

# M&G Fixed Income’s approach to responsible investment



Contents	
Introduction .....	1
ESG integration.....	1
Engagement.....	2
Screening .....	3
Impact .....	3
Oversight of Responsible Investment .....	3
Disclosure and transparency.....	3

## Introduction

M&G is a long-term investor across both public and private fixed income markets. Our large team of credit analysts enables a bottom-up, credit-driven approach to fixed income investment. Our aim is to provide our clients with superior, long-term risk-adjusted returns driven by an in-depth analysis of all factors that are material to the risk or return of the investments that we make. M&G believes that ESG factors can have a material impact on long-term investment outcomes, so the consideration of such factors forms an important component of our investment process.

## ESG integration

The integration of ESG factors into credit analysis and investment decisions is central to M&G’s approach to responsible investment.

M&G has one of the largest teams of credit analysts in Europe, covering public and private debt, and our investments span a diverse range of fixed income sectors and instrument types. Our analysts assess the relevance of ESG factors to risk and return for the issuers that they cover, and incorporate such factors into their credit analysis where considered material. Investment views are not based on ESG factors in isolation, rather, ESG issues are analysed in conjunction with all other factors that can influence the risk or return of an investment in order to form credit views.

Given the limited upside and potential significant downside of fixed income investments, the focus of our ESG analysis is on understanding downside risks. Since ESG risks often develop over the longer term and given our long-term investment approach, we believe it is essential to integrate ESG issues into our investment process.

Our integrated approach to ESG is applied across all forms of fixed income including corporate bonds, government bonds, securitised debt, real estate debt, infrastructure debt, leveraged finance, direct lending and private placements, although flexibility in the implementation of ESG integration is often required to allow for differences across markets, sectors and instrument types.

The relevance of specific ESG factors to the credit quality of an investment can vary across different industries, countries and issuers.

For example, environmental factors may be extremely important when assessing mining companies, but much less material for financial companies. Or social factors such as labour rights may be particularly important for companies with supply chains in certain emerging markets. However, M&G considers governance factors as particularly important across the wide range of fixed income markets and sectors where we invest.

Characteristics that our analysts would view as indicative of an issuer with effective processes to manage ESG risks include:

- A diverse and effective board
- A culture of disclosure, transparency and accountability
- Remuneration aligned with long-term value
- ESG issues are regularly discussed at board level
- Strong internal controls and risk management
- Full compliance with relevant laws, standards and regulations
- Clear disclosure of environmental and social risks
- Appropriate management of resource use (eg raw materials, energy and water)
- Suitable processes in place to manage waste and minimise pollution and carbon intensity
- Focus on employee welfare, development and retention
- Attention to community relations and stakeholder management
- Appropriate procedures for data protection and cyber-crime reporting
- Appropriate procedures to treat customers fairly
- Attention to ESG issues in the supply chain
- Internal policies covering environmental risks, anti-corruption, anti-bribery, equality and diversity, health and safety, etc and clear evidence of the implementation of these policies.

Issuers that lack many of the above characteristics often face reputational, litigation and regulatory risk, inefficiencies and disruptions to operations – all of which can have a negative impact on credit quality.

While we may use third-party ESG research on occasion to help inform our analysis, we generally prefer to use our own internal resources and expertise to form views on ESG issues and the impact of these issues on our investments.

ESG themes, such as climate change, are considered by our analysts and portfolio managers and reflected in portfolio positions where they have an impact on the credit fundamentals of the borrower.

M&G's credit analysts must ensure that ESG issues are incorporated into their credit views and our portfolio managers must ensure that these credit views (which incorporate ESG considerations) are used when making investment decisions.

ESG factors are often material to the risk or return of fixed income investments, and as such, M&G considers the integration of ESG factors into our investment process as essential to fulfilling our fiduciary duty to clients.

## Engagement

Engagement with issuers is usually undertaken by our credit analyst teams, since they have a clear and detailed understanding of the ESG issues affecting the credit quality of the issuers that they cover. Although bondholders normally have less influence than equity holders when engaging with companies, M&G considers it important to engage with fixed income issuers regarding material ESG issues in order to gain a better understanding of ESG risks, and to encourage improved ESG practices. The additional insight often gained through ESG engagement also better informs our credit views and investment decisions. We prefer to engage on ESG issues directly with an issuer's senior management, and M&G's significant scale in fixed income markets provides us with the necessary access to an issuer's senior management in order to do so. In our private debt business, we are often one of the primary sources of finance for the borrower, which can give us significant access and influence to engage.

M&G also engages on ESG issues with regulators, policy makers and government bodies, both collaboratively and individually, in order to protect and promote our clients' interests. M&G's scale as a fixed income investor often provides the necessary access to engage directly with public bodies, particularly in the UK. Our engagement activities with such bodies can include responding to consultations, collaborating with industry associations and direct dialogue.

In addition, M&G is involved in a number of industry associations and responsible investment initiatives, where we work with others to help develop and promote responsible investment practices across fixed income markets. For example, M&G is a member of the UNPRI Fixed Income Engagement sub-committee, a signatory to the Green Bond Principles, an active partner of the Climate Bond Initiative (CBI), a member of the Global Impact Investing Network (GIIN) and has participated in responsible investment working groups with the Association of British Insurers (ABI) and the Loan Market Association (LMA).

## Screening

Rather than have hard screening rules based on ESG criteria, M&G Fixed Income prefers to integrate ESG issues directly into investment analysis, considering ESG issues in conjunction with all other relevant factors when forming investment views. Also, rather than exclude companies based on ESG screens, M&G generally prefers to engage with companies to encourage better practices, which ultimately will benefit our clients' portfolios and the market as a whole. That being said, we do have one broadly applied ESG screen – our Cluster Munitions Policy prohibits investment in companies involved in the manufacture of cluster munitions across most of our pooled funds. In addition, we also manage some segregated mandates where we apply certain specific ESG screens at the request of the client – such screens are normally country or sector based, for example, excluding companies involved in weapons, alcohol or tobacco. We also offer ESG and impact investment products that apply screening to meet the requirements of investors in these strategies.

## Impact

At M&G we are cognisant of the impact our investments may have on the environment and wider society – both positive and negative – and factor such considerations into our investment analysis where appropriate.

M&G Fixed Income has significant resources and expertise in a range of environmentally or socially beneficial investment areas. For example, we regularly make investments on behalf of our clients in areas including renewable energy, energy efficiency, green buildings, green transport, waste management, social housing, affordable housing, healthcare and education. All such investments must meet our usual requirements for providing appropriate risk-adjusted returns for our clients.

We also manage impact investment strategies for clients who want to achieve clear and measurable positive environmental or social impact in addition to financial returns.

## Oversight of Responsible Investment

The incorporation of ESG into M&G's fixed income investment process is considered the responsibility of all our investment professionals. As such, appropriate consideration of ESG factors is a mandatory objective in the appraisal process for all fixed income credit analysts and portfolio managers. Investment team managers have oversight of ESG incorporation within their respective teams.

The M&G Responsible Investment Advisory Forum (RIAF) has overall responsibility and oversight of ESG practices and responsible investment initiatives across M&G. The RIAF has representatives from each of M&G's key business areas, with two representatives from fixed income – including the Head of Fixed Income.

## Disclosure and transparency

Further details of M&G Fixed Income's responsible investment activities, including case studies, can be found on our responsible investment webpages<sup>1</sup>.

M&G's UNPRI transparency report can be found on the UNPRI website<sup>2</sup>, and our UNPRI assessment scores are provided on the M&G responsible investment webpages<sup>3</sup>.



<sup>1</sup> <http://www.mandg.com/corporate/about-mg/responsible-investment/>

<sup>2</sup> <https://reporting.unpri.org/surveys/PRI-reporting-framework-2017/20D82558-766E-4597-955B-160D36E7D1A2/79894dbc337a40828d895f9402aa63de/html/2/?lang=English&a=1>

<sup>3</sup> <http://www.mandg.com/en/corporate/about-mg/responsible-investment/unpri/>

Issued by M&G Securities Limited, which is authorised and regulated by the Financial Conduct Authority in the UK and its registered office is at Laurence Pountney Hill, London EC4R 0HH. **MAR 18 /273904\_291104**