AIM Affirmative Investment Management | MetLife Investment Management

LO-Funds – Global Climate Bond

Quarterly portfolio impact update Q1 2024

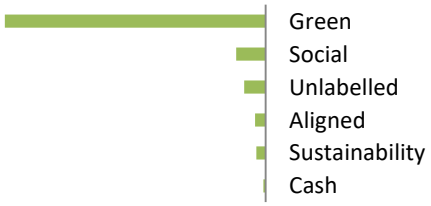
Impact reporting

At MIM, in accordance with issuers annual reporting cycles, we produce our comprehensive annual Impact Reports which detail the environmental and social impacts of our portfolios based on project level data collected by our engagement with issuers. The following quarterly update is a forward-looking snapshot showing selected expected impacts of the portfolio based on the information provided at issuance.

This year we continue to innovate and bring new reporting elements, one of which being a thematic engagement focusing on biodiversity. Although a relatively small proportion of green bond use of proceeds are dedicated to protecting or restoring biodiversity, many projects and assets include biodiversity management in their operations. Examples include infrastructure projects such as electricity grids and railways which own large areas of land. Last September, the Taskforce on Nature-related Financial Disclosure (TNFD) published its final recommendations setting out 14 core global indicators related to the risks and opportunities of nature as well as the dependencies and impacts on nature. We anticipate that there will be an increasing focus on biodiversity in the market as companies begin to implement the TNFD recommendations. With this in mind, we plan to engage with a targeted set of issuers regarding their policies and disclosure in the context of the TNFD update and advocate for best practice disclosure.

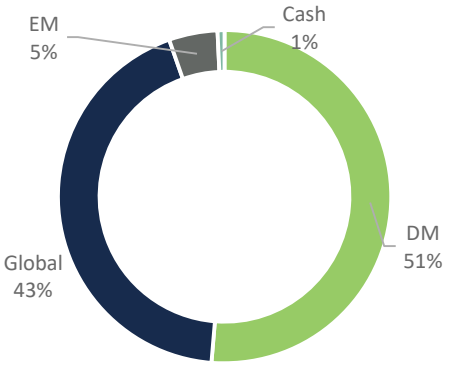
Distribution by bond type

(% of portfolio holdings YTD to 31st March 2024)



Expected project Geographic distribution

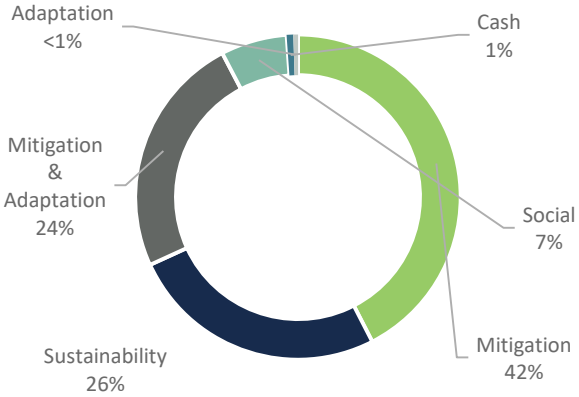
(% of portfolio holdings YTD 31 March 2024



The fund is invested in impact bonds across geographically diverse areas, including developed market focussed issuers such as NWB Bank Green Bond, the Dutch sustainable water bank, and Asian Development Bank Green Bond, which invests in emerging markets across Asia.

Expected project Impact goal distribution

(% of portfolio holdings YTD 31 March 2024)



Reflecting the heavy concentration of the portfolio in green bonds (78%), the majority of the portfolio supports climate change mitigation and adaptation, most closely related to SDG 7 - affordable and clean energy, SDG 9 - industry, innovation and infrastructure, SDG 11 – sustainable cities and communities and SDG 13 - climate action.

Note: charts may not add to 100% due to rounding.

Impact bond highlight

Bank of America

Framework Excluded from our universe and sold

Moody's: A1
Fitch: A-

Verification process overview

The SPECTRUM process is primarily one of positive selection, a judgement based and forward-looking approach. It involves a detailed assessment to understand the investment's environmental, social and governance performance alongside the impacts – desired and undesired; direct and indirect – that could be associated with that investment. While we do apply exclusions on tobacco, gambling, thermal coal mining or production and the manufacture or sale of weapons and/or ammunition for corporate issuers and we review sanction lists and ESG performance for non-corporates, we primarily focus on positive selection, rather than negative screening, to ensure all issues and issuers meet the highest standard.

A framework can be excluded from our investable universe during our initial screening process, as an outcome of our full verification review or verification rescore process. Typically, when a deal is announced, both the sustainability and credit teams undertake a first high-level review of the issuer and framework to identify any red flags highlighting clear misalignment with our SPECTRUM process that would trigger an immediate exclusion. If no such red flags are identified, both teams proceed with conducting a full verification review. If the outcome of the review indicates that the issuer or the framework fails to meet our evaluation criteria from either a sustainability or credit perspective (or both), the framework is excluded from the SPECTRUM Bond® universe. If the sustainability and credit verification reviews lead to a framework being included in our investable universe, the framework is regularly rescored to capture updated research/developments and determine whether the framework's position within the investable universe is still valid. If a framework is shifted from included to excluded in our investable universe, then the Portfolio Management team have 30 days to sell all held securities, in line with the divestment timeframe outlined in our Responsible Investment Policy.

Issuer Description

Bank of America is a US-based multinational bank - the second largest bank in the United States and the eighth largest bank in the world, according to S&P Global[1]. In 2013, the bank was one of the first corporates to issue green bonds and subsequently launched a sustainability bond framework in 2021.

Example expenditure

Bank of America sets out eligible categories and criteria for each bond in the relevant prospectus. For each new issuance, the sustainability team reviews the prospectus to confirm that the use of proceeds are acceptable. Green project categories include renewable energy, energy efficiency, clean transportation, sustainable water and wastewater management, green buildings, and carbon capture. Eligible social project categories include access to essential services – health and education, and affordable housing.

Bank of America Sustainability Bond Transaction Details

Issue date	Size	Maturity date	ISIN
Oct 2019	USD 2b	October 2025	US06051GHW24

Purchase date	Sold date	ISIN
Oct 2020	February 2024	XS2318745937

MIM verification summary

Bank of America was downgraded to a tier of exclude following updates to its environmental and social risk policy and the bond was then sold on the 23rd February 2024. The new policy removes several exclusions on the bank's financing that had previously been in place, such as: project financing for new coal mines, new coal-fired power plants, and for exploration and production of oil and gas in the Arctic Circle. This change in the bank's environmental policy represents a material weakening in its climate ambition and enables the bank to provide direct financing for the development of new assets that are highly misaligned with the transition to a low-carbon economy. The other five banks in the 'big six' in the US have exclusions on project financing for new coal mines and coal-fired power plants. As such, Bank of America now stands out as the only issuer in its peer group that will provide capital for these assets.

Bank of America was an include, before the policy update, as it is a relatively large financier of low-carbon energy sources and committed to reducing its financed emissions in a number of relevant sectors. However, BNEF research indicates that this decade, banks need to provide $4 of financing to low-carbon energy sources for every $1 they provide to fossil fuels in order to align with the goals of the Paris Agreement[2]. With the global banking sector, including Bank of America, a long way off achieving this target[3], the issuer's policy update opens the door for additional fossil fuel financing, making this target even more challenging.

Furthermore, the policy update impacts the banks direction of travel on its own climate targets. Bank of America had previously published a TCFD report setting out financed emissions targets and some consideration of how it plans to achieve them. However, with the removal of its coal financing policy, it is difficult to have confidence that Bank of America will implement its strategy in full, and it seems even less likely that its performance will improve at the rate required going forward.

Credit

Bank of America's credit strength lies in a well-diversified business mix, underpinned by robust franchises in both retail and commercial banking. It has the largest share in the US retail deposit market and holds top-tier market positions across its businesses. The bank follows a conservative strategy, with a well-balanced mix of NII and non-NII revenue sources. Asset quality remains healthy, with a diversified loan portfolio. The bank's funding and liquidity profile remains strong, given its retail-oriented structure and solid access to wholesale markets. Its capital position remains strong. The bank consistently ranks among the best performers in Fed stress tests. Bank of America's policies on issuer conduct are sound, with a strong focus on diversity and inclusion, equal opportunities, and sustainability.

This bond was fully sold on the 23rd February 2024.

[1] *The world's 100 largest banks, 2023 | S&P Global Market Intelligence (spglobal.com)*
[2] *https://about.bnef.com/blog/financing-the-transition-energy-supply-investment-and-bank-financing-activity/*
[3] *https://www.bloomberg.com/news/articles/2023-02-28/banks-need-even-bigger-low-carbon-pivot-to-avert-climate-crisis*

Impact Bond Highlight

Xylem

Included and purchased in portfolio

S&P: BBB
Moody's: Baa2

Issuer Description

Xylem is a large American water technology provider. with a global operations footprint, including 42 manufacturing facilities in 19 countries. With the acquisition of Evoqua Water Technologies in May 2023, Xylem became world's largest pure-play water technology company.

Green bond framework

Xylem published a green bond framework in 2020, aimed at financing CapEx, R&D or M&A related to products and services for sustainable water and wastewater management, and water productivity solutions. Each eligible category is mapped to a company-wide 2025 Signature Goal, for example, R&D toward technologies that optimise and automate water management is linked to Xylem's goal to save more than 16.5 billion cubic meters of water through advanced technologies. Products or services related to fossil fuels are explicitly excluded by the framework.

The green bond framework is fully aligned with the issuer's strategy to increase the share of green lending in their portfolio. It also aligns with the substantial contribution to mitigation criteria of the EU Taxonomy and ICMA's Green Bond Principles.

Example of expenditure

Green project categories include sustainable water and wastewater management and water efficient products. Based on the 2021 impact report, the proceed allocation is fairly split across the two categories. Overall 36% of proceeds have been allocated to R&D, 36% to CAPEX, and 28% to M&A expenditure. The issuer's impact report provides us with KPIs on cubic meter of water for reuse and water saved through the green projects in the portfolio. The impact report also provides CO2 reduction due efficient of products. Case studies are also provided, with a good level of detail.

One highlighted project is Xylem working with the city of Buffalo, New York, to implement a real time control program to convert the City's gravity fed sewer system into a managed conveyance and storage system. In 2019, this program helped prevent 1.48 billion gallons of sewer and storm overflows from entering local waterways.

Xylem Transaction Details

Issue date	Size	Maturity date	ISIN
June 2020	EUR 500m	Jan 2031	US98419MAL46

MIM verification summary

The issuer's green bond framework is in line with their sustainability strategy and targets. Xylem has 2025 Sustainability Goals, which include achieving 100% renewable energy, and has submitted a net zero by 2050 target to the SBTi for approval. All material environmental factors are mitigated with strong policies and performance in line with expected trajectories.

Over 95% of Xylem's emissions profile is attributable to the scope 3 category use of sold products. There is a specific target, to reduce emission economic intensity by 55% by 2030 against a 2019 baseline, relevant to this category. Xylem highlight three main levers being used to achieve this target – designing for sustainability, innovative water technologies and variable-frequency drives to reduce energy usage.

Xylem provide regular allocation and impact reporting.

From a fundamental credit standpoint, Xylem whose strength benefits from a strong market position in the water infrastructure market and good exposure to water utilities, providing a stable revenue base stable and profitability less volatile to market conditions. The company has generated healthy free cash flow (FCF), more than sufficient to cover dividends and share repurchases. Profitability has been sound and margin remained healthy in 2023 owing to favourable pricing and the Evoque acquisition. Margins are expected to expand in 2024 driven by solid demand and backlog execution as week as the delivery of cost synergies. Robust FCF conversion should allow for bolt-on acquisitions while keep leverage in check, in line with the company's commitment to BBB/Baa2 credit ratings. Xylem's business profile is well positioned to benefit from the medium to long term increased global focus on clean water scarcity and water treatment, especially in emerging markets.

Xylem performs well on ethics and issuer conduct and has a strong governance structure, with no major controversies.

The above bond was purchased for this portfolio in January 2024.

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