

# Ardea ESG Policy

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## Introduction

Ardea Investment Management is a specialist fixed income investment manager serving a diverse range of global clients from pension funds, government entities, insurers, and retail investors.

Environmental, Social and Governance (ESG) considerations are integrated into the fabric of Ardea's operations and investment decision-making. This reflects our commitment to responsible investing, stewardship, and aligns with our goal of delivering long-term value to our clients while contributing to sustainable benefits for the broader community.

## ESG at Ardea

As stewards of capital, we have a duty to ensure that we are operating and investing sustainably; making a full effort to identify and mitigate all risks to our portfolios. Given our focus on advanced economy sovereign bond markets, Ardea sees climate change as the ESG risk of most concern. We are committed to use our knowledge and to effect change in government bond markets arising from the realisation of risks related to climate change.

## ESG Scope

We take seriously our rights and responsibilities as an active owner and participant in the global government bond market. We view a well-functioning government bond market as an essential component of a modern economy and financial system, and essential for investors seeking low-risk, predictable returns, and high liquidity. Government bonds are also critical for the functioning of monetary policy, as a secure asset held for prudential regulatory purposes, and for use as a risk-free rate when pricing a wide range of other asset classes.

Given the large number of investors in advanced economy sovereign bond markets, we acknowledge that our ability to influence is limited. The central role that government bonds play also means that divestment and allocation away from the asset class is of limited usefulness. Furthermore, much of the governance and social risks which may present in government bond markets are reduced by default given Ardea's strategies restrict the investible universe to countries with high governance and transparency standards.

However, environmental risks are not currently adequately addressed by credit ratings given the longer time horizon of some of these risks. Further, we believe that environmental risks (and, in particular, climate change) will become increasingly important over time.

We therefore place a reliance on engagement and specific initiatives, such as growing green bond turnover, to deliver change. As government bond investors, we have direct access to issuers and can leverage the alignment present between issuers and investors in ensuring that securities continue to perform within the expectations of end investors. The focus on ensuring consistent investment returns above all else ensures that other issues that may be deemed overly political in nature do not detract from the core objectives of engagement.

## ESG Programme

To meet our commitments to ESG and sustainability, Ardea has prioritised the following activities:

1. Research,
2. Integration,
3. Engagement, and
4. Corporate Sustainability.

## ESG Research

Research is integral to Ardea's investment process, and the consideration of ESG is consistent with that approach. Furthermore, the research projects help to inform our broader investment and operational ESG activities as well as to raise awareness of the importance of sustainability risks and opportunities when it comes to investing in government bonds.

In response to the limited literature and principles on managing ESG risks in advanced economy sovereign bond markets, Ardea is committed to conducting and promoting research that complements existing materials on equities, corporate bonds, and private assets. We have a formalised research partnership with academic institutions with the express goal of understanding how climate and transition risks impact government bond markets.

It is our intention to contribute to the development in the narrative on ESG matters specifically related to government bond investing via additional engagement with the media, clients and across the industry more broadly. Our research findings are also published on our website.

## ESG Integration in the Investment Process

Ardea adopts a pure 'relative value' (RV) investment approach to generate alpha that identifies government bonds that are closely related and have similar underlying risk characteristics but are priced inconsistently with each other - known as 'relative value mispricing' - and therefore have the potential for their prices to rise or fall independently of broader market direction. An essential element of this pure RV investing approach is to isolate these positions from unwanted market risks, including those stemming from ESG-related factors, by using a wide range of risk management strategies which allows low volatility returns to be generated independent of broader market movements, including the level or direction of interest rates.

In prioritising ESG integration into our investment process, Ardea has focused on system-wide risks such as climate change and the financial sustainability of governments' fiscal burdens. Given the threat climate change poses to the global economy and the fast materialisation of transition risk, these risk factors are most likely to be material determinants of sovereign bond markets.

Whilst focusing on climate change and transition risks may convey an emphasis on the environment in our ESG integration, we remain cognisant of the potential flow-on social and governance impacts to underlying communities and the broader economy. Through our research, engagement and corporate activities, these important and interrelated factors are further considered.

We strongly advocate for engagement, in contrast to exclusion or divestment, to influence change and encourage long-term value creation.

## Sustainability Risks

Ardea evaluates and integrates Sustainability Risks, most significantly climate change risk, at multiple stages throughout the investment process. This is considered both an important element in contributing towards long-term investment returns and an effective risk-mitigation technique.

Ardea believes its ESG-related research capabilities enable the identification of ESG risks and opportunities of most relevance to the strategy. Specifically, the strategy generates returns via the implementation of the RV strategy outlined above which isolates mispricing between securities and mitigates exposure to market risks, including Sustainability Risks.

## Modern Slavery

Ardea strongly opposes modern slavery in all forms. Ardea takes steps to actively counter modern slavery practices throughout its business. In our investible universe of advanced economy sovereign bonds, which meet high standards of governance and are high investment grade credits, oversight and monitoring is well established, and thus the risk of egregious practices escaping undetected is low.

## Promoting the Growth and Development of a Government Green Bond Market

An inherent and distinctive feature of our investment approach is its highly active trading style, which results in frequent and high-volume trading of government bonds. We aim to utilise this strong presence in the market to foster growth of the green bond market, contributing materially towards improving market liquidity and price discovery for green government bonds.

To practically integrate these ideas into our investment process, Ardea is committed to:

- Preference trading green bonds over conventional bonds when the relative value is similar, and
- Regular engagement with government bond issuers to advocate for more green bond issuance, including participation in new bond syndications when the relative value is attractive.

By creating more opportunities for trading and enhancing price discovery, our aim is to contribute to advancing the development and growth of the green bond market globally which, in turn, has encouraged governments to issue more green bonds and contributes to a reduction in sustainability risk for issuers, and therefore economies overall. This has direct implications for the sustainability of the government bond market in aggregate and therefore all investors in government bond strategies.

## Climate transition risks

Our research has found that climate transition risks are priced into government bond markets. The climate change scenarios, shown below and as defined by the IPCC in its fifth assessment report, results in shocks to the level of government bond yields and the shape of yield curves with these effects expected to eventuate over an extended period:

- (i) *The Paris Agreement*: average global temperature rise will remain below 2°C by 2100
  - a. Emissions stay constant
- (ii) *Intermediate Scenario*: Emissions in the atmosphere peak at around 2040 and then decline. Global temperatures will rise by between 1.7–3.2°C by 2100
  - a. Emission increase by say 0.5% per year
- (iii) *No Action*: according to the IPCC, global temperatures will rise by between 3.2–5.4°C between the years 2081–2100 from pre-industrial times
  - a. Emissions increase by say 1% per year

The climate change scenarios form part of a broader series of stress tests Ardea runs across all portfolios daily. The scenario modelling is reviewed regularly at our weekly portfolio construction meetings to assess the potential impact on the portfolios and address undesirable risk exposures. All scenario models are considered within the context of Ardea's active trading style that allows for the dynamic rebalancing of

positions. We continue to refine our risk management processes related to climate change as the market and data continue to evolve.

## ESG Engagement

Engagement seeks to move beyond demonstrating the impact of ESG factors for investment returns and risk. We view engagement with stakeholders including clients, media, debt management offices, academia, and issuers as the most efficient and logical way to promote sustainable outcomes generally, not just within our industry or asset class. Engagement also broadens the scope to include a wider discussion on ESG issues with the key entities that produce the supply of a large part of the fixed income universe, namely governments.

With an objective to promote the development of the green government bond market, Ardea regularly engages with all major government bond issuers across the markets it invests. This engagement is to:

- help sovereigns better understand the increasing ESG demands of investors,
- convey expectations and concerns on behalf of our clients,
- promote discussions between investors, sovereign issuers, and other stakeholders,
- increase the information provided to the market on ESG matters,
- extract ESG information important for our analysis, and
- encourage ESG data transparency.

Our goal is to further develop our participation in the issuance of different instrument types, currencies, and maturities with a skew towards market segments which need developing. This approach also extends to specific engagement with banks to promote secondary market turnover and liquidity in the global green government bond market.

We record and report on our participation in the primary market and our engagement activities with the issuers and banks. Our goal is to see an improvement year-on-year with respect to our overall engagement and our participation in under-developed green markets (and tenors), and to encourage banks to provide the liquidity needed to foster the development of a green bond market.

## Corporate Sustainability

Ardea is committed to drive long-term change and improve outcomes for both the company and its stakeholders. By fostering a culture of improvement and innovation, we continue to evolve our corporate approach including by:

- assigning an ESG objective or Key Performance Indicator to each Ardea employee to embed sustainability as a core corporate value,
- training applicable full-time employees on diversity, equity and inclusion, First Nations peoples, modern slavery, cybersecurity and artificial intelligence, fiduciary duties, personal trading, and conflicts of interest in addition to an annual compliance attestation,
- maintaining a Conflicts of Interest policy to ensure that any actual, potential and/or perceived conflict of interest that may arise both between itself and its clients, a staff member, and a client and between clients are identified, prevented, or managed and disclosed in the best interests of clients,
- measuring and fostering our existing diverse talent and inclusive culture, and raising awareness of diverse groups through our research, recruitment processes and networking events, and
- taking steps to actively counter modern slavery practices throughout our business, in client and supplier relationships, and in our engagement with the industry and with issuers.

## ESG Collaboration

As a specialist investor in advanced economy sovereign bonds, it is critical that we collaborate across the industry to amplify our influence and impact.

Since 2010, Ardea has been a signatory of the UN Principles for Responsible Investment and committed to the six key principles to develop a more sustainable financial system.

Finally, we believe it is our duty to act responsibly and sustainably with respect to our own carbon footprint and our actions as global citizens. As such, we:

- support the Paris Agreement and its goals of limiting global warming to 1.5 degrees Celsius compared to industrial levels via economic and social transformation based on the best available science<sup>1</sup>,
- are a signatory to the Global Investor Statement to Governments on Climate Change<sup>2</sup> which calls on world governments to:
  - Achieve the Paris Agreement's goals
  - Accelerate private sector investment into the net-zero transition
  - Commit to improve climate-related financial reporting.

## Responsible Investment Governance

The Ardea Board has oversight over high level firm strategy and ensures appropriate risk management processes and policies are in place. This oversight extends to policies that address regulatory and fiduciary risks relating to ESG or sustainability related elements. The Ardea Board receive regular ESG Reporting as part of the CEO update at each board meeting and, together with the CEO and CIOs, ensure that the ESG Policy is consistent with Ardea's investment philosophy, risk management approach, and overall strategy.

The Sustainability Committee is responsible for overseeing Ardea's sustainability initiatives and ensuring that investments are consistent with ESG principles. The committee is chaired by the CEO and includes our Co-CIO, Head of Research and internal ESG resource.

The Ardea ESG Policy is part of the overall Governance, Risk and Compliance (GRC) Framework, managed by the Ardea Compliance Manager. The Compliance Manager is responsible for the implementation and day-to-day operation of the GRC Framework, with the support of the Fidante Compliance team's resources. All staff are provided with a copy of Ardea's GRC Framework and are required to sign the GRC Framework Acknowledgement to acknowledge that they have read and will abide by the policies and procedures contained within it. As the ESG Policy forms part of this Framework, the Compliance Manager is responsible for ensuring adherence with this Policy.

## External Reporting

In addition to the UNPRI reporting requirements, we have established a log which tracks our engagement activities and outcomes sought. We share these activities as well as additional ESG research and analysis with clients during periodical portfolio reviews.

With respect to climate change, we are supportive of and seek to follow the recommendations as described in the "Task Force on Climate Related Financial Disclosures"<sup>3</sup> (TCFD). Specifically, we seek to "disclose the metrics and targets used to assess and manage relevant climate related risks and opportunities where such

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<sup>1</sup> <https://unfccc.int/process-and-meetings/the-paris-agreement/the-paris-agreement>

<sup>2</sup> <https://theinvestoragenda.org/focus-areas/policy-advocacy/>

<sup>3</sup> <https://www.fsb-tcf.org/recommendations/>

information is material” to help investors make better informed capital allocation decisions with respect to climate related risks.

Furthermore, certain Ardea’s strategies have been determined to be Article 8 Strategies under the European Union’s Sustainable Finance Disclosure Regulation (SFDR) as they promote environmental characteristics due to our green bond investments and engagement with issuers.

## Review

Given the rapidly changing ESG landscape, for our ESG policy to maintain its relevance it is prudent for us to regularly review the policy. This policy document will evolve over time as a function of our own research, feedback from clients and stakeholders, the literature, and other relevant ESG authorities.

We disclose our ESG Policy publicly and aim to review and update the policy at least every 12 months.

We are continuously seeking to improve our analyses, processes, and transparency around sustainable investing. We are always very keen to learn about new ideas in sustainable investing and to understand how these might be complementary to and an improvement on our existing approach. As such, we welcome feedback from our clients and stakeholders.