



# ESG Engagement Report

Third quarter 2019

## Nordea 1 – North American Stars Equity Fund<sup>1</sup>

The aim of this document is to describe some of the activities that the Responsible Investment (RI) team has done over the last quarter for this specific fund. This tool, therefore, is not meant to be fully comprehensive, but to allow investors to follow-up on the fund's relevant ESG-related issues (Environmental, Social and Governance) and the main activities that the RI team has been involved in.

### Introduction to the STARS concept

Nordea's STARS funds proactively select high-quality ESG companies with the objective to identify tomorrow's winners, which, we believe, will have sustainable business models and the ability to conduct their businesses responsibly in relation to their stakeholders – employees, suppliers, customers, investors and society at large. Nordea's RI team works together with the fund's financial analysts and portfolio managers in order to deliver a solution that is able to:

- **Outperform the benchmark:** creating added value by enhanced long-term returns.<sup>2</sup>
- **Meet Nordea's ESG standards:** analysing each individual stock to ensure that the fund invests only in companies that respect certain ESG criteria. The idea is to invest in leading companies (rated A<sup>3</sup>) or companies with a sufficient rising ESG profile (e.g. rated B<sup>-3</sup> in the case of the Nordea 1 – Global Stars Equity Fund), thus avoiding the laggards (lower rated companies).
- **Active ownership:** proactively engaging companies and encouraging them to improve their management systems, their ESG performance or their reporting, as well as exercising formal rights in the voting resolutions.

### Engagement is key for active ownership

Being part of Nordea's responsible investment policy, the fund excludes companies involved in the production of nuclear

weapons and cluster munitions as well as companies with large exposure to coal mining (>30% revenues). However, excluding a company from our portfolios is always a last resort: the **STARS concept aims for positive selection** with the objective to influence companies to improve their ESG profiles. **Engagement therefore takes a new dimension with the STARS.** It does not only consist of the traditional forms of engagement, like the exercise of voting rights or entering into a dialogue to encourage companies to improve their management systems, their ESG performance or their reporting. When assessing a company's ESG risk profile we also focus on specific themes utilising UN Sustainable Development Goals. Thus, we distinguish two types of engagement:

- **Risk Engagement:** if a company is not managing its material ESG risks well, the RI team engages with the company on the issue. The ESG risks can be company specific or stem from the country in which the company operates or its industry. Violations of international norms and conventions are also addressed under Risk Engagement.
- **SDG Engagement:** conducted with a specific focus on companies' exposure to certain themes, which might represent a significant material risk for the company. **Nordea believes that companies that align their strategies with the UN Sustainable Development Goals (SDGs) will be successful** in the long-term, because they are adjusting to global society's future needs.

**The UN Sustainable Development Goals (SDGs)** cover a broad range of social and economic development issues as part of the 2030 Agenda.

1)With effect as of 19/11/2018 the sub-fund is renamed from Nordea 1 – North American All Cap Fund to Nordea 1 – North American Stars Equity Fund and the investment policy of the sub-fund was modified. 2) There can be no guarantee that this strategy and process will produce the intended results and no guarantee that the strategy will achieve its investment objective. The value of your investment can go up and down, and you could lose some or all of your invested money. 3) ESG rating scale

## Top ESG activities over the quarter

Holding	Current Rating	Proxy Voting <sup>3</sup>	SDG Engagement	Risk Engagement	Activity
Littelfuse	B+	✓	N/A	Labor & Market	Research/Call
Johnson & Johnson	B+	✓	N/A	Product Quality & Marketing	Call/Meeting
AbbVie	A	✓	N/A	Product Quality & Marketing	Research/Call

<sup>3</sup> Proxy voting refers to the last 12 month-period. Generally we vote in annual reports and most of the Annual General Meetings (AGM) which occurs once a year. If there is no vote, it is generally because the fund was not invested at the time when the AGM happened. Please find out more on [nordea.com/sustainability](https://nordea.com/sustainability) or access directly the [voting portal](#).

ESG rating distribution (from best to worst) applicable to this fund:



Sustainable Development Goals (SDG) utilised in this report:



## Rating changes

There were no rating changes during the quarter.

## Main highlights of the ESG activities over the quarter

The following activities have been selected to share with investors some of the highlights of the period. Please note that when engaging with companies, the processes might last for multiple quarters, as such we might not necessarily report on the final decisions.

### AbbVie Inc.

During the quarter we added AbbVie Inc. to the portfolio. The company researches and develops a wide range of pharmaceutical drugs, addressing areas such as immunology, oncology and neuroscience.

The last two years has seen the attention towards the HealthCare sector spike on the back of the opioid epidemic in the United States. Our take is that the opioid crisis is in large part explained by excessive selling practices where volumes dominate "risk adjusted results" – a combination that can tease out bad corporate behavior in even strongly regulated industries – anyone recalls the financial crisis?

Although AbbVie is not involved in the opioid crisis, we believe that the issue has highlighted the importance of understanding a company's culture and incentive structure. We typically place these aspects under our "Business Ethics" pillars within our ESG-research framework. When discussing Business Ethics with AbbVie, we found some promising aspects that are generally aligned with global best practices: the R&D, Commercial and Safety & Control departments are functionally separated with different reporting lines and incentive structures that ensure independence between the different departments. Further, AbbVie was one of the first in the industry to adopt 2015 FDA guidelines of independent internal safety committees. The company's ERM system is verified against international conventions such as ISO & ICFHOTR. Lastly, on a positive note, the 30-60 audits by regulatory agencies in 2018 resulted in

no production stoppages – indicating functioning systems in place.

We also touched on the anti-trust litigation that AbbVie is involved in at present. We believe that the issue is of relatively little material importance and it is too early to comment on that at the time since there are going to be appeals.

All in all, we A/ (flat) rated the company reflecting in part its best practices around the governance structure to tackle the perhaps most material risk; mis-selling, and overall strong policies and procedures in regard to product quality and safety.

### Johnson & Johnson

We had two interactions with Johnson & Johnson during the quarter. The current controversies surrounding the company has probably not evaded anyone within the sustainable investing space. At this point, it is crystal clear that the accountability and responsibility of the opioid crisis will need to be assigned somewhere.

The legal system will play a role into interpreting to what extent industry should be held accountable, in monetary terms, for the opioid crisis. We should be wary of completely discounting the societal backlash the industry is facing on the back of the opioid crisis and what that might add to the health care debate in the United States.

We are aware of the Oklahoma ruling in August, and we will follow the company's appeal closely. Our first discussion with Johnson & Johnson during the quarter concerned primarily governance and related aspects with respect to the company's commercial, R&D and Safety & Quality departments. Here, like with AbbVie, we could not identify anything that would suggest that the overall structure at the company is systematically misaligned with what we would consider best practices.

At the second meeting in London, we discussed the opioid crisis and specifically the ruling. We are still digesting that information in the greater context of the company but at this point we are still not in a position to have a definitive view of how that ruling will impact the rating of Johnson & Johnson. Expect more from us on the company in the upcoming quarters.

## Littelfuse

We met with Littelfuse again this quarter and discussed the company's business plans going forward. Littelfuse sits at a sweet spot in terms of its exposure to the megatrend of 'greening' certain parts of the economy through electrification. The electrical grid, renewable energy and electrical vehicles are the main touch points for the company.

Having gone through a couple of acquisitions and especially the biggest in their history, IXYS Corporation, Littelfuse is going through a consolidation program where the manufacturing capacities are being reallocated to fit with the overall Littelfuse setup. From a labor management perspective, the

manufacturing will move to more challenging countries. But apart from an incident in Mexico, we have not documented any noteworthy incidents that would suggest that the company does not manage this transition appropriately. Further, the company has received recognition for its employee management programs reflected by inclusions in different states' Best Places to Work in.

Even though the automotive sector has seen its fair share of challenges since the beginning of the year, we believe that long-term Littelfuse is going to be positively impacted by for example the emissions regulations in the European Union as it incentivises the transition towards a greener car fleet.

## Complete list of SDGs:



Source: [un.org/development/desa/en/news/sustainable/sustainable-development-goals.html](https://un.org/development/desa/en/news/sustainable/sustainable-development-goals.html)

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