Vontobel

Exclusion framework

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Content

Exclusion framework

1. Introduction

This document sets out Vontobel Investments' approach to exclusions. At Vontobel Investments, we incorporate Environmental, Social, and Governance (ESG) considerations into our investment processes to enable our clients to better achieve their investment objectives. One of the tools we employ in this context is the use of exclusions.

As an active investment firm, we believe exclusions should be employed as a final recourse. However, we also recognize their relevance in achieving investment objectives and aligning with the sustainability ambition of our respective strategies. It can help us avoid exposure to companies that may pose financial risks or have significant negative impacts on the environment and society. For example, we may exclude companies at risk of holding stranded assets—assets that have lost value due to changes in market or regulatory conditions. Additionally, we may exclude companies that contribute to adverse sustainability impacts.

To effectively implement this approach, Vontobel has established a minimum exclusion framework structured around three levels:

- **Level 1: Universal Exclusions**
  These exclusions apply across all investment solutions, regardless of their individual sustainability objectives.

- **Level 2: Targeted Exclusions**
  A defined set of exclusions focusing on the most controversial activities and sectors.

- **Level 3: Advanced Exclusions**
  A stricter set of exclusions, including alignment with the requirements outlined by the Paris-Aligned Benchmark regulation, among other high standards. This structured approach allows us to tailor our exclusion approaches to the varying degrees of sustainability integration across our investment solutions.

Detailed information on each exclusion level is provided in Table 1 on page 4.

The term "exclusions" refers to the exclusion of securities or other instruments based on specific factors attributable to the issuer or underlying, such as but not limited to economic activities, business practices, including compliance with certain international norms, and standards. Employing exclusions is a screening approach. As any screening approach, exclusions may lead to the reduction of the investment universe.

2. Three exclusion levels

The table below provides an overview of the exclusions applied by level. Additional information on the individual exclusion categories is available in the subsequent sections of this document.

Table 1 Three levels of Vontobel's exclusion framework[1,2]

EXCLUSION LEVEL		LEVEL 1	LEVEL 2[3]	LEVEL 3[4]
Critical controversies				
International sanctions		✓	✓	✓
Critical ESG Events		✓	✓	✓
Weapons				
Controversial weapons		0%	0%	0%
Nuclear weapons			0%	0%
Conventional weapons				10%
Energy				
Extraction[5]				
Thermal coal			10%	1% and/or expansion projects[6]
Oil sands & Arctic drilling			10%	5%
Oil				10%
Gas				50%
Carbon intensive power generation				
Thermal coal			25% Ⓔ[7]	10%
Other sources of high CO2e intensity power generation[8]				50%
Other controversial activities				
Tobacco	Production		5%	0%
	Distribution		10%	10%
Adult entertainment	Production			10%
	Distribution			10%
Alcohol	Production			10% Ⓔ[9]
	Distribution			10% Ⓔ[9]
Gambling	Operations			10% Ⓔ[9]
Sovereign issuers				
Country exclusion list				✓

[1] The percentages indicated in this table and subsequent pages reflect the threshold of a company's revenues stemming from a certain exclusion category ("revenue threshold"). Companies exceeding such revenue threshold are excluded, for the products falling under the respective exclusion level, unless exceptions are specified. The revenue data typically reflects the latest available percentage of revenue derived from such activity by a company.

[2] "Ⓔ" signalizes that exceptions can apply to this exclusion. These exceptions are detailed in the respective subsequent sections of this document.

[3] This level is aligned with the exclusions set out for the EU Climate Transition Benchmarks (Article 12 EU Regulation for EU Climate Transition Benchmarks and EU Paris-aligned Benchmarks)

[4] This level is aligned with the exclusions set out for the Paris Aligned Benchmarks (Article 12 EU Regulation for EU Climate Transition Benchmarks and EU Paris-aligned Benchmarks)

[5] In this context, the term « extraction » is understood as exploration, mining, extraction, refining or distribution.

[6] Based on Urgewald list. More information can be found under https://www.coalexit.org/

[7] For companies mainly operating in emerging market companies, exceptions can apply considering 'Just transition' aspects. More details can be found in the subsequent sections of this document

[8] Defined as such if power generation has a GHG intensity of more than 100 g CO2 e/kWh

[9] Our approach is guided by nuanced evaluation on a case-by-case basis rather than blanket exclusions. We understand that within these industries, there are varying levels of social and environmental responsibility. Companies engaged in alcohol or gambling may demonstrate responsible practices, including initiatives, policies and campaigns promoting moderation and health. Where this is not the case, or where we are not in a position to conclude such assessment, we apply a 10% revenue threshold related to these activities.

3. Definition related to the exclusion categories

3.1. Exclusions related to critical controversies

3.1.1. International sanctions

Vontobel has put in place policies and procedures to ensure compliance with all relevant international sanctions provisions of Switzerland, the United Nations, the European Union, the United States and the United Kingdom, unless in conflict with local applicable law.[9]

3.1.2. Critical ESG events

Critical controversies, and breaches of international norms and standards (collectively 'Critical ESG Events') are often related to Principal Adverse Sustainability Impacts such as significant negative impact on the environment, forced labor, or child labor. Moreover, these instances can signal insufficient or inefficient management of sustainability risks by a company or a government and excessive harm to the society or the environment, which is beyond the tolerance of many of Vontobel's investors and stakeholders. Accordingly, Vontobel has a process in place for the monitoring of these Critical ESG Events, which applies at Group level.

More information about this process and its scope can be found in our ESG investing and advisory policy under www.vontobel.com/esg-library.

3.2. Exclusions related to weapons

3.2.1. Controversial weapons

Vontobel prohibits investments in companies that manufacture and/or produce controversial weapons. In addition, Vontobel does not provide any investment advice on the securities of these companies to clients. Vontobel considers the following weapon types as controversial weapons:

- Anti-personnel mines (Ottawa Treaty (1997)),
- Cluster munitions (Convention on Cluster Munitions (2008)),
- Chemical weapons (Chemical Weapons Convention (1997)),
- Biological weapons (Biological Weapons Convention (1975)),
- Non-Detectable Fragments (Protocol I of the Convention on Certain Conventional Weapons (1980)),
- Incendiary Weapons (Protocol III of the Convention on Certain Conventional Weapons (1980)), and
- Blinding Laser weapons (Protocol IV of the Convention on Certain Conventional Weapons (1980)).

This exclusion category is part of our approach to the consideration of Principal Adverse Sustainability Impacts indicators related to social matters.

3.2.2. Nuclear weapons

Our Level 2 and 3 exclusion levels entail exclusions for nuclear weapons, which are based on exclusive use. Accordingly, it focuses on manufacturers of warheads and missiles, including assembly and integration; manufacturers of exclusive delivery platforms; based on a 0% revenue threshold.

3.2.3. Conventional weapons

For our products applying "Level 3" exclusions, conventional weapons and related systems and components are excluded with a threshold of 10% revenue exposure. This includes various types of conventional weapons used by the military forces.

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[9] The selling of securities of sanctioned issuers may be restricted, thus divestment may be impossible for an unpredictable period of time.

3.3. Exclusions related to the energy sector

The energy sector encompasses the production, distribution, and consumption of energy, vital for powering various aspects of modern life, sustaining economic activities, powering industries, and enhancing the quality of life. From electricity generation to transportation of fuels, the energy sector plays a pivotal role in economic development and societal progress. Access to reliable and affordable energy sources is crucial for sustaining economic activities, powering industries, and enhancing the quality of life.

While the energy sector is essential, it also raises significant challenges, necessitating careful consideration. These challenges include, among others:

- A consideration of the financial risks and opportunities associated with investments in the energy sector associated with the energy transition;
- An assessment of the negative impacts of companies in the energy sector, e.g. air, soil and water pollution, accidents and greenhouse gas emissions;
- The necessity to apply a considerate approach, by balancing environmental imperatives with societal needs, thus ensuring a Just Transition.

When considering the energy sector, we differentiate between fossil fuel energy sources and their alternatives. Fossil fuels are known as, by far, the source of energy having the highest negative impacts. Transitioning away from fossil fuels presents a great challenge and opportunity at the same time, as they account for about 60% of the world's electricity mix.[10] Accordingly, our exclusion approach concentrates on fossil fuels, namely coal, oil and gas.

These exclusions are a part of our approach in the consideration of Principal Adverse Sustainability Impacts indicators related to greenhouse gas emissions.

3.3.1. Extraction[11]

Thermal coal extraction

Coal stands out as the most carbon-intensive among fossil fuel energy source[12][13], carrying significant financial and regulatory risks. Consequently, it presents the greatest investment risk while considering investments in the energy sector. Among energy sources, coal is associated with the most significant impact in terms of greenhouse gas emissions, accidents, and air pollution. To mitigate these risks, we apply additional exclusions to companies deriving their revenues from coal extraction:

- For our products falling under "Level 2", companies with more than 10% revenues stemming from thermal coal extraction are excluded.
- For our products falling under "Level 3", we apply even stricter thresholds and exclude:
  - Any company that derives more than 1% of its revenues from thermal coal extraction activities;
  - Any company that has expansion plans related to thermal coal, based on the Urgewald coal exit list[14].

Oil and gas extraction

Oil and gas follow coal in terms of carbon intensity, air pollution and accidents.[15] We address exclusions related to oil and gas extractions for our products falling under "Level 3", by excluding any company that derives, respectively more than 10% of its revenues from oil extraction and/or 50% from gas extraction activities.

We also recognize that within oil and gas, the impact of oil sands and arctic drilling can be even more significant. For instance, the generation of artificial heat and pressure needed for these extraction activities requires significant quantities of freshwater, that leads to challenges in both supply and disposal management. These techniques are also frequently employed in the Arctic, a region known for its extreme environmental sensitivity and status as one of the planet's most fragile biological ecosystems. The extreme condition of this region also increases the risk of environmental disasters.[16] Accordingly, investments in companies in such activities are excluded not only for products falling under "Level 3" (5% revenue threshold), but also for products falling under "Level 2" (10% revenue threshold).

[10] Source : https://www.iea.org/data-and-statistics/data-tools/greenhouse-gas-emissions-from-energy-data-explorer, https://ourworldindata.org/safest-sources-of-energy
[11] In this context, the term « extraction » is understood as exploration, mining, extraction, refining or distribution.
[12] Source: https://ourworldindata.org/safest-sources-of-energy
[13] Source: Coal in Net Zero Transitions: Strategies for rapid, secure and people-centred change, International Energy Agency, 2022.
[14] Based on Urgewald list. More information can be found under https://www.coalexit.org/
[15] Source: https://ourworldindata.org/safest-sources-of-energy
[16] Source: Chapter 6 of IPCC Sixth Assessment Report https://www.ipcc.ch/report/ar6/wg3/chapter/chapter-6/

3.3.2. Carbon intensive power generation

Thermal coal power generation
We extend our exclusions to encompass carbon-intensive power generation.

For our products falling under Level 2, we apply a 25% revenue threshold, while some provisions apply for emerging markets. Recognizing the importance of facilitating a fair transition to a low-carbon economy, particularly in emerging markets, we adopt a nuanced approach. Companies operating in these regions face less strict thresholds, considering the unique challenges they encounter in shifting away from thermal coal power generation. Companies with over 25% revenues from thermal coal power generation may still be considered investable if they present an appropriate climate transition plan or operate in areas where alternative electricity access options are limited.

For our products falling under Level 3, we apply stricter thresholds and exclude any company that derives more than 10% of its revenues from thermal coal power generation activities.

Other sources of high CO2e intensity power generation
For our products falling under Level 3, we apply stricter exclusion and exclude any company that derives more than 50% of its revenues from other high CO2e intensity power generation activities (GHG intensity of more than 100 g CO2 e/kWh).

3.4. Exclusion related to other activities

3.4.1. Tobacco

The World Health Organization considers tobacco consumption as “one of the biggest public health threats the world has ever faced”. The financial burdens associated with tobacco consumption are considerable, encompassing substantial healthcare expenses to address tobacco-induced illnesses, alongside the depletion of human potential due to the morbidity and mortality attributed to tobacco use.[17] Apart from the negative impacts on social aspects, the tobacco industry can also present risks for investors, as it became strongly regulated in respect to health impacts, advertising, labeling, distribution, and product ingredients. Over the past few decades, tobacco product manufacturers have faced lawsuits from individuals, governments, corporations, and other groups given the link of tobacco use and cancer as well as other diseases. More recently, vaping and other types of electronic tobacco products are also gaining popularity, especially among adolescents. Regulation around these products is also expected to evolve, as research progresses.

Engaging with the tobacco industry is unlikely to result in significant transformative shifts. Therefore, tobacco related activities are excluded based on pre-defined revenue thresholds. For our financial products falling under Level 2 and 3, we apply a revenue threshold on tobacco producers of 5% (Level 2) and 0% (Level 3) respectively, as well as a 10% revenue threshold on distribution activities (including retail of such products).

3.4.2. Other controversial activities: adult entertainment, alcohol, gambling

We recognize that certain activities may not be compatible with the investment objectives of our products falling under Level 3.

Amongst other, we recognize that adult entertainment can carry social risks. It may also encourage negative behaviors, such as physical and/or emotional distress, and even violence, particularly against women. Accordingly, for our financial products falling under “Level 3”, we exclude companies involved in adult entertainment based on a 10% revenue threshold (both for production and distribution activities).

Alcohol and gambling can be associated with substantial addictions, and thus, social problems. However, we understand that within these industries, there are varying levels of social and environmental responsibility. Accordingly, our approach is guided by nuanced evaluation: We exclude companies involved in alcohol and gambling, based on a 10% revenue threshold (both for production and distribution for alcohol, and operations for gambling), unless the company demonstrates responsible practices, including initiatives, policies and campaigns about moderation, health and the protection of minors.

By following this approach, we aim to ensure that investments of our products falling under Level 3 align with their commitment towards sustainability practices.

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[17] Source: https://www.who.int/news-room/fact-sheets/detail/tobacco

3.5. Exclusions related to sovereigns

For products falling under levels 1 and 2, we adhere to international sanctions lists[18]. This means that we exclude countries listed on these lists.

For products falling under level 3, our exclusion criteria extend beyond international sanctions. We also exclude sovereign bonds of countries that are deemed non-democratic. Non-democratic countries are those where the political system lacks the essential elements of democracy, such as free and fair elections, respect for human rights, and the rule of law. Our preferred source for evaluating the democratic status of countries is Freedom House, a respected organization that provides comprehensive assessments of political rights and civil liberties worldwide.

4. Exclusions related to the application of sustainability product labels

Financial products that carry sustainability labels typically apply additional exclusion criteria, which are detailed under the respective label's website. Specifically, the 'Towards Sustainability' label-details can be found on the website www.towardssustainability.be.

5. Exclusions related to SVVK-ASIR for Swiss domiciled funds

The Swiss Association for Responsible Investments (SVVK-ASIR) is an alliance of major Swiss pension and social security funds. While Vontobel is not a member of SVVK-ASIR, we recognize the relevance of this institution for the Swiss market. Accordingly, our funds domiciled in Switzerland that fall under Level 2 or 3 include the recommendations for exclusion provided by SVVK-ASIR. More information can be found under svvk-asir.ch.

6. Exclusions related to the compliance with the "Do No Significant Harm" principle

Financial products partially or exclusively investing in "sustainable investments"[19] must comply with the "Do No Significant Harm" principle (at least for the sustainable investments' portion in case of partial investments). For the compliance with this principle, we may apply additional exclusions for activities that we consider having significant negative impacts on the environment and/or society.

7. Data and processes related to this exclusion framework

7.1. Data sources

For the implementation of this exclusion framework, Vontobel primarily relies on third-party data providers, such as MSCI and Sustainalytics. The data provided by our third-party data providers may be inaccurate and/or incomplete.[20] Accordingly, we retain the authority to conduct our own assessment on the implication of an issuer in an exclusion category. We will analyze these instances on a case-by-case basis.

7.2. Divestment

Prior to investment, any security is being analyzed based on the applicable exclusion levels described in this document. In case of investment, the applicable exclusion criteria and threshold are monitored on a continuous basis. If an issuer does not comply anymore with these exclusion levels, Vontobel will divest from such an issuer within a reasonable time period after such breach was detected according to dedicated policies, prevailing market conditions and in best interests of the investors. Any stricter local requirements pursuant to the relevant offering documents will be appropriately considered.

[18] More information about the sanction lists we consider can be found under 3.1.1 International sanctions (page 5).
[19] In accordance with Article 2 (17) SFDR

[20] Methodological limits are described under "8. Limitations" (page 8) of this document.

8. Limitations

For certain investment universes, we acknowledge that applying an exclusion threshold may not impact potential investments significantly. A typical example is the exclusion of companies involved in adult entertainment activities. We may still have formalized it as a formal exclusion to reassure our investors that there will be no exposure to such activities for the products falling under the corresponding exclusion levels.

Applying exclusions can lead to a reduction of the investment universe. It may affect the investment performance of a financial product positively or negatively since the execution of the exclusions may result in foregoing opportunities to buy certain securities, and/or selling securities due to their ESG-related characteristics. The fact that an activity is not explicitly mentioned in this exclusion framework does not mean that our investment solutions will actively seek exposure to it.

Methodological limits: In assessing the eligibility of an issuer based on exclusion criteria and/or ESG research, there is a dependence upon information and data from third party ESG data providers, and from issuers, and on internal analyses, which may be based on certain assumptions or hypothesis. The data obtained from third-party data providers or issuers may be incomplete, inaccurate, or unavailable and the assumptions or models on which internal analysis rests may have flaws which render the internal assessment incomplete or inaccurate. As a result, there exists a risk of incorrectly assessing a security or issuer, resulting in the incorrect inclusion or exclusion of a security. Considering that ESG data providers may change the evaluation of issuers or instruments at their discretion and from time to time due to ESG or other factors, updated information on the methodology used by the current ESG data providers can be found on their websites. There is also a risk that Vontobel may not apply the relevant criteria of the sustainability research correctly. Vontobel does not make any representation or warranty, express or implied, with respect to the fairness, correctness, accuracy, reasonableness or completeness of an assessment of sustainability research and the correct execution of the ESG approaches.

9. Scope of application

This exclusion framework applies to Vontobel funds administered by Vontobel Asset Management S.A. (Luxembourg) and Vontobel Fonds Services AG (Switzerland), unless specified differently in their respective product disclosures.

Other financial products managed by Vontobel such as discretionary mandates, will in principle apply Level 1 exclusions[21], and may subscribe to this framework upon agreement with clients.

Certain financial products may apply additional exclusions, for example if they hold a sustainability product label (more details are available in this document in section 4) or if additional local regulatory requirements and/or standards apply.

The exclusions mentioned in this framework focus on all direct investments in securities issued by corporate or sovereign issuers held by a fund. Other exclusions may apply for indirect investments, such as those in target funds. More information can be found in the respective financial product's documentation, e.g. in its pre-contractual disclosures, where applicable.

Our financial products may apply additional filters that lead to further reduction of the investment universe (e.g. screening based on an ESG rating). These are detailed in the respective financial product's documentation, e.g. in its pre-contractual disclosures, as applicable.

[21] Unless client specific provisions apply.

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