progress made at a global level; **working towards clearer links between V&E**	Focus of V&E tends to be on **governance topics only**, or more regionally focused, with **less evidence of E&S** (in V&E, as well as other internal ESG initiatives)	**Little or no initiatives taken** on developing a global V&E capability, reactive engagements; little progress made on other ESG initiatives

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