Sustainable Investment Methodology

Danske Bank A/S

Danske Bank

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Introduction

A sustainable investment is defined by the EU Sustainable Finance Disclosure Regulation (EU) 2019/2088 (SFDR) as an investment that contributes to either an environmental or social objective while not doing significant harm to other sustainable investment objectives and abiding to principles on good governance. More precisely a "sustainable investment" means an investment in an economic activity that contributes to an environmental objective, as measured, for example, by key resource efficiency indicators on the use of energy, renewable energy, raw materials, water and land, on the production of waste, and greenhouse gas emissions, or on its impact on biodiversity and the circular economy, or an investment in an economic activity that contributes to a social objective, in particular an investment that contributes to tackling inequality or that fosters social cohesion, social integration and labour relations, or an investment in human capital or economically or socially disadvantaged communities, provided that such investments do not significantly harm any of those objectives and that the investee companies follow good governance practices, in particular with respect to sound management structures, employee relations, remuneration of staff and tax compliance.

To qualify as a sustainable investment, an investment must therefore meet the following criteria:

1. Contribute to an environmental or social objective, e.g., measured by indicators for use of energy, renewable energy, raw materials, water and land, the production of waste, and greenhouse gas emissions, or based on its impact on biodiversity and the circular economy; or a social objective, e.g., tackling inequality or fostering social cohesion, social integration, or labor relations, or in human capital or economically or socially disadvantaged communities";

2. Do No Significant Harm: respect of "Do No Significant Harm" principle (DNSH) on other environmental or social sustainability factors is widely interpreted as requiring to adopt an approach to assess and take into account principal adverse impacts based on principal adverse impact (PAI) indicators and whether the issuer adheres to the OECD Guidelines for Multinational Enterprises and the UN Guiding Principles on Business and Human Rights;

3. Good Governance: demonstrate that investee follows good governance practices, requiring to have a policy to assess good governance practices (sound management structures, employee relations, remuneration and tax compliance).

Scope

This methodology description covers sustainable investment assessments relating to assets managed by Danske Bank on behalf of customers through investment product offerings, such as discretionary mandates, managed portfolios, alternative investment funds, insurance-based investment products (IBIPs), pension products/ schemes, and UCITS funds.

The assessment framework does not cover externally managed investment products distributed to Danske Bank's customers or UCITS funds with investment managers outside of Danske Bank Group When we invest in externally managed products (i.e. products managed by asset managers that are not part of the Danske Bank Group), we may choose to take reliance on the models and methodologies applied by those managers in respect to identifying sustainable investments, if we deem the processes and methodologies sufficiently robust to manage the sustainable investments through the lifecycle of the investments or apply look-through per the methodology principles.

Sustainable Investment Model

In order to determine whether an investment qualify as a sustainable investment a framework has been developed. This framework is implemented on a best-effort basis, taking into account the best interests of both the client and the investment product.

Our framework identifies issuers as either sustainable or not sustainable (i.e. entity rather than activity based approach). We have implemented various quantitative and qualitative processes to identify sustainable investments across all in-scope investment products. The framework relies to a larger degree on external data providers. Within our sustainable investment framework there are four underlying approaches that can determine an investment as sustainable:

1. EU Taxonomy alignment
2. EU Climate Benchmark constituent
3. Use-of-proceeds/labelled bonds
4. The SDG Model

An investment products allocation may have any or all of the different types of sustainable investments depending on the investment strategy of the fund.

EU Taxonomy aligned-investments

The Taxonomy Regulation (Regulation (EU) 2020/852) entered into force on 12 July 2020 and is a cornerstone of the EU's sustainable finance framework. It helps direct investments to the economic activities most needed for the transition, by establishing a classification system for the identification of environmentally sustainable economic activities. In order to meet the EU's climate and energy targets for 2030 and reach the objectives of the European green deal, it is vital that we direct investments towards sustainable projects and activities.

The EU Taxonomy is centered around six environmental objectives: climate change mitigation, climate change adaptation, sustainable use and protection of water and marine resources, transition to a circular economy, pollution prevention and control, and protection and restoration of biodiversity and ecosystems.

The EU Taxonomy does not lay down a list of socially sustainable economic activities. Also, sustainable investments with an environmental objective might not be aligned with EU Taxonomy.

Whilst taxonomy-aligned activities are always deemed as sustainable investments on activity-basis, issuers with taxonomy-aligned investments are not in per se sustainable investments at an entity-level. For this, a specific assessment is needed as to whether the issuer at an entity level contributes to an environmental or social objective, do not significantly harm any of those objectives and follow good governance practices.

Per the sustainable investment method in Danske Bank, all issuers, deriving more than 50% of revenues from EU-Taxonomy aligned activities are deemed to contribute to an environmental objective. An issuer with more than 50% of revenues from EU-Taxonomy aligned investments will therefore qualify as a sustainable investments, provided that the overarching DNSH and good governance criteria are met.

Currently, the identification of EU Taxonomy aligned investments is heavily impacted by data constraints and lack of company reporting, meaning that the majority of our sustainable investments are not and will not be reported as taxonomy aligned.

EU Climate Benchmark constituents

The Paris Agreement is essential for achieving the UN SDGs due to the close interlinkages between climate change mitigation, development pathways and the pursuit of the goals.

To support the long-term goals of the Paris Agreement, the European Commission has developed a methodology for two climate benchmarks, the EU Climate Transition Benchmark ("**EU CTB**") and EU Paris-aligned Benchmark ("**EU PAB**").

The EU Climate Benchmarks are investment benchmarks that incorporate – next to financial objectives – specific objectives related to green house gas ("**GHG**") emission reductions and the transition to a low-carbon economy. The benchmarks are based on the scientific evidence of IPCC and criteria aiming to ensure a transition path for portfolios that is compatible with the transition to a sustainable economy through outlined decarbonisation targets and trajectories in respect to GHG intensity and GHG emissions.

In Danske Bank, we view all passive investments tracking either an EU CTB or EU PAB sustainable investments. Therefore, our passively managed products tracking an EU Climate Benchmarks are deemed to have dual investment objectives, supporting financial objectives as well as the long-term goals of the Paris Agreement through GHG reductions. When a managed investment product partly invest into underlying funds or mandates tracking such objective, the subset of these investments are considered sustainable for the specific product.

The EU Climate Benchmarks have exclusions in place safeguarding global standards such as UNGC Standards and DNSH assessments for the EU Taxonomy Regulation, however, the weighting principles of the benchmarks do not allow for full divestments from sectors key to the transition as the benchmarks are based on the belief that no company by its activities is unable to transition. This also implies that companies from certain high emission sectors can be found in funds tracking these benchmarks.

All our directly managed CTB or PAB products track climate indices administered by MSCI.

Investments into any external fund tracking a CTB or PAB can be tied to benchmarks maintained by other administrators.

To address climate change, countries adopted the Paris Agreement at the COP21 in Paris on 12 December 2015. The Agreement entered into force less than a year later. In the agreement, all countries agreed to work to limit global temperature rise to well below 2 degrees Celsius, and given the grave risks, to strive for 1.5 degrees Celsius.

Use-of-proceeds/labelled bonds

Companies, sovereigns, and sovereign-related issuers (collectively "***issuers***") can issue bonds to finance social and environmental projects and to finance their transition. These instruments are often referred to as Green and Social bonds, and/or (collectively) Sustainability bonds.

In Danske Bank, we consider an investment in a Sustainability Bond a sustainable investment in support of the UN SDGs, if the issuance follows ICMA's principles on Green and Social Bonds, and sustainability safeguards are in place, ensuring that the issuance does not cause a significant harm to a sustainable investment objective, and – for investee companies – meet principles on good governance.

We also consider Green Bonds issued in accordance with the EU Green Bond Framework a sustainable investment.

*European Green Bonds are bonds that meet the legislative green bond standard ("**GBS**") defined in the EU Regulation on European Green Bonds, which applies from end-2024. Bonds issued under GBS will align with the EU Taxonomy for environmentally sustainable activities and are seen as one of the main instruments for financing investments related to green technologies, energy efficiency and resource efficiency as well as sustainable transport infrastructure and research infrastructures.*

For the assessment of a bond's adherence to the ICMA principles for Green and Social Bonds, we rely on Refinitiv data. Here the key indicators applied to assess the contribution to a social or environmental objective are:

Step 1: Use of proceeds

The utilisation of proceeds must target eligible green or social projects, contributing to environmental or social objectives covered by the UN SDGs.

Eligible green projects are in that respect, but not limited to: renewable energy, energy efficiency, pollution prevention and control, environmentally sustainable management of living natural resources and land use, terrestrial and aquatic biodiversity, clean transportation, sustainable water and wastewater management, climate change adaption, circular economy adapted products, production technologies and processes and green bonds.

Eligible social projects are, but also not limited to: affordable basic infrastructure, access to essential services, affordable housing, employment generation and programmes designed to prevent and/or alleviate unemployment stemming from socioeconomic crises, climate transition projects and/or other considerations for a "just transition", food security and sustainable food systems, socioeconomic advancement and empowerment.

The management of proceeds relating to these projects shall be sufficiently ringfenced through sub-accounts held by the issuer.

Step 2: Project Evaluation and Selection

To qualify a bond as Green or Social, the issuer must outline:

- the sustainability objectives of the eligible project;
- the process by which the issuer determines how the projects fit within the eligible Green/Social Projects; and
- complementary information on processes by which the issuer identifies and manages perceived social and environmental risks associated with the relevant project(s).

Step 3: Reporting

Reporting issuers should make, and keep, readily available up to date information on the use of proceeds to be renewed annually until full allocation, and on a timely basis in case of material developments. The annual report should include a list of the projects to which Green Bond and Social Bond proceeds have been allocated, as well as a brief description of the projects, the amounts allocated, and their expected impact.

The ambition of Danske Bank is to include use of proceeds in the annual reporting tied to Sustainability Bonds in our managed products. However, due to central data constraints in respect to tracebility of such impact data, this is not included in the annual reporting as of current date.

For more information on ICMA's principles for Green and Social Bonds see the Methodology Documents.

The SDG Model

At Danske Bank, we have developed a proprietary SDG Model for the evaluation of companies' contribution to environmental and/or social objectives of the UN SDGs. The model applies to listed equity as well as bond issuers and ensures a replicable and consistent approach for assessing an investment's contribution to the SDGs through the sustainability-indicators and assessment criteria applied herein.

Under the SDG Model, a company's contribution to the SDGs is assessed through two dimensions:

1. What products and services the company produce (Product and Service Contribution)
2. How the company produces its products and services (Operational Contribution).

The SDG Model is data driven and relies on revenue datasets from Factset with SDG data from Util as well as PAI Indicators from ISS-ESG and ESG scores from Sustainalytics. Companies with insufficient data per the methodology of the model are not eligible to be sustainable, unless demonstrated through a qualitative assessment that the criteria in the model are met.

The UN Sustainable Development Goals (the " ***UN SDGs****") are the globally agreed framework for achieving a better and more sustainable future for all. The SDGs consist of 17 interlinked goals, made actionable by underpinning 169 targets, designed to be a "blueprint to achieve a better and more sustainable future for all".*

The SDGs were set up in 2015 by United Nations General Assembly and are intended to be achieved by the year 2030. The SDGs are an increasingly accepted standard for companies to help clarify, prioritize and maximize the value their products and services have on society. Consequently, assessing the SDG contributions of companies provides a powerful means of demonstrating the overall impact of positive contribution a given company has on environmental or social objectives. The SDGs work as a lens for any market, asset class and geography and can be set as a benchmark for any company/issuer thanks to the universality of their underlying principles.

Step 1: Product and Service Contribution

Product and Service Contribution is measured as the contribution of a company's revenues against each applicable SDG. For this exercise, revenues are mapped against business activities assessed to positively contribute to the UN SDGs. The data from Factset indicates the revenues that a company have from different business activities, whereas the data from Util is used to assess how those business activities contribute to SDGs. For a representative sample of the business activities assessed to contribute to each of the UN SDGs, see Appendix 1.

Product and Service Contribution also captures negative alignment, meaning that a product line contributing negatively to the SDGs impacts the overall weight of revenues assigned to the support the SDGs.

Example company product/service contribution:

In the below examples, a company's revenue is divided to five different product families. Some of these qualify to be fully contributing to the SDGs (SDG Aligned), some qualify to be partially SDG Aligned and one product line contributes negatively. As the overall weighted average sums up to 10% of sustainable revenue, the company will have very limited positive contribution from product/service side to be a sustainable investment.

		Revenues (Factset)	SDG Business Activity (Util)	SDG Aligned Revenues
Com	Business Activity A	20%	Yes, positive	20%

	Business Activity B	20%	Yes, partially positive	10%
	Business Activity C	20%	Neutral	0%
	Business Activity D	20%	Neutral	0%
	Business Activity E	20%	No, negative	-20%
		=		=
	Total Business Activities	**100%**		**10%**

For certain business activities (e.g. Banks, Utilities), where the business activity eligibility is not nuanced enough additional sectors specific criteria are applied (e.g. UPRB signatory, Renewable energy production).

Examples of sustainability-eligible business activities leveraged in the SDG Model:

SDG	Fully Sustainable Business Activities (Examples)		
1 – No Poverty	Solar power generation	Pre-school childcare	Healthcare education
2 – Zero Hunger	Nutritional health products	Sustainable agriculture	
3 – Good Health and Well-Being	Solid waste recycling equipment	Accident and health insurance	Major disease treatment
4 – Quality Education	Educational services	Communications equipment	Telecommunications infrastructure construction
5 – Gender equality	*N/A business activities not identified to contribute to specific SDG*		
6 – Clean Water and Sanitation	Wastewater treatment	Water utilities	
7 – Affordable and Clean Energy	Wind energy products	Energy storage and batteries	
8 – Decent Work and Economic Growth	*N/A business activities not identified to contribute to specific SDG*		
9 – Industry, Innovation and Infrastructure	Clean transport infrastructure	Energy efficient industry automation	
10 – Reduced Inequalities	*N/A business activities not identified to contribute to specific SDG*		
11 - Sustainable cities and Communities	Affordable real estate	Green buildings	
12 – Responsible Consumption and Production	Pollution prevention	Resource recovery	
13 – Climate Action	Hydropower	Wind energy	Inland and ocean marine Insurance
14 – Life Below Water	Environmental remediation	Wastewater treatment	
15 – Life Above Land	Environmental remediation	Recycling services	Wholesale electricity generated by wind power
16 – Peace, Justice and Strong Institutions	*N/A business activities not identified to contribute to specific SDG*		

17 – Partnership for Goals	*N/A business activities not identified to contribute to specific SDG*		

SDGs 05, 08, 10, 16, 17 are ouf-of-scope as indicators for Product and Service contribution as they are not directly linked to business activities or are too generic in nature and are more suitable to be assessed via operations and conduct.

Step 2: Operational Contribution

The Operational Contribution is based on an assessment of how well a company manages material sustainability issues from the perspective of the goals.

Operational Contribution is measured through proxies for principal adverse impact ("**PAI**") indicators based on the sectors and industries where the company is active relative to the company's own performance against these indicators. The PAI indicators, derived from ISS-ESG, do not capture all material sustainability issues (e.g. data security), and are supplemented with management quality indicators/ESG scores derived from Sustainalytics.

The rationale of having a combination of two different datasets is based on having a balanced view on the evaluation of operational assessment by analyzing both past results via material PAI-indicators and performance going forward via the ESG scores that focus on management quality aspects. The two datasets also complement each other as when PAI indicators do not capture all material sustainability issues (e.g. data security), they are supported by management quality indicators.

Potential to impact SDGs via operations varies significantly over industries based on which sustainability issues are material in a given industry.

An example is the Industrial Machinery & Goods. The way industrial machinery companies manage their materials sourcing, product design & lifecycle management and energy consumption influences how societies may reach their goal of building resilient infrastructure, promoting inclusive and sustainable industrialization and foster innovation (SDG9).

Step 3: Combining the Assessments

By combining the measured Product and Service Contribution and Operational Contribution, the SDG Model captures the aggregate contribution to the SDGs by a given company. This approach, among others, ensures that even companies with a substantially high revenue weight of business activities contributing to the SDGs will not be eligible as sustainable investments, when these business activities are produced through negative/significant negative operations as demonstrated in the figure below.

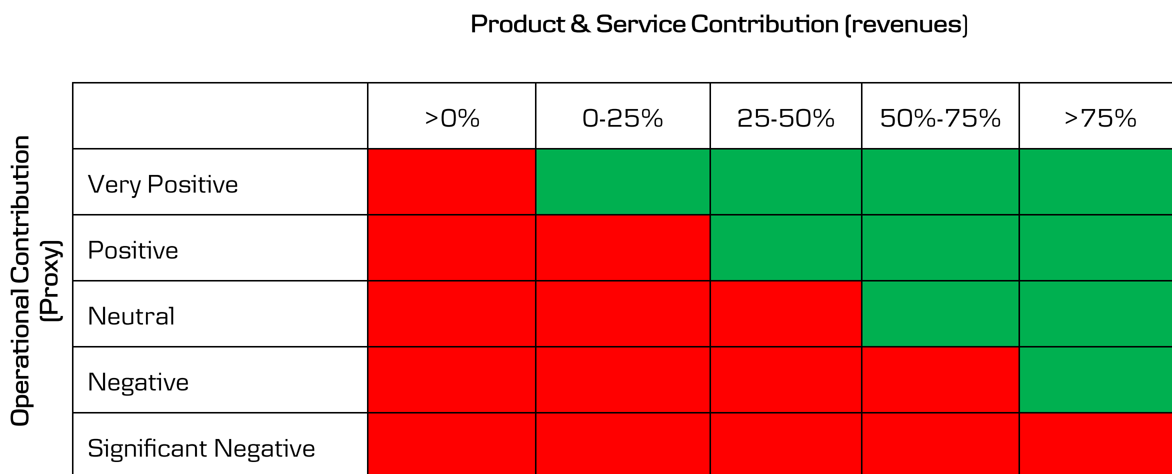

Figure 1: Assessment of Positive Contribution

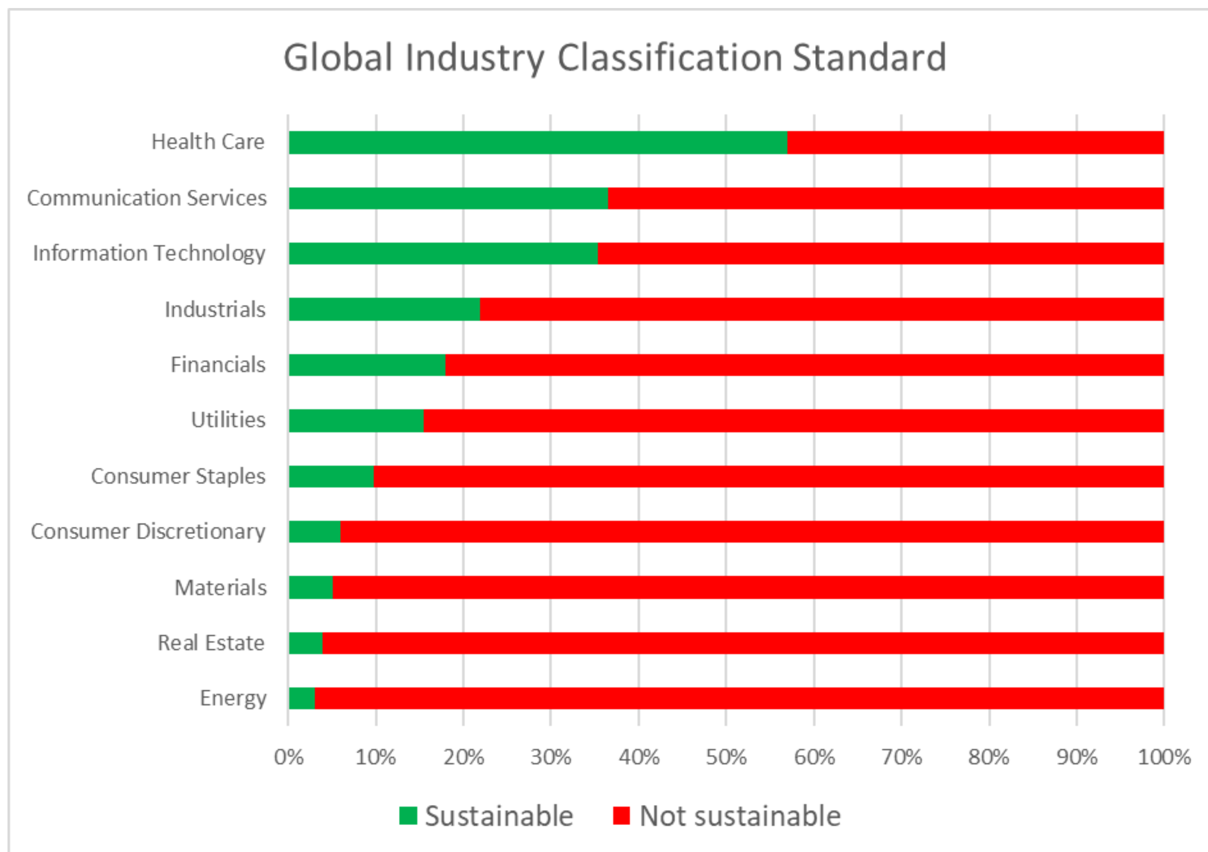

Figure 2: Sustainable investment share (unweighted) of MSCI World ACWI

Given that sustainability data is dynamic and that corporate disclosures are continuously improving means also that assessments may also evolve over time and additional companies will be assessed as part of the model. As of November 2023, around 5 700 issuers have been identified as sustainable investments using the quantitative SDG model component and around 50 issuers identified using the qualitative model component. Through reporting on the aggregate SDG contributions for investment portfolios leveraging the model, it will be visible to investors the extent to which their investments have positive contribution to the SDGs.

Qualitative overlay

While the Product and Service Contribution of a company can be assessed through revenue lines, in certain instances, a supplementing qualitative overlay is needed to cater for inherent ESG data gaps and challenges:

- there is an extensive amount of unique characteristics and challenges that come with ESG data, one of them being that the data to a certain extent can never fully capture the true characteristics of a given company. As a result, issuers can be misrepresented as either being sustainable or not sustainable according to quantitative models just because their business activities are classified in a certain way.
- many issuers are not covered by ESG-data vendors today. This means for instance that large cap companies, European companies and certain industries have better data coverage.
- available data to evaluate potential impacts may have biases towards past decisions and the resulting business model, while many issuers have stated intent, made commitments and started establishing procedures to transform their business models into a more sustainable business model.

These use cases will often be relevant in cases where companies do not consistently report ESG data, or such data is not fetched by the data vendors, e.g. as is the case for many private equity companies, as well as small cap companies and certain companies operating outside the European region, where we tend to a see a lower data quality.

The qualitative model component is structured through specific assessment criteria rooted in assessing issuers' business alignment with and contribution to the UN SDGs through their business activities and

operations. The assessments are in this respect applying proxies for sustainability-performance and targets in order to assess how positive impact is created and how harm via operations is minimized. Qualitative assessments are performed by dedicated analysts and approved by a qualitative assessment forum established under the Sustainability-Related Model Risk framework in Danske Bank. The qualitative assessment is specifically mandated to decide on the following use cases:

- an issuer is assessed as sustainable according to the quantitative model but where our own, or other research, points toward that the issuer is not sustainable.
- an issuer is assessed as not sustainable according to the quantitative model but where our own, or other research, points towards that the issuer is sustainable.
- an issuer is not covered by the quantitative model but where our own, or other research, points toward that the issuer is sustainable.

Do No Significant Harm Assessment

All sustainable investments managed by Danske Bank must pass the "do no significant harm assessment" (**DNSH**).

The do significant harm assessment is managed through exclusion criteria applied by the given product as further outlined in the product disclosures. Also, certain models/frameworks (such as the EU Climate Benchmark, ICMA's principles on Green and Social Bonds and the SDG Model) additional exclusionary filters or requirements.

Principal Adverse Impacts

Principal adverse impacts on sustainability factors are specifically addressed in the DNSH assessments for our sustainable investments through pre-set thresholds defined for the PAI indicators in respect to investee companies. This ensures that even if a company might have passed an operational assessment, relevant activity based exclusions etc., the company or investment will still not be deemed sustainable in case it is assessed to have a significant negative performance against the PAIs as based on these thresholds and indicators.

The thresholds have been set with the intention to capture the weakest performing companies on the outlined metrics. That means that the thresholds have been set at different levels dependent on the indicator and the data availability as well as data quality. Certain metrics have been combined in order to achieve intended outcome as further demonstrated in the table below. As the assessment and relevant ESG data supporting the assessment continuously evolves, the thresholds and the table will updated at an ongoing basis. Additional indicators will be added over time as data quality and availability improves.

Adverse sustainability indicator	Metric	ISS ESG Data point	Threshold
Greenhouse gas emissions	Scope 1 GHG emissions	ClimateScope1Emissions EV	>2 665
	Scope 2 GHG emissions	ClimateScope2Emissions EV	>8 785
	Scope 3 GHG emissions	ClimateScope3Emissions EV	>70 761
	Total Scope 1|2 emissions	ClimateScope12 EmissionsEV	>11 391
	Total Scope 1|2|3 emissions	ClimateScope123 EmissionsEV	>82 151
	GHG intensity of investee Companies	ClimateTotalEmissionsInt EUR	>5 979
	GHG intensity of investee Companies	ClimateScope123Emission sIntEUR	>2 5687

	Share of non-renewable energy consumption and non- renewable energy production of investee companies from non-renewableenergy sources compared to renewable energy sources	NonRenewableEnergy Production	Value equals = 1
	Energy consumption intensity	EnergyConsumption Intensity	>57
Greenhouse gas emissions/Biodiversity	Companies active in the fossil fuel sector	FossilFuelInvolvementPAI	Fossil fuel involvement = true AND negative biodiversity impacts = true AND companies without carbon emission reductions = true
	Activities negatively affecting biodiversity-sensitiveareas	CompNegAffectBioSensAreas	
	Companies without carbon emission reduction initiatives	CompWOCarbonEmission Reduct	
Water	Emissions to water	CRCODEmissionsEvic	>10
Waste	Hazardous waste and radioactive wasteratio	CRHazardousWasteEvic	>3 967
Social and employee matters	Violations of UN Global Compact principles and Organisation for Economic Cooperation and Development (OECD) Guidelines for Multinational Enterprises	Enhanced Sustainability Standards	UNGC Violation = true AND Lack processes for monitoring UNGC/OECD guidelines = true
	Violations of UN Global Compact principles and Organisation for Economic Cooperation and Development (OECD) Guidelines for Multinational Enterprises	LackProcessesUNGCOECD Guidelines	
	Exposure to controversial weapons (anti-personnel mines, cluster munitions, chemical weapons and biological weapons)	InvolvInContrWeapons	Involvement = True
	Board gender diversity	RatioOfWomenOnBoard	Zero women on board = true AND lacks human right policy = ture AND lacks whistleblower protection = true
	Lack of a human rights policy	LackHumanRightsPolicy	
	Insufficient whistleblower protection	InsWhistleBlowerProtection	

Minimum safeguards

Alignment with OECD Guidelines for Multinational Enterprises and the UN Guiding Principles on Business and Human Rights is specifically sought through the Enhanced Sustainaiblity Standards Screening excluding certain conduct and activities deemed harmful to society. The screening, among others, screen for companies' and other issuers' adherence to OECD Guidelines for Multinational Enterprises and the UN Guiding Principles on Business and Human Rights. Issuers assessed to act in breach of conventions in accordance with the critiera of the Enhanced Sustainaiblity Standards screening are not investable as a sustainable investment.

For the SDG Model, the Enhanced Sustainability Standard screening is supplemented by extended norm exclusions, meaning that issuers with the highest/"worst" signal according to ISS-ESG Norm-Based

Research, MSCI Controversy Indicator, or Sustainalytics Controversy Indicator cannot be classified as sustainable.

Good Governance

Corporate Governance refers to a set of rules or principles defining rights, responsibilities, and expectations between different stakeholders in the governance of corporations. A well-defined corporate governance system can be used to balance or align interests between stakeholders and can work as a tool to support a company's long-term strategy. Good governance is critical to the efficient and effective operation of any company, and the protection of shareholder value.

For purposes of the Good Governance test for sustainable investments we leverage again the enhanced screening, where we consider seven indicators relating to sound management structures, employee relations, remuneration of staff and tax compliance. The indicators are purposefully simplistic, considering the differences in market-specific, and industryspecific governance practices across the globe, to allow for comparability and monitoring. The screening is done on our entire investment universe wherever data on the indicators are available. Failure to adhere more than half of the criteria will always lead to a failure of the good governance test and Exclusion per the enhanced screening.

For more information see the method paper available here: Enhanced Sustainability Standards Screening.

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