Environmental and/or social characteristics of the External Funds mandate

Product name	Discretionary External Funds Mandate
Legal entity identifier	PSZXLEV07O5MHRRFCW56

1. Environmental and/or social characteristics

Does this financial product have a sustainable investment objective[1]?	
●● ☐ **Yes**	●○ ☑ **No**
☐ It will make a minimum of **sustainable investments with an environmental objective: _____%**	☐ It promotes Environmental/Social (E/S) characteristics and while it does not have as its objective a sustainable investment, it will have a minimum proportion of ____% of sustainable investments
☐ In economic activities that qualify as environmentally sustainable under the EU Taxonomy[2] ☐ In economic activities that do not qualify as environmentally sustainable under the EU Taxonomy	☐ With an environmental objective in economic activities that qualify as environmentally sustainable under the EU Taxonomy ☐ With an environmental objective in economic activities that do not qualify as environmentally sustainable under the EU Taxonomy ☐ With a social objective
☐ It will make a minimum of **sustainable investments with a social objective: _____%**	☑ It promotes E/S characteristics, but **will not make any sustainable investments**

2. What environmental and/or social characteristics are promoted by this financial product?

The discretionary external funds mandate ("External Funds Mandate") aims to direct investments in such a way as to limit adverse impacts on the climate and environment, and encourage adherence to the principles of the UN Global Compact.

Furthermore, management of the External Funds Mandate is based on the following characteristics:

1. Monitoring of environmental and social controversies
2. Respect for the sector exclusion policies of Banque de Luxembourg (the Bank).
3. Respect for the United Nations Global Compact

Lastly, the External Funds Mandate ensures that the companies in which investments are made apply good governance practices. The objective of the External Funds Mandate is to have at least 50% of investments aligned with these environmental and social characteristics.

The Mandate is therefore classified as an Article 8 product under Regulation (EU) 2019/2088 (the "SFDR"). A reference benchmark has not been designated for the attainment of this product's environmental and social characteristics.

1. **Sustainable investment** means an investment in an economic activity that contributes to an environmental or social objective, provided that the investment does not significantly harm any environmental or social objective and that the investee companies follow good governance practices.

2. The **EU Taxonomy** is a classification system laid down in Regulation (EU) 2020/852, establishing a list of **environmentally sustainable economic activities**. That Regulation does not lay down a list of socially sustainable economic activities. Sustainable investments with an environmental objective might be aligned with the Taxonomy or not.

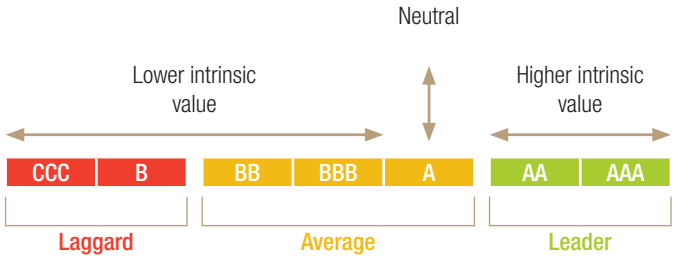
What sustainability indicators[3] are used to measure the attainment of each of the environmental or social characteristics promoted by this financial product?

The Bank invests first and foremost in assets whose data is covered by MSCI ESG Manager[4]. At least 50% of the assets for which data is available must be aligned with the sustainability characteristics promoted by the mandate.

The Bank has selected several sustainability indicators to measure these characteristics:

1. The exclusion of the environmental and/or social controversies deemed the most severe;
2. The restriction or exclusion of assets linked to certain industries such as coal;
3. Alignment with the UN SDGs.

MSCI ESG Manger's ESG ratings are aimed at measuring a company's management of financially relevant ESG risks and opportunities. This method is based on rules for identifying industry leaders and laggards according to their ESG risk exposure, and the way in which they manage these risks relative to their peers.



This approach uses the following additional indicators:

– The implementation of limits for the principal adverse impacts of investments, which are set by the Bank based on data provided by MSCI ESG Manager. These limits are determined for each adverse impact based on an average of the adverse impacts of comparable assets. The mandate's approach requires at least 50% of the invested portfolio to be aligned with these limits, i.e. to have a lower adverse impact than the average for its peers;

– An average overall rating of at least A for the proportion of assets covered by MSCI ESG Manager (excluding cash and gold);

– At least 50% of the assets covered by MSCI ESG Manager (excluding cash and gold) must be rated at least BBB;

The investment decisions of this mandate consider all of these indicators, measured using a proprietary calculation methodology of the Bank based principally on an analysis of the data provided by MSCI ESG Manager.

The EU Taxonomy sets out a "do not significant harm" principle by which Taxonomy-aligned investments should not significantly harm EU Taxonomy objectives and is accompanied by specific EU criteria.

The "do no significant harm" principle applies only to those investments underlying the financial product that take into account the EU criteria for environmentally sustainable economic activities. The investments underlying the remaining portion of this financial product do not take into account the EU criteria for environmentally sustainable economic activities.

Any other sustainable investments must also not significantly harm any environmental or social objectives.

3. Does this financial product consider principal adverse impacts[5] on sustainability factors?

☑ **Yes**, in addition to the ESG approach followed in the management of this product, the principal adverse impacts on sustainability factors are also taken into account.

For each asset class, and for each of the principal adverse impacts that must be considered, the Bank has set a threshold that is either fixed (according to EU recommendations or the Bank's sector exclusion policies), or variable, according to a regional average of adverse impacts from comparable assets, provided by MSCI ESG Manager.

3. **Sustainability indicators** measure how the environmental or social characteristics promoted by the financial product are attained.
4. MSCI is a financial data provider selected by the Bank.
5. **Principal adverse impacts** are the most significant negative impacts of investment decisions on sustainability factors relating to environmental, social and employee matters, respect for human rights, anti-corruption and anti-bribery matters.

To reflect our clients' preferences more closely, the Bank has divided these indicators into the following four categories:

1. the climate and the environment (e.g. greenhouse gas emissions, the use of fossil fuels, etc.);
2. waste production and the use of water resources (e.g. production of hazardous waste, etc.);
3. the United Nations Global Compact (e.g. human rights abuses, inefficient anti-corruption processes, etc.);
4. social themes and employee rights (e.g. a lack of diversity within businesses).

In its discretionary management, the Bank has implemented an approach that considers all of these categories. For assets in this mandate covered by MSCI ESG Manager (excluding cash and gold), an objective of at least 50% of investments must respect the criteria set by the Bank. This approach aims to ensure that the positions held have lower adverse impacts than the average for market assets and that the portfolio as a whole has a limited adverse impact on environmental and social issues.

More information on this consideration will be disclosed in the periodic reports of the External Funds Mandate. Information on consideration of the principal adverse impacts on sustainability factors will be published and disclosed in the section entitled *"How does this financial product consider principal adverse impacts?"* included in the periodic reports of the External Funds Mandate.

☐ **No**.

4. What investment strategy does this financial product follow?

The Discretionary External Funds Mandate is invested in a selection of high-quality international funds recommended by our analysts. These funds are selected on the basis of a detailed analysis.

Initially, we carry out quantitative analysis to refine the investment universe and identify the funds that offer a good risk/return ratio. We then apply qualitative analysis to understand how the funds work with respect to different factors such as the promoter, their management team, their investment style and investment philosophy. The funds retained, promoted by financially sound specialists in a particular asset class, with a sound financial basis, have a stable management team and approach; they offer a good balance between the expected return and the level of risk accepted. The portfolio is managed on an opportunistic basis by specialists, who adjust its structure based on economic developments.

In addition to these strict selection criteria for the funds, the Discretionary External Funds Mandate is also based on the underlying fundamental principle of diversification (across asset classes, sectors and geographical regions). The portfolio construction process entails combining decorrelated asset classes, so that the total portfolio risk is lower than the sum of the risks of the various assets (or instruments) within it. This serves to minimise the risk per unit of return or maximise the return per unit of risk. We also focus on the relative valuation levels of the various asset classes.

What are the binding elements of the investment strategy[6] used to select the investments to attain each of the environmental or social characteristics promoted by this financial product?

To supplement the ESG approach specific to each of the funds that make up the portfolio, a quantitative approach is also applied to the portfolio as a whole.

– The Bank's aim is for the weighted average MSCI ESG score of the various investments of this portfolio to be A or higher. The Bank also aims for at least 50% of assets to be defined as "responsible", i.e. rated at least BBB on the MSCI ESG Manager scale, this proportion (50%) being determined after excluding out-of-scope assets (cash and gold).
– Assets with a score of CCC may not be held in the External Funds Mandate.
– The Bank aims to have at least 75% of assets (excluding cash and gold) covered by MSCI ESG Manager, to ensure the portfolio is well represented.

This strategy is supplemented by:

– Consideration of the principal adverse impacts based on a definition of restrictive and binding quantitative thresholds.
– The exclusion of assets affected by very severe controversies as defined by MSCI ESG Manager.
– The introduction of and compliance with sector policies (limiting or directly excluding the selection of products linked to certain industries such as coal).

6. The **investment strategy** guides investment decisions based on factors such as investment objectives and risk tolerance.

What is the policy to assess good governance practices[7] of the investee companies?

Assessment of investee companies' good governance practices involves:

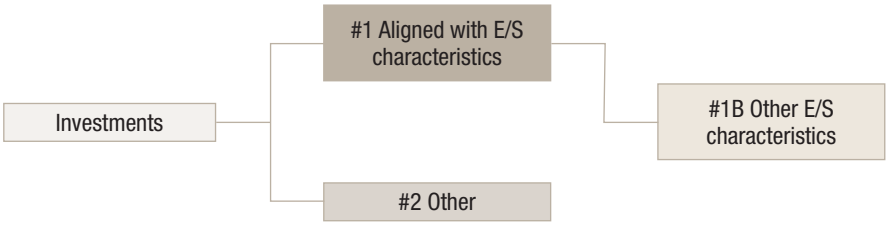
– Monitoring and analysing controversies, especially social. The Bank has implemented an exclusion policy for assets exposed to controversies classified as very severe by our data provider. This monitoring may be supplemented by the Bank's qualitative analysis.

– A quantitative approach based on the ESG ratings for companies provided by our data provider and the exclusion of assets with an MSCI ESG rating of CCC. These ratings are designed to measure the ability of companies to manage the ESG risks and opportunities linked to their businesses and operations. They give an overview of companies' ability to manage resources, including human capital, sustainably, to guarantee operational integrity on the basis of sound management practices, and to comply with relevant standards including tax legislation. An MSCI ESG rating of BB or higher illustrates a company's ability to manage its resources, mitigate the principal risk, seize opportunities, and meet basic corporate governance expectations. The use of MSCI ESG ratings as a basic measure of good governance encompasses four aspects of such practices.

5. What is the asset allocation[8] planned for this financial product?

For the proportion of assets covered by MSCI ESG Manager, the discretionary External Funds Mandate's objective is to have at least 50% of investments aligned with the environmental and social characteristics promoted by the discretionary External Funds Mandate (#1).

The External Funds Mandate's remaining assets (#2) include any cash and gold reserves, as well as investments made for diversification and/or hedging purposes, which may not be considered to promote environmental or social characteristics due to a lack of data from our data supplier, but which – after qualitative analysis by the Bank – respect the restrictive characteristics and features specified for the External Funds Mandate[9].



#1 Aligned with E/S characteristics includes the investments of the financial product used to attain the environmental or social characteristics promoted by the financial product.

#2 Other includes the remaining investments of the financial product which are neither aligned with the environmental or social characteristics, nor are qualified as sustainable investments.

6. To what minimum extent are sustainable investments with an environmental objective aligned with the EU Taxonomy?

This product does not intend to make sustainable investments.

Does the financial product invest in fossil gas and/or nuclear energy related activities that comply with EU Taxonomy [10] ?

☐ **Yes**,

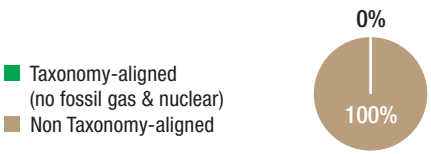
☐ In fossil gas ☐ In nuclear energy

☑ **No**.

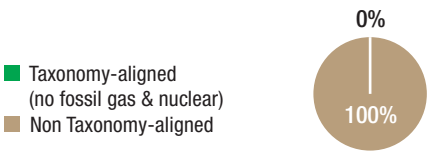
7. **Good governance practices** include sound management structures, employee relations, remuneration of staff and tax compliance.
8. **Asset allocation** describes the share of investments in specific assets.
9. Taxonomy-aligned activities are expressed as a share of:
   – **turnover** reflecting the share of revenue from green activities of investee companies.
   – **capital expenditure** (CapEx) showing the green investments made by investee companies, e.g. for a transition to a green economy.
   – **operational expenditure** (OpEx) reflecting green operational activities of investee companies.
10. Fossil gas and/or nuclear related activities will only comply with the EU Taxonomy where they contribute to limiting climate change ("climate change mitigation") and do not significantly harm any EU Taxonomy objective - see explanatory note. The full criteria for fossil gas nuclear energy economic activities that comply that comply with the EU Taxonomw are laid down in Commission Delegated Regulation (EU) 2022/2014.

The two graphs below show in green the minimum percentage of investments that are aligned with the EU Taxonomy. As there is no appropriate methodology to determine the Taxonomy-alignment of sovereign bonds*, the first graph shows the Taxonomy alignment in relation to all the investments of the financial product including sovereign bonds, while the second graph shows the Taxonomy alignment only in relation to the investments of the financial product other than sovereign bonds.

1. Taxonomy alignment of investments, **including sovereign bonds***



2. Taxonomy alignment of investments, **excluding sovereign bonds***



* For the purpose of these graphs, "sovereign bonds" consist of all sovereign exposures.

What is the minimum share of investments in transitional[11] and enabling[12] activities?

No target for a minimum share of investment in transitional and enabling activities has been chosen for the External Funds Mandate. This position may change over time as the availability and quality of data relating to this alignment improve.

7. What is the minimum share of sustainable investments with an environmental objective that are not aligned with the EU Taxonomy?[13]

This product does not intend to make sustainable investments.

8. What investments are included under "#2 Other", what is their purpose and are there any minimum environmental or social safeguards?

Assets considered in "#2 Other" are assets that cannot be deemed to promote environmental or social characteristics. This category covers assets for which data supplied by MSCI ESG Manager is available and meaningful, and indicates a rating below BBB, or assets for which MSCI ESG Manager provides no data but which respect the binding characteristics and elements defined for the discretionary External Funds Mandate following specific quantitative analysis from an ESG perspective. This category includes any cash and gold reserves, as well as investments made for diversification and/or hedging purposes.

These assets may be included in the managed portfolio to meet performance or risk management targets that the Bank has set, in accordance with the investment strategy followed by the External Funds Mandate.

In all cases, these assets will comply with the following:

– Respect for limitations applicable in virtue of the sector policies implemented by the Bank;

– Exclusion of the environmental and/or social controversies deemed the most severe;

– Consideration of the principal adverse impacts;

– The Bank's qualitative asset selection process for building the managed portfolio.

9. Where can I find more product specific information online?

More product-specific information can be found on the website: www.bdl.lu/Mandat_FondsExternes

11. **Transitional activities** are activities for which low-carbon alternatives are not yet available and among others have greenhouse gas emission levels corresponding to the best performance.

12. **Enabling activities** directly enable other activities to make a substantial contribution to an environmental objective.

13. Are sustainable investments with an environmental objective that **do not take into account the criteria** for environmentally sustainable economic activities under the EU Taxonomy.