



# Fund Portrait



## Nordea 1 – Emerging Stars Local Bond Fund

ISIN: LU1160612526 (BP-USD) / LU1160610405 (BI-USD)

### Highlights

- **A modern EMD team**, applying **full ESG integration** coupled with quantitative screening and risk budgeting techniques relying on economic fundamental and credit analysis contributing to the success of investors over the long term in the EM Debt with a **strong proprietary ESG scoring model**
- **Proactive engagement** through dialogues around specific ESG topics to foster change and encourage countries to improve their overall ESG performance



### Asset Management at Nordea

As an active investment manager, Nordea Asset Management (NAM) manages asset classes across the full investment spectrum and aims to serve its clients in every market condition. Nordea's success is based on a sustainable and unique multi-boutique approach that combines the expertise of specialized internal boutiques with exclusive external competences allowing us to deliver alpha in a stable way for the benefit of our clients.<sup>1</sup>

While the first EMD strategy within NAM was launched in 2012, the Nordea Emerging Market Debt has been created in 2016 to solely focus on this asset class. **Thede Rüst was appointed Head of the EMD team** with mission to build a modern EMD team, with full ESG integration and quantitative investment and risk budgeting techniques relying on economic fundamental and credit analysis in the Emerging Market Debt universe.

In 2015, the **Nordea 1 – Emerging Stars Local Bond Fund**<sup>2</sup> was launched – a true ESG solution within the ESG STARS product range with a complete ESG approach, strong emphasis on improving ESG profiles and exploiting sustainability trends. The team has **fully integrated ESG activities** within the investment process, complemented by the Nordea Responsible Investment team ("RI team"). This solution offers a consistent, disciplined investment process, **delivering returns with responsibility** by an experienced investment team<sup>1</sup>. **Thorben Velling** is the Lead Portfolio Manager of the Nordea 1 – Emerging Stars Local Bond Fund since inception.

### The ESG STARS concept

We at NAM consider it our **fiduciary duty** to care about all factors that are material to our clients' investments, **whether financial or non-financial**: responsible investing is part of this. At the Nordea corporate level, we have defined sustainability-related eligibility criteria that apply to all our active funds. We do not, for instance, invest in companies involved in the production of illegal or nuclear weapons or that make more than 10% of their revenues from oil sand. We also exclude companies with large and sustained exposure to coal mining, with a 10% revenue threshold on thermal coal and a 30% revenue threshold on total coal (including metallurgical coal). However, beyond these corporate exclusions, we have developed a **specific range of cuttingedge products** that takes Responsible Investment ("RI") to the next level. We call these the ESG STARS funds.

The **Nordea 1 – Emerging Stars Local Bond Fund** is an ESG STARS fund and has the following objectives:

- **Outperform the benchmark:** alpha generation is a core part of the fund's value proposition. We aim to deliver long-term sustainable returns and responsibility with true ESG integration<sup>1</sup>
- **Invest in countries living up to ESG standards:** we conduct in-depth ESG analysis and ensure that the fund invests only in countries that meet our ESG criteria; and

<sup>1</sup>) There can be no warranty that an investment objective, targeted returns and results of an investment structure is achieved. The value of your investment can go up and down, and you could lose some or all of your invested money.

- **Create impact:** we influence and foster change by proactively engaging in dialogues around specific ESG topics and encouraging countries to improve their overall ESG performance



The fund also complies with Nordea Sensitive Industries Guidelines and the NAM Fossil Fuel Policy, both available at NAM website.

## Investing in Emerging Market Debt

The EM Debt asset class has come a long way. Over the last three decades, it has matured and today it is part of the asset allocation of many investors. The **diversity of EM Debt** – +60 countries – comes with an **extra layer of challenges**. While investors are used to manage a limited amount of financial variables – such as yield, maturity, rating, etc. – when going into more traditional fixed income asset classes, **investing in EMD requires a more comprehensive set of skills**. EMD investors normally combine those quantitative financial variables with a more qualitative – often political assessment.

At NAM, we believe **adding our ESG expertise** in this investment universe will contribute to the **success of investors over the long term**. While we seek to select the **best performing countries** in terms of ESG, we also invest and engage in **countries with an improvement in ESG trajectory** and exclude the countries with poor ESG performance. Combined with traditional financial modelling, this selection process leads us to a portfolio that looks very different from the benchmark from a risk perspective.

## Investment Philosophy

Nordea’s EMD team believes that **ESG factors have an impact on sovereign credit risk** and that ESG risks in EM can be higher than in more developed markets. Our investment style is long term value driven, as we believe that we can identify credits where the future development of structural features, cyclical economic variables or politics, warrant a risk premium that deviates from the market spread. Whilst seeking these bottom-up fundamental value opportunities, we monitor our top-down risk and exposures to global factors.

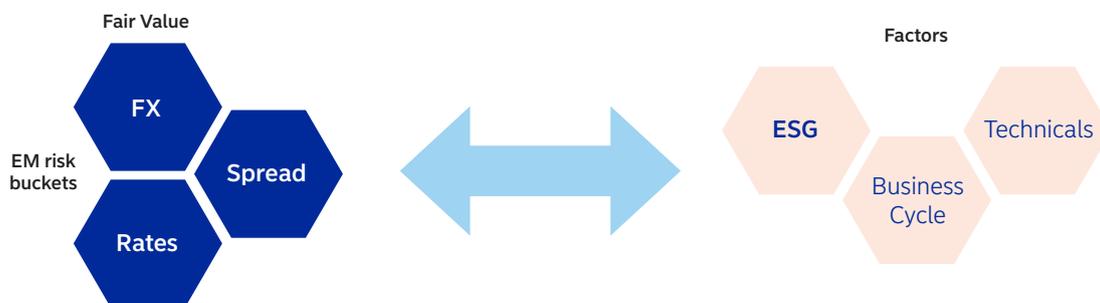
We take **both an economic fundamental and quantitative approach** into investing in EM Debt. We operate within a disciplined portfolio construction process seeking diversification and implement our strategies with balanced risk contribution **avoiding risk concentrations** to offer attractive risk-adjusted returns.<sup>2</sup> We attach a high value to documenting our trading activities allowing us to learn and grow as investors. We take a **team-based approach** and operate in a collaborative culture with clear definitions of roles and responsibilities.

## Investment process

The investment process consists of a **bottom-up fundamental view with a top-down overlay**. The fundamental bottom-up investment process starts with the establishment of **fair value** across the EMD main risk buckets: FX, Rates and Spreads. We

## Investment Process: Alpha Sources

ESG is seriously taken into consideration in our active positioning



Source: Nordea Investment Management AB. There can be no warranty that an investment objective, targeted returns and results of an investment structure is achieved. The value of your investment can go up and down, and you could lose some or all of your invested money.

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apply quantitative screens and tools that enable us to establish if a bond or a currency is over or under-priced. After having established fair values we focus our analysis on the (i) **ESG profile and structural potential of a country's economy**; (ii) **where an economy is situated in its business cycle**; and (ii) **technical factors**. Top-down and bottom-up analysis are **integrated** to generate the portfolio construction with a risk framework that enables the team to constantly monitor the sizing of the positions relying on proprietary risk management tools, as well as, third party provided tools.

## Fully integrated ESG Analysis

We rank the issuers into three categories:

- A. Investable:** issuers within this category are in principal judged to be investable. The EMD team conducts a qualitative review of the individual questions identifying ESG issues / risks that we can identify beyond what is included in the data driven approach.
- B. Investable only when an improving ESG trend can be established:** investments in issuers within this category can only take place when the EMD team judges the country to be on an improving or neutral ESG trend – as such avoiding issuers that are ESG wise getting worse off. The reasons for doing so is that the issuers are already judged to have a so high ESG risk that we question whether one as a medium to long-term investor will benefit from inclusion into the portfolio.
- C. Non-investable:** the issuers in the non-investable category are excluded from the portfolio.

E	S	G
<ul style="list-style-type: none"> <li>• Transitioning Economy</li> <li>• Climate Change Exposure</li> <li>• Environment</li> </ul>	<ul style="list-style-type: none"> <li>• Education</li> <li>• Health</li> <li>• Innovation and Productivity</li> <li>• Digital Inclusion</li> </ul>	<ul style="list-style-type: none"> <li>• Democratic Governance</li> <li>• Government Stability</li> <li>• Judicial Independence</li> <li>• Judicial Effectiveness</li> <li>• Corruption</li> <li>• Ease of Doing Business</li> </ul>

The issuer's classification is conducted taking into account **qualitative measures** with a **quantitative overlay** involving both the EMD team as well as the RI team. We include **discretionary judgement** into our assessment of investments. Our EMD sovereign ESG scoring model is the **starting point** to the responsible investment approach. This model was developed **based on academic research** describing the relationship between **sovereign spreads and ESG factors**. Our strategy is to assign numerical values to individual ESG factors that have proven to have a **material impact on sovereign spreads** – based on ESG scores that we are able to retrieve from third party data providers. The aggregation of these scores allows us to constitute a **proprietary ESG score on every country within the EMD universe**.

## Engagement

Engagement is a key part of the ESG STARS concept. Engagement means having a constructive dialogue with the issuers whose bonds we invest in or are considering for investment. We see engagement as a way to preserve and enhance long-term shareholder value, as well as create a positive impact for the broader society. As the fund invests heavily in Sovereigns bonds, the investment team does not hesitate to approach various governments to incentivize ESG enhancements. The team prefers to engage with sovereigns over ESG issues that arise and works with them to advance their ESG practices, using exclusion as a last resort. When there is no response from governments and where relevant ESG risks are present, the EMD team can freeze the investments in those countries. Depending on the situation the team either does not invest or will withdraw the investment if there is no improvement in the situation. We believe a collaborative approach is most impactful when engaging with sovereign issuers.

## Unique approach with full ESG integration

The Nordea 1 – Emerging Stars Local Bond Fund is a **true ESG solution** within the STARS product range, with complete ESG integration in the investment process, strong emphasis on improving ESG profiles and exploiting sustainability trends. The expert ESG knowledge within the investment team is complemented by Nordea's RIT. We offer a **consistent, disciplined ESG integrated investment process, delivering returns with responsibility** by an experienced investment team with asset class and regional EM focus<sup>3</sup>:

- **Specialists in portfolio management, economics and EM country research analysts** provide ability to nimbly **extract alpha from numerous sources** with focus on ESG & sustainability integration<sup>3</sup>
- The fund incorporates **qualitative and quantitative investment techniques** into the investment process because the combination of the two has been a better indicator for future performance than either qualitative or quantitative alone
- A **well-resourced investment team** that was purposefully set-up to manage ESG-integrated; ESG is not an add-on to existing processes or products but in the DNA of the investment team
- The investment team closely co-operates with one of the **largest and most accomplished responsible investment teams** in the world
- The investment team is **directly involved in various ESG and sustainable related organisations**, including but not limited to the United Nations Principles for Responsible Investment ("PRI"), Emerging Markets Investor Alliance and SDGs initiative

<sup>3</sup>) There can be no warranty that an investment objective, targeted returns and results of an investment structure is achieved. The value of your investment can go up and down, and you could lose some or all of your invested money.

Nordea 1 – Emerging Stars Local Bond Fund	
Fund manager	Nordea Emerging Markets Debt Team
Fund domicile	Luxembourg
ISIN codes*	LU1160612526 (BP-USD) LU1160610405 (BI-USD)
Annual management fees	1.00% (BP-USD) 0.60% (BI-USD)
Base currency	USD
Reference index	JP Morgan GBI Emerging Market Global Diversified
Launch date	26.10.2015

## Risks

Please be aware that there are risks associated with investing in this sub-fund, amongst others in: **ABS/MBS, Country risk — China, Credit, Derivatives, Emerging and frontier markets, Prepayment and extension, Securities handling, Taxation.** For further details, please refer to the Key Investor Information Document, which is available as described in the disclaimer at the end of this document.

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