ESG integration in corporate credit

Environmental, social, and governance (ESG) analysis represents an important source of risk and opportunity for investors. Performing a material ESG risk analysis should be considered as essential as other conventional credit research. The following overview outlines the significance of conducting this work, as well as our approach to incorporating ESG risk analysis into Investment Grade Corporate Credit research, decision-making, and monitoring.

The PH&N Corporate Credit team follows a systematic approach to incorporating ESG risk analysis into our decision-making process. The degree to which ESG considerations are integrated into portfolio positioning can be viewed on a spectrum.

ESG integration is the process of incorporating ESG risk analysis into investment decision making. The assessment of material ESG considerations is essential to ensure the review of an issuer is comprehensive and that a company is being evaluated in its entirety. Our team believes that ESG concerns can be just as important as "traditional" measures of corporate health.

ESG screening and exclusion strategies apply positive or negative screens to include or exclude companies from an investable universe. These are mandate-specific restrictions and can include limitations on sectors such as oil & gas or require all holdings to align with best-in-class screening.

Thematic portfolios typically narrow down the investable universe to consist of issuers that align with one or multiple ESG-related themes. For example, an investment mandate may only allow holdings that support clean energy transition or social initiatives, such as housing.

In this paper, we share our perspectives regarding the relevance of ESG for fixed income investors, our philosophy and process for integrating ESG risk analysis, as well as a step-by-step explanation of how we put this approach into practice. As active managers, our fiduciary responsibility to our clients is to maximize investment returns without undue risk of loss. We believe that being an active, engaged, and responsible investor empowers us to enhance the long-term, risk adjusted performance of our clients' portfolios.

ESG within the fixed income context

ESG analysis is the study of ESG practices of an organization in the belief that they may impact the company's financial or operating performance. The degree to which ESG risks are material to a particular security depends on the issuing entity, the industry in which it operates, and the nature of the portfolio for which the security is purchased. The goal is to mitigate downside risks and, in turn, enhance the potential for long-term risk-adjusted performance.

As fixed income investors, our foremost concern with ESG risks is whether they may have an impact on a company's ability to repay its debt. Issuers with higher unmitigated ESG-related risk exposures may face a deterioration in credit quality, which could impact portfolio returns. Ultimately, the angle through which we approach and evaluate ESG is centered on credit risk mitigation.

The materiality of an issuer's ESG risks can depend on the company's unique characteristics, line of business, and other considerations. However, governance risks will often play a critical role regardless of the entity's sector. For corporate issuers, management will need to evaluate how its actions affect all stakeholders. Generally speaking, management that makes poor decisions with respect to financial policy, treatment of capital providers, and corporate structure can affect an issuer's ability to maintain its credit quality. Conversely, companies with strong governance may stand to benefit from a range of potential competitive advantages, including capital cost efficiencies, productivity gains, and new business opportunities.

However, governance decisions made in the best interest of the company can have negative externalities for certain groups while being beneficial to others. Actions typically funded with debt, such as (but not limited to) share buybacks and/or leveraged buyout transactions would be flagged as credit negative from bondholders' perspective. The added leverage could impact the issuer's ability to repay its existing debt or refinance bonds in the future. At the same time, shareholders may welcome and vote in favour of these same actions, especially if they contribute to share price performance. Favourable corporate governance is open to interpretation depending on the investor's position in the capital structure.

Increasing leverage can still make sense if management is attempting to improve the company's operations and competitiveness, while providing clear guidance on how the balance sheet will be considered. Overall, the team favours activities that serve a strategic purpose. We believe that prudent and transparent corporate governance that does not disadvantage bondholders is fundamental to a company's long-term viability and is a critical characteristic the team requires of the issuers in which we invest.

The table below highlights a few examples of features that would typically signal good governance practices to fixed income investors, as well as some potential red flags that would make us exert caution.

Fixed Income investors like to see	Potential red flags for fixed income investors
Prudent balance sheet	Dividends growing at a faster pace than earnings
Management transparency about key business priorities	Share buyback programs
Public commitment to specific leverage metrics and credit ratings	Increasing leverage to support shareholder reward programs
Debt issuance proceeds used towards improving business profile	Executive compensation tied to share performance
Active engagement with investors	Reliance on merger and acquisition (M&A) activity to support growth

Approach to corporate credit analysis

ESG analysis should not be considered in isolation

The PH&N Corporate Credit team analyzes material ESG risks to ensure that our review of an issuer is comprehensive and that a company is being evaluated in its entirety. This research naturally includes ESG considerations to the extent that they reflect the quality and value proposition of an investment. The same approach applies to labelled bonds. For a more detailed overview of labelled bond issuance, please refer to the Labelled Bond Primer published by our team.

Prior to analyzing each credit, we conduct research and analysis at the sector level, which includes an assessment of material ESG risks, themes, and trends affecting that sector. We then complete in-depth fundamental and ESG analysis at the issuer level, gathering information from multiple sources including company publications, management, rating agencies, as well as third-party research. Our main goal is to understand the impact of all material risks on the company's overall sustainability and credit quality.

This analysis forms the basis of a credit report and an internal ESG score, which is used to inform security selection and portfolio management decisions. Risks, including ESG, are then monitored throughout the lifetime of the investment. The purpose of this work is not to capture all business practices that relate to ESG but rather to focus on those that would pose a material risk to credit quality. Issuers contain a multitude of ESG risks and opportunities, however, not all of them will have a substantive influence on a company's operating or financial performance. We prioritize our assessment based on relevance of each risk, regardless of whether the risk is ESG-related or not. As such, when forming our view, we do not arbitrarily assign weights to individual risks by default. Instead, we focus on developing a thorough understanding of each entity in order to determine the most relevant and unmitigated risks associated with a credit.

The diagram below illustrates some of the ESG considerations we may take into account during our due diligence process.

ESG

Environmental

- Does the issuer operate in a carbon-intensive industry with potential for stranded asset risk?
- How is the issuer addressing transition risk?
- Has the issuer been involved in environmental disasters and/or controversies?
- Are the issuer's ESG policies and goals relevant to addressing long-term viability risk to the business model?
- What are the issuer's options and plans with regards to protecting its business against climate change risk?

Social

- Does the issuer have strong labour management practices that would prevent business interruption risk?
- Does the issuer have a good health and safety track record?
- How is the issuer addressing its relationship with and impact on Indigenous communities?
- Are there data privacy, security, and consumer fairness concerns surrounding the issuer or its line of business?
- Does the issuer operate in an industry subject to social, political, and/or regulatory scrutiny?

Governance

- Does the issuer have an independent board structure and experienced management team?
- Does the issuer have a publicly stated financial policy and has it historically adhered to this policy?
- How committed is the issuer to its external credit ratings and is management willing and able to protect them?
- Have management's decisions put bondholders at a disadvantage in the past?
- Is management's compensation heavily tied to equity performance?

Consistent with the key objective of our overall approach to fixed income investing and our fiduciary responsibility – to add value while controlling risk – there are two critical objectives when analyzing ESG as well as other risks:

1. The first objective is to identify the relevant and material risks in order to determine if and to what extent they may jeopardize the viability of a company. For example, it would be imprudent to analyze an oil and gas issuer without examining its environmental impact as well as its plans to address the energy transition and potential stranded asset risk. Analysis of the same risks may not be as relevant to a telecommunications company, which in turn, contains its own set of ESG concerns that need to be addressed. In essence, because there are no blanket ESG criteria that can be applied to all industries and
2. environments, the team's approach to ESG integration is sensitive to the operating framework and business nature germane to an issuer.
3. The second objective is to ensure our clients are being appropriately compensated for having exposure to such risks. Unless prohibited by an investment mandate constraint, the mere presence of an ESG risk would not preclude us from investing in issuers or sectors as long as compensation for that risk is deemed to be adequate.

As the team views credit risk holistically, we might participate in a bond if we feel that the ESG risk is properly mitigated, and that we are being well compensated for the added risk. The below example for Fair Hydro Trust illustrates a combination of significant ESG attributes and when we might participate in a credit when ESG risks are present.

Case Study: Fair Hydro Trust (Internal rating: AAA | Internal ESG rating: 0)

In March 2017, the Province of Ontario announced that it would look to lower average electricity bills by 25%, subsequently passing the Ontario Fair Hydro Plan Act, 2017. The Act reallocated certain electricity infrastructure costs over a 30-year period according to the Fair Allocation Amount and provided immediate rate relief to consumers. Fair Hydro Trust (FHT) was set up to facilitate the funding and execution of the Ontario Fair Hydro Plan. The issuer was 100% owned by Ontario Power Generation, which in turn is 100% owned by the Province of Ontario.

The nature of the plan's structure was unique. Customers would see a 25% discount on their electricity bills, which over time would aggregate to approximately $20 billion.[1] This amount, called the Clean Energy Adjustment (CEA), plus the cost of the program charges would be collected over a period from 2021 to 2047. The bonds came with numerous protection measures, most notably a change of law protection clause. This clause would require the Province of Ontario to make payments with respect to all obligations upon an occurrence of a protection event – for example, a negative legislative amendment. This effectively made FHT a quasi-provincial credit that came at corporate level spreads.

Interestingly, there were distinct ESG considerations. FHT was created for the sole purpose of funding and executing the provincial government's decision to move towards cleaner energy sources. It also came with the social benefit of providing relief to current ratepayers. However, the structure had an intergenerational effect. The CEA as well as the program costs would eventually be borne by future ratepayers. In our view, this increases the risk of generational inequity. For example, the Financial Accountability Office estimated that the net cost to Ontarians could be $21 billion or higher.[2]

Outcome:
In our experience, materiality is important in determining the potential implications of E, S, or G-related risks on a credit. The materiality of an ESG risk will differ sector to sector and issuer to issuer. For example, social concerns may be more prevalent for certain entities. In such instances, we look for strong mitigants that may reduce S-related risks to bondholders. In this case, we were mindful of the negative public sentiment and conscious of the potential social considerations associated with the credit. However, there were sufficient structural protections in place providing coverage in the event of an adverse legislative action. We felt the FHT structure came with a strong covenant package and an attractive risk-reward profile given the quasi-government nature of the credit. As such, we participated in the February 2018 FRHYDR 3.357% 2033 new issue.

[1] Fair Hydro Trust, Investor Presentation, January 22, 2018
[2] An Assessment of the Fiscal Impact of the Province's Fair Hydro Plan, Financial Accountability Office of Ontario, Spring 2017. (www.fao-on.org/)

Disciplined investment process

Our credit analysis process generally involves steps dedicated to research and team discussions that lead to an investment decision, as well as continuous monitoring and engagement. The below graphic illustrates our step-by-step issuer review process.

Analysis:
Conduct comprehensive, in-depth research and fundamental analysis of issuer

ESG scoring & internal credit rating:
Discuss research findings as a team to determine credit quality

Investment decisions:
Make investment decisions based on fundamentals, technicals, and valuations

Monitoring & engagement:
Continuously monitor evolving risk factors. Deepen relationships with issuers though ongoing engagement

Analysis

We begin by examining the company's operating environment and gathering high-level information pertinent to its business model, such as industry characteristics, historical trends, competitive nature, and regulatory landscape. Relevant ESG themes are an important component of this research. The goal is to identify key risks and challenges that could result in material credit implications for the company and the sector in which it operates. We seek to identify such risks through a variety of techniques, which might include but are not limited to:

- identifying operating strengths and weaknesses of the organization and its units;
- analyzing financial statements;
- identifying and assessing material environmental, social, and governance risks;
- assessing history of stakeholder management;
- assessing organizational structure;
- evaluating characteristics and covenants of debt instruments; and
- stress testing key assumptions when appropriate; and assessing credit ratings risk.

The above list is not exhaustive. For example, additional research may need to be undertaken for project finance or structured credit.

We evaluate material ESG risks throughout the course of all our work. Our emphasis is on how ESG factors may impact the company's operating performance, future cash flows, as well as the company's ability to access the capital markets or funding. To complement our internal analysis and deepen our insights, we often incorporate relevant findings from third-party ESG research, rankings, and publications, such as MSCI and Sustainalytics. Engagement with management is at the core of this process as well.

The concluding step of our analysis is to compile all research into a credit report, customized to focus on the areas specific to each sector and issuer. ESG issues can affect different aspects of the business on multiple levels; therefore, while our reports contain a summarized ESG assessment section, we discuss relevant ESG risks throughout the report where it is logical and a natural fit. Only risks expected to materially impact investment fundamentals or an issuer's debt servicing capabilities will influence the team's final internal ESG scoring, internal credit rating, and investment decision.

ESG scoring & internal credit rating

Once all risks have been thoroughly assessed and summarized, we meet to discuss and debate the recommended internal credit and ESG ratings. This occurs on a weekly basis and more frequently if necessary.

During such meetings, team members challenge each other on what is presented in the credit report and draw attention to risks and mitigants that may have been overlooked. Based on extensive discussion of research findings and an open exchange of ideas, we arrive at a final internal ESG score and internal credit rating.

The issuer's internal ESG score is assigned based on our team's ESG Rating Framework. As part of our ESG analysis we consider data and evidence presented by third-party vendors, however, such data can be limited, not relevant, or simply not comprehensive. Further, we feel our direct access to management, where available, allows for better and more transparent communication and clarification of any targets and ESG commitments. The ultimate internal rating decision is independent and remains with the team. Specifically, we have evolved our ESG process to set internal ESG scores on a scale from -1 to +3. For an overview of our ESG Rating Framework for corporate issuers, please refer to Appendix I.

The below case study, Électricité de France Group, illustrates our analysis, ESG scoring, and internal credit rating process, and demonstrates how material ESG risks play a role in our ultimate credit assessment of an issuer.

Case study: Électricité de France Group (EDF) (Internal rating: BB+ | Internal ESG rating: -1)

EDF is one of the largest vertically integrated electric utilities in Europe, providing generation, distribution, and supply services to customers worldwide. EDF is a leading electric utility in France and benefits from geographical diversification, material scale, and having a portion of their business regulated, supporting stable cash flows. The majority of EDF's installed capacity comes from clean energy sources, including nuclear, hydro, and other renewables. With nuclear now being included in the EU taxonomy as a low-carbon power source, EDF is positioned to help France reach its goal of net-zero by 2050.

In July 2022, the French government announced its intent to pursue a tender offer of all outstanding equity securities of EDF, fully nationalizing the company. The transaction closed in May 2023.[3] EDF is considered essential to France and is structurally intertwined with the energy politics of the country.

Our analysis considered ESG risks as well as more "traditional" aspects of credit research, including operating history, free cash flow generation, capital spending, liquidity, use of leverage, and debt covenant strength. We felt that the below risks were material to the long-term profitability and operational success of EDF:

1. Governance concerns over full nationalization

In 2022, the French government sought to subsidize customer bills by capping regulated power prices and forcing EDF to sell more electricity to rivals well below market rates.[4] EDF sought to appeal this to the Conseil d'État (French Administrative Supreme Court) to obtain compensation from this decision but was ultimately rejected in February 2023.[5] The French government's ability to enact such changes raises significant governance concerns, as the state has demonstrated a willingness to implement measures that benefit the public interest at the expense of EDF's financial performance.

2. Stress corrosion detected in several nuclear reactors

Stress corrosion issues in nuclear reactors pose a material concern and require EDF to shut down the reactors for repair and further investigation. According to the Nuclear Safety Authority, which oversees nuclear safety in France, repairing these reactors can be lengthy and complex, and further problems can arise from other reactors throughout the inspections, leading to additional closures. The potential severity of nuclear disasters and the spread of radioactive materials makes safety related to these reactors more material, as any problems could have a significant impact on surrounding populations. Although we view nuclear to be a low-carbon energy source, the social and governance risks associated with EDF overshadow the environmental positives of the credit.

3. Impact from "Accès Régulé à l'Énergie Nucléaire Historique" (ARENH)

The ARENH contract (translated to "regulated access to historic nuclear power"), set up in 2011 and due to end in December 2025, was intended to allow alternative suppliers to purchase electricity from EDF to supply customers at a regulated price and with set quantities. Essentially, ARENH is operating at a structural disadvantage to EDF by limiting the company's capacity to invest and instead subsidizing its competitors.

4. Construction risk for power plant projects

Flamanville 3 is a European Pressurized Water Reactor (EPR) in Flamanville, France that began construction in 2007. Operations were scheduled to start in 2012, but the project has been plagued by a series of cost overruns, component delays, and safety-related issues. The commissioning of the reactor was delayed in 2019, and again in 2022. At the end of 2022, EDF adjusted the schedule for the Flamanville 3 project to be completed in the 1st quarter of 2024.[6] Similarly, the Hinkley Point C (HPC) reactors are two EPR power plants in England, U.K. that began construction in March 2017. This project has also experienced several delays, partially from the COVID-19 pandemic, that resulted in significant cost overruns.

Nuclear power plant construction is complex, and the long construction phases impact the company's profitability as cash flow generation doesn't start until the plant is operational. EDF is looking to build at least six (and up to potentially 14) new EPRs by 2050, starting in 2028, with the first commissioning expected to come in 2035. This poses significant medium-to-long-term risk given the construction headwinds that EDF has faced to date.

[3] EDF, 2022 Tender Offer (www.edf.fr/)
[4] Reuters, France Caps Energy Price Increase at 15%, September 14, 2002 (www.reuters.com/)
[5] EDF, Decision of the Conseil d'Etat on the Appeal Concerning the Cancellation of the Allocation of 20TWh of Electricity Additional ARENH for 2022 (www.edf.fr)
[6] EDF Group 2022 Consolidated Financial Statements(www.edf.fr/)

5. Elevated capital spending program
In conjunction with the construction risk associated with new power plant projects, EDF's elevated capital spending program to maintain and enhance its distribution network and nuclear fleet in France is likely to lead to negative free cash flow in the coming years. This could result in EDF drawing from its cash reserves and the need for additional financing outside of their asset disposal program.

Outcome:
These embedded risks led our team to assign an internal rating of BB+, and an ESG rating of -1. This rating is lower than S&P's BBB and Moody's Baa1 ratings as of December 31, 2023.

Investment decision

An investment decision within a portfolio cannot be made on the basis of fundamentals alone and requires us to consider valuations and technical analysis. We must also examine a security's relative value versus other investment options, whether in the same sector or another. Combining all of the information from our comprehensive research and analysis, the final step is to make an investment decision. It is worth noting that mandates with ESG screening, exclusions, thematic, or impact requirements will be managed in accordance with specific guidelines that may restrict their investable universe in order to align with clients' values and beliefs.

Monitoring

Our team monitors issuers on an ongoing basis and continuously assesses risks as they evolve. This naturally includes ESG concerns. Over time and as developments unfold, we may revisit the issuer's credit rating and/or investment decision to review original assumptions and determine whether we over- or underestimated certain risks versus what actually occurred. This could result in us revising our original conclusions.

Engagement

According to the CFA Institute, “Engagement is the way in which investors put into effect their stewardship responsibilities and is described as purposeful dialogue with a specific objective in mind. The purpose may vary from engagement to engagement, but often relates to improving companies’ business practices, especially in relation to the management of ESG issues.”[7]

Engagement with the company’s management team is an important part of our investment process and is an essential tool for deepening our team’s relationship with issuers. It provides an opportunity to communicate our feedback and encourage management to address ESG-related risks for applicable issuers. We meet and speak with senior management on a regular basis to enhance the impact of our research on the company’s ESG risk mitigation strategies and practices. Given the PH&N Fixed Income team’s size and industry position, our team typically has direct and timely access to relevant management teams to make inquiries and voice our opinions. We do not restrict our engagement efforts to the time of new issue or the refinancing of an upcoming maturity. Instead, engagement is done at the initial analysis stage as well as through ongoing monitoring. As with any risk assessment tool, if any new information is deemed to materially impact the credit profile of a company, our team reviews the internal ESG and credit ratings on a case-by-case basis. Engagement efforts can be largely classified into three categories:

1. An opportunity to understand management’s awareness and mitigation of ESG risks. If an issuer has a publicly disclosed ESG strategy, engagement can be used to confirm the quality of the company’s public ESG efforts and if applicable, the relevance of a labelled bond program. For example, an issuer purchasing carbon offsets located far from where its own physical emissions take place may not be in alignment with the spirit of their ESG strategy. Engagement is critical to shedding light on discrepancies between well-presented and polished external ESG materials and actual views and activities of management teams.
2. An opportunity to provide feedback and encourage mitigation strategies to address material ESG risks. This can include but is not limited to discussions on stranded asset risks, regulatory compliance, and setting of prudent financial policies. Our team’s ongoing issuer engagement allows us to check in with management on a regular basis to evaluate progress, identify deviations, and hold management accountable to previously made commitments. Using the example in the bullet above, we could suggest that management amend their carbon offset program to reduce greenwashing risk.
3. An opportunity to provide guidance on labelled new issuance. We have been part of numerous discussions with dealers and companies to provide our views on new and existing labelled bond frameworks or to encourage issuers to consider labelled instruments as part of their overall financing strategy.

Some examples of engagement efforts we’ve undertaken include:

- encouraging management to increase capital allocation to nuclear and renewable energy assets, protecting against transition risks;
- recommending changes to capital allocation, leverage, and debt structuring;
- suggesting betterment of corporate policies to mitigate ESG and other fundamental risks;
- encouraging public disclosure of balance sheet management policies;
- supporting improvements to transparency;
- urging issuers to pursue additional credit ratings;
- questioning dividend and capital allocation policies; and
- encouraging labelled bond issuance, where appropriate.

[7] Certificate in ESG Investing Curriculum, Edition 3, CFA Society of the UK, 2021

Case Study: Hydro One Inc. (Internal rating: AA- | Internal ESG rating +2)

Hydro One Inc. (HOI) is the largest electricity transmission and distribution company in Ontario, serving ~1.5 million customers through approximately 30,000 circuit KMs of transmission lines and 125,000 circuit KMs of distribution lines. HOI operates under its parent holding company Hydro One Ltd. (HOL). 99% of overall revenues are fully rate-regulated by the Ontario Energy Board (OEB), with HOI accounting for 92% of Ontario's transmission capacity.[8]

The issuer operates in the regulated electricity distribution and transmission segments, which are determined to be 96% carbon emission-free by the Canadian Energy Regulator. Further, over 90% of the electricity generated in Ontario comes from non-emitting sources.[9] Management is committed to improve on all three ESG fronts and has been producing an annual sustainability report since 2018. In January 2022, HOL made amendments to its syndicated lines of credit to incorporate ESG targets that adjust HOL's cost of funding based on certain sustainability performance measures related to converting gas powered vehicles to EV, Indigenous procurement spending, and achieving 30% female executives and board members.

Hydro One is ~47.2% owned by the Province of Ontario. Under the Electricity Act, 1998 (Ontario), the province must retain 40% equity interest in HOL and has the option to acquire up to 45% of certain new issues of voting securities. In 2018, Hydro One experienced a rather turbulent time between its management team and the Province of Ontario leadership. As a result of these events, Hydro One emerged with what we feel are stronger governance controls and an improved regulatory relationship with the province.

Hydro One is one of the largest issuers in the Canadian utility space. We felt that given its electricity distribution and transmission assets, efforts develop stronger relationships with Indigenous communities, robust governance profile, and ongoing work to assist in Ontario's energy transition provide a strong rationale for an active labelled bond program. Starting in 2022, we proactively reached out to management to discuss the possibility of launching a labelled bond framework. During our calls we went over whether use of proceeds or key performance indictor style labelled issuance would be most appropriate, whether green or sustainable frameworks would be a better fit, and our views on the presence of nuclear power generation in the Ontario grid.

Outcome:

We are cognizant that our efforts may be only one part of why an issuer chooses to make changes to its financial policy approach. However, we feel that our support for HOI's labelled bond program provided some level of comfort for management to launch their inaugural labelled bond offering in 2023. At the time of writing, HOI has five labelled securities outstanding, some of which we own in our clients' portfolios.

Conclusion

The PH&N Corporate Credit team is committed to maintaining the highest standards of credit research and active ownership in order to fulfill our fiduciary duty to clients. We strive to identify, understand, and analyze material risks and opportunities to inform our investment decisions. The integration of material ESG factors is an important part of this approach.

The growth in attention given to ESG reporting is a positive step forward for the investment industry, as it encourages companies to be more transparent and communicative with the investing public. The team welcomes the additional disclosure and resources that are becoming available as a result and will continue to stay at the forefront of major developments in this area to reinforce our knowledge for the benefit of our clients.

[8] Hydro One, 2022 Annual Report (www.hydroone.com/)
[9] Hydro One, 2023 Sustainable Financing Framework (www.hydroone.com/)

Appendix I: ESG Rating Framework

Rating	PH&N Investment Grade Corporate Credit Rating Guidance
3	Issuer is exclusively engaged in activities that include but are not limited to the provision of housing, education, healthcare, renewable energy, and other types of social infrastructure. The services will often contribute positively towards sustainable development objectives. The issuer has not been associated with past ESG controversies. There is a low probability that its activities could generate ESG controversies going forward.
2	Issuer operates in an industry that has low ESG risks. In addition, management makes substantial effort to further mitigate its exposure to ESG risks. While the presence of a green or sustainable bond program could be considered a positive, the analyst will evaluate the strength of the framework and ultimate use of proceeds.
1	Issuer operates in an industry that may be exposed to medium or low ESG risks. For medium-risk sectors, management is proactively addressing its business profile to significantly reduce downside risks. Presence of sustainability reporting, policies, disclosures, and generic commitments is not enough to demonstrate significant risk mitigation.
0	Issuer operates in an industry with medium exposure to ESG tail risks. While management may demonstrate awareness and action towards mitigation, they are unable to meaningfully lower the risk profile.
-1	Issuer operates in a sector that is exposed to significant ESG risks. Management actions and approach are deemed inadequate in attempting to address or minimize such risks. Rating may be assigned based on severe governance concerns for issuers in other sectors.

This document has been provided by PH&N Institutional for information purposes only and may not be reproduced, distributed or published without the written consent of PH&N Institutional. It is not intended to provide professional advice and should not be relied upon in that regard.

PH&N Institutional takes reasonable steps to provide up-to-date, accurate and reliable information, and believes the information to be so when printed. The views and opinions expressed herein are those of PH&N Institutional as of the publication date and are subject to change without notice. This information is not intended to be an offer or solicitation to buy or sell securities or to participate in or subscribe for any service.

Information obtained from third parties is believed to be reliable, but no representation or warranty, express or implied, is made by PH&N Institutional, its affiliates or any other person as to its accuracy, completeness or correctness. We assume no responsibility for any errors or omissions.

PH&N Institutional is the institutional business division of RBC Global Asset Management Inc. Phillips, Hager & North Investment Management is a division of RBC Global Asset Management Inc. RBC Global Asset Management Inc. is an indirect, wholly-owned subsidiary of Royal Bank of Canada.

®/™ Trademark(s) of Royal Bank of Canada. Used under licence.
© RBC Global Asset Management Inc., 2024

IC2401120 (09/2024)

019PIM127 (09-2024) ESG ANALYSIS AND INTEGRATION EN V1 ACC 09/06/2024