



PORTFOLIO/METRIX  
Investment Management **by Design**

# UNDERSTANDING THE PMX SUSTAINABLE WORLD PORTFOLIOS

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## UNDERSTANDING THE PMX SUSTAINABLE WORLD PORTFOLIOS

The guide below provides an explanation of the conceptual framework for, and construction of, the PMX Sustainable World Portfolios with the aim of helping advisers to understand which clients they could be suitable for.

### 1. AIM OF THE PMX SUSTAINABLE WORLD PORTFOLIOS

To construct portfolios that behave in a similar risk-controlled manner to the PMX Core Portfolios (and so correspond to PortfolioMetrix Financial Personality Assessment results), but utilise funds which focus on sustainability and positive engagement to drive beneficial social and environmental change.

### 2. KEY FEATURES

- Look to achieve a positive social and environmental impact without sacrificing clients' financial objectives
- Invest in funds that:
  - ◊ Focus on companies that deliver a clear positive net benefit to society and the environment
  - ◊ Focus on sustainability of product, service and business operations when selecting companies to invest in
  - ◊ Seek to improve the behaviour of the companies invested in
  - ◊ Exclude industries and specific companies with negative social or environmental impacts
- Option to achieve cheaper portfolios by tilting towards passive negatively-screened funds, although with the downside of slightly less focus on positive screening and company engagement, and slightly less strict negative screening

*Note: Individual investors will have different concepts about what exactly is beneficial from a societal point of view. The PMX Sustainable World portfolios have been designed to focus on investing in companies widely considered to have positive social attributes and to screen out those widely considered troubling. The expectation is that they could be appropriate for the majority of socially conscious investors looking for multi-asset investments. They will not, however, suit all such investors, and those with more specialist requirements should speak to their financial adviser about alternatives.*

### 3. WHAT DOES SUSTAINABILITY MEAN IN THE CONTEXT OF INVESTING?

Socially conscious investing goes by many names: sustainable investing, ethical investing, ESG (Environmental, Social, Governance) investing, green investing, impact investing or SRI (Socially Responsible Investing). Each of these terms does tend to signify something slightly different, but all mean investing when financial returns are not the sole goal, but rather an objective alongside seeking to avoid doing harm and seeking to actively benefit people and the planet. The Investment Association (IA), the trade body for UK investment managers, uses the term 'Responsible Investment'<sup>1</sup> as the catch-all phrase to encompass all of these approaches, as do we at PortfolioMetrix.

Historically, responsible investment was interpreted and applied narrowly through excluding certain 'problem' stocks such as tobacco companies and armament manufacturers (so called 'negative screening' techniques). Often this sort of investing was referred to as 'Ethical' investing because many of the exclusions were based on the values and beliefs of those investing. Over time, responsible investment evolved more towards so called 'positive investing' – investing in companies with positive social, environmental and governance attributes and actively engaging with companies to improve their policies and practices.

**Currently the IA defines Responsible Investment as being made up of the following main sub-components<sup>2</sup>:**

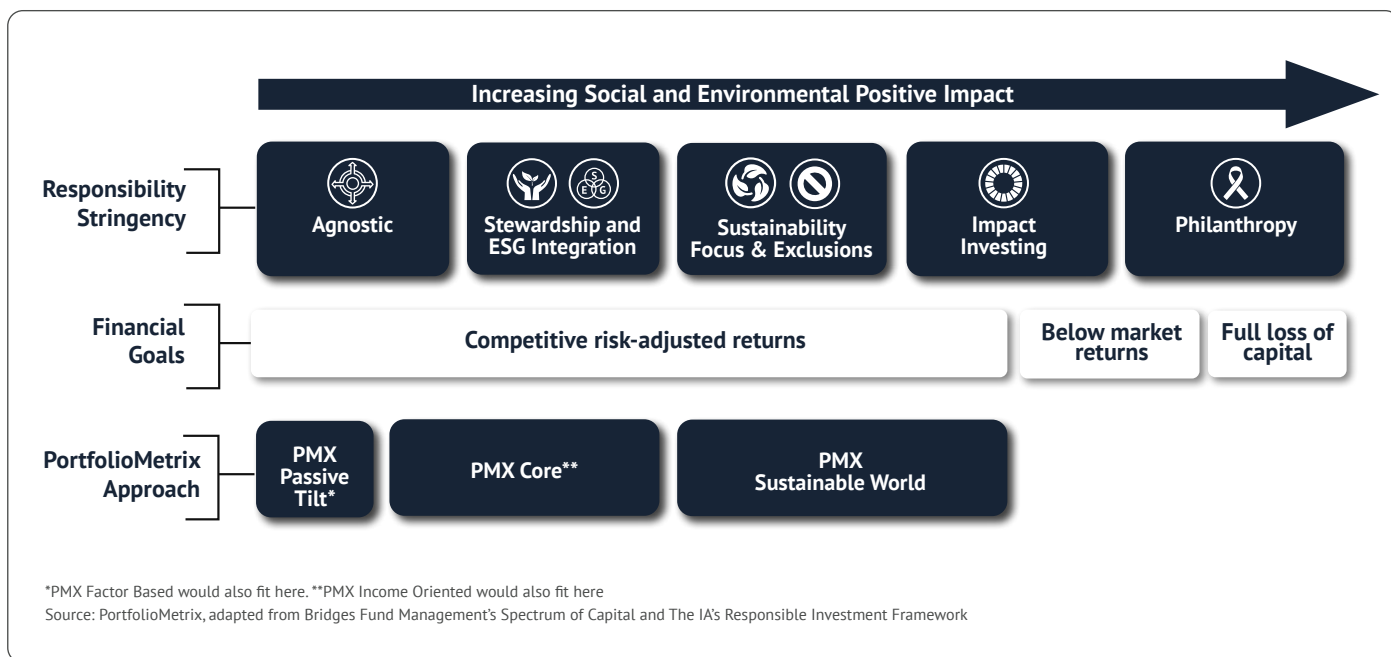
- **ESG Integration:** The systematic and explicit inclusion of material ESG factors into investment analysis and investment decisions
- **Stewardship:** Responsible allocation, management and oversight of capital to create long-term benefits for clients and beneficiaries leading to sustainable benefits for the economy, the environment and society
- **Exclusions:** Investments into certain companies / issuers are prohibited
- **Sustainability Focus:** Approaches that select and include investments based on their fulfilling sustainability criteria and/or delivering on sustainability outcomes with respect to the products/services they produce and how the business runs
- **Impact Investing:** Investments made with the intention to generate positive, measurable social and environmental impact alongside financial return

<sup>1</sup> <https://www.theia.org/sites/default/files/2019-11/20191118-iaresponsibleinvestmentframework.pdf>

<sup>2</sup> The following are abbreviated definitions. For the full ones please see: <https://www.theia.org/sites/default/files/2019-11/20191118-iaresponsibleinvestmentframework.pdf>

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Whilst there is a certain amount of overlap in these 5 components, they can usefully be thought of as lying in a spectrum of increasing positive impact:



As can be seen by the above graphic, within this framework PortfolioMetrix's Sustainable World portfolios are most closely aligned with "Sustainability Focus", aiming to use funds that embrace positive screening and engagement to select companies that achieve a net benefit to society and the environment. Those funds should also incorporate Stewardship and ESG Integration, and where appropriate key exclusions including controversial armaments and tobacco. If possible, impact investing funds will also be used.

## 4. CONSTRUCTION METHODOLOGY

The construction of the PMX Sustainable World portfolios starts with the PMX Core portfolios as a basis, but with the constraint that funds in the portfolio should:

- Focus on companies that deliver a clear positive net benefit to society and the environment
- Focus on sustainability of product, service and operations when selecting companies to invest in
- Seek to improve the behaviour of the companies invested in
- Exclude industries and specific companies with negative social or environmental impacts

In addition to the above criteria, funds must meet PortfolioMetrix's existing financial criteria for selection (coherent philosophy and process, experienced people, a track record of strong performance). We are still aiming to choose funds that will have market to above market risk-adjusted returns.

Using these sorts of funds does require small changes to the asset allocation used in Core, specifically:

- High Yield as an asset class is left out and, in its place, a greater allocation is made to Global Corporate Bonds
- Rather than the six regions for Core, equities are only broken down into three regions: Global Developed Equities, UK Equities and Emerging Market Equities. These asset classes are blended together to mimic the equity asset allocation of Core as closely as possible

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### 5. OVERVIEW OF FUND RESPONSIBLE INVESTMENT CHARACTERISTICS

Using the IA's Responsible Investment Framework, PortfolioMetrix has internally classified each of the funds used in the Sustainable World Portfolios<sup>3</sup> :

Asset Class	Fund Name	Stewardship	ESG Integration	Exclusions*	Sustainability Focus	Impact Investing	Comments
<b>Active Funds</b>							
<b>Cash &amp; Stable Income-Assets</b>	Royal London Enhanced Cash Plus	✓	✓	✓	✗	✗	Exclusions: Tobacco, Armaments, Fossil Fuels
	Royal London Short Duration Gilts	○	○	○	○	○	N/A UK Government Debt Fund
	NN (L) Green Bond Short Duration	✓	✓	✓	✓	✓	Thermal Coal, Oil Sands, Shale Energy, Tobacco, Controversial Weapons, Small Arms, Military Contracting, Gambling, Arctic Oil and Exploration, Fur & Specialty Leather, Adult Entertainment, Nuclear Energy, and Fossil Fuels
	TwentyFour Sustainable Short Term Bond Income	✓	✓	✓	✓	✗	Exclusions: Tobacco, Armaments, Oil & Gas, Adult Entertainment, Carbon Intensive Industries
<b>Global Government Bonds</b>	Wellington Global Impact Bond	✓	✓	✓	✓	✓	Exclusions: Weapons and Fire Arms, Tobacco or Alcohol, Coal, Oil or Nuclear Power, Gambling and Transgenic Food
<b>Global Corporate Bonds</b>	Rathbone Ethical Bond	✓	✓	✓	✗	✗	Exclusions: Tobacco, Armaments, Animal Testing**, Adult Entertainment, Gambling, Alcohol
	PIMCO Climate Bond	✓	✓	✓	✓	✗	Exclusions: Weapons, Tobacco, Adult Entertainment, Coal and Coal Fired Generation, Oil Sands Extraction, Governments Sanctioned by UN Security Council & Violations of UN Global Compact. Plus PIMCO's dynamic exclusions list
<b>Emerging Market Bonds</b>	PIMCO Emerging Markets Bond ESG	✓	✓	✓	✓	✗	Exclusions: Weapons, tobacco, adult entertainment, coal and coal fired generation, oil sands extraction, Governments sanctioned by UN Security Council & Violations of UN Global Compact. Plus PIMCO's dynamic exclusions list
<b>Global Developed Equities</b>	BMO Responsible Global Equity	✓	✓	✓	✓	✗	Exclusions: Tobacco, Armaments, Adult Entertainment, Gambling, Alcohol
	Janus Henderson Global Sustainable Equity	✓	✓	✓	✓	✗	Exclusions: Tobacco, Armaments, Animal Testing**, Adult Entertainment, Gambling, Alcohol, Fossil Fuels
	Montanaro Better World	✓	✓	✓	✓	✓	Exclusions: Tobacco, Alcohol, Weapons, Adult Entertainment, Gambling, High-interest Rate Lending, and Fossil Fuel Exploration and Production
	JOHCM Regnan Global Equity Impact Solutions	✓	✓	✓	✓	✓	Exclusions: Fossil Fuels, Uranium, Tobacco, Weapons & Armaments, Gambling, Adult Entertainment and Alcohol
	Stewart Investors Worldwide Sustainability	✓	✓	○	✓	✗	No explicit exclusions. Undesirable industries / companies avoided as by-product of only investing in companies without controversies
	WHEB Sustainability	✓	✓	○	✓	✓	No explicit exclusions. Undesirable industries / companies avoided as by-product of only investing in companies without controversies
<b>UK Equities</b>	Liontrust Sustainable Future UK Growth	✓	✓	✓	✓	✗	Exclusions: Tobacco, Armaments, Animal Testing**, Adult Entertainment, Gambling, Greenhouse Gases, Fossil Fuels
	Ninety One UK Sustainable Equity	✓	✓	✓	✓	✓	Exclusions: Alcohol, Gambling, Tobacco, Controversial Weapons, Adult Entertainment, and Heavy Extractive Industries
	Royal London Sustainable Leaders Trust	✓	✓	✓	✓	✗	Exclusions: Tobacco, Armaments, Animal Testing**, Adult Entertainment, Gambling, and Alcohol
<b>Emerging Market Equities</b>	Candriam SRI Equity Emerging Markets	✓	✓	✓	✓	✗	Exclusions: Tobacco, Armaments, Adult Entertainment, Gambling, Alcohol
	BMO Responsible Global EM Equity	✓	✓	✓	✓	✗	Exclusions: Tobacco, Armaments, Adult Entertainment, Gambling, Alcohol
	Nomura ACI Emerging Markets Sustainable Impact Equity	✓	✓	✓	✓	✗	Exclusions: Fails UN global Compact, Norwegian Government Pension fund exclusion list, Alcohol, Gambling, Weapons and Adult Entertainment
<b>Global Listed Infrastructure</b>	Foresight Global Real Infrastructure	✓	✓	✓	✓	✗	Exclusions: Violations of UN Global Compact
<b>Global Property</b>	Sarasin Sustainable Global Real Estate Equity	✓	✓	○	✓	✗	No explicit exclusions. Undesirable industries / companies avoided as by-product of only investing in companies without controversies

\* On a complete exclusion basis or in some instances (where the activity is not the main source of company revenue) revenues from the activity are below a small minimum level

\*\* Consumer products, Cosmetics but may include animal testing if required by law - Eg Pharmaceutical company medicine testing

○ Neutral or Not Applicable

<sup>3</sup>The IA is examining introducing its own label for UK responsible investment funds which we will take into account when it becomes available

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Asset Class	Fund Name	Stewardship	ESG Integration	Exclusions*	Sustainability Focus	Impact Investing	Comments
<b>Passive Funds</b>							
<b>Global Developed Equities</b>	Vanguard ESG Developed World All Cap	✓	✗	✓	✗	✗	Fossil Fuels, Nuclear Power, Adult Entertainment, Alcohol, Gambling, Tobacco, Weapons and Controversies based on UN Global Impact
	Dimensional Global Sustainability Core Equity	✓	✓	✓	✗	✗	Exclusions: Tobacco, Armaments
<b>UK Equities</b>	L&G Future World UK Index	✓	✓	✓	✗	✗	Exclusions: Coal Miners, Controversial Weapons Manufacturers & offenders of UN Global Compact Exclusions
<b>Global Emerging Market Equities</b>	Vanguard ESG Emerging Markets All Cap	✓	✗	✓	✗	✗	Exclusions: Fossil Fuels, Nuclear Power, Adult Entertainment, Alcohol, Gambling, Tobacco, Weapons and Controversies based on UN Global Compact

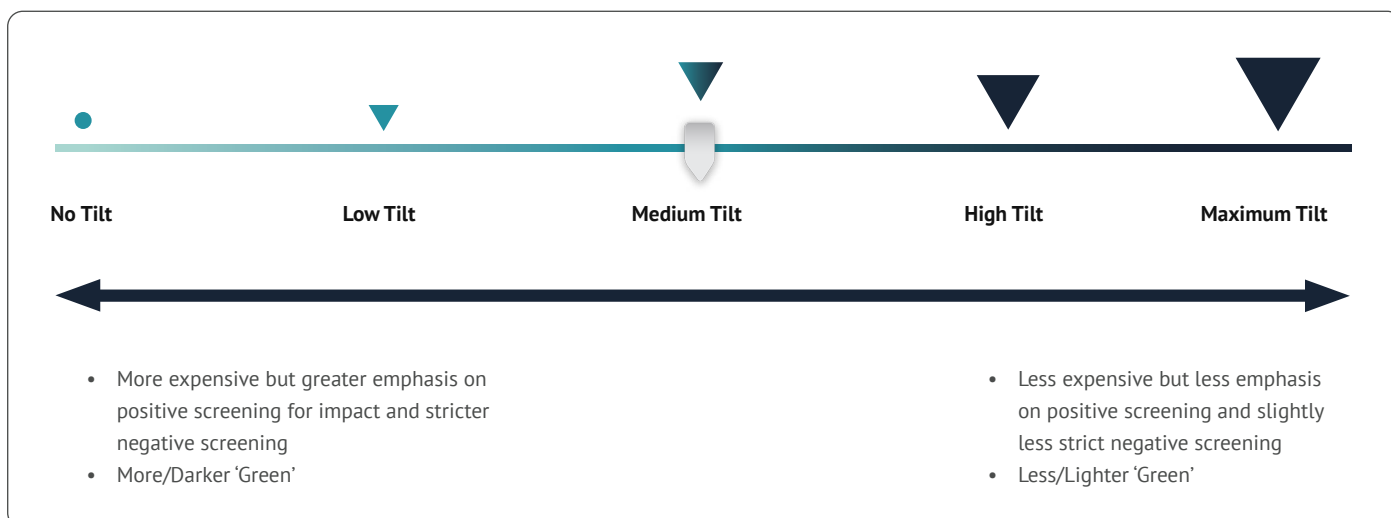
## 6. PASSIVE TILT

Positive screening, the activity of really getting to grips with the social and environmental effects of a business, is a bottom up active research function and so more difficult for a passive fund to undertake. Successful engagement is also arguably easier for an active fund to undertake. Thus, active responsible investment funds have the potential to be 'darker green' than passive funds which are often limited to negative screening.

This is true for the PMX Sustainable World Portfolios, where tilting towards passive includes the Vanguard ESG Developed World All Cap Fund, Dimensional Global Sustainability Core Fund, L&G Future World UK Index and Vanguard ESG Emerging Markets All Cap Fund, which are cheaper, but 'lighter green', alternatives to the active sustainability focused and impact equity fund picks used in No Tilt Sustainable World Portfolios.

Changing passive tilt thus has the following effect in the portfolios:

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