

# Responsible Investment at Zurich

What we want to achieve, and how we do it



This document explains Zurich's responsible investment approach in detail: what we want to achieve, and how we do it. It outlines our responsible investment strategy and describes its three individual elements in the context of Zurich's overall approach to investment management and corporate responsibility. It also makes reference to specific policies, procedures, and practices outlined in the appendix. This document is aimed at everyone seeking to learn more about how responsible investment can be practiced by a large, global institutional investor, but should also provide insight to specialists seeking to analyze Zurich's practices. The document complements our position paper ['Doing well and doing good: Why Zurich practices responsible investment.'](#)

The first section describes the overall approach to responsible investment in the context of insurance investment practices. The following three sections describe the individual elements of this approach: 'ESG integration,' (integrating environmental, social and governance factors into the investment process), 'impact investing' and 'advancing together.'

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# Section I

Zurich's responsible investment strategy:  
there is only one way to manage our assets  
– as a responsible investor

“Our approach to corporate responsibility strives to create value for both our company and for society as a whole.”

Responsible investment means different things to different people. A clear understanding of Zurich’s approach to corporate responsibility is the starting point for defining our responsible investment strategy.

At Zurich Insurance Group (Zurich), being a responsible and sustainable company is at the foundation of our business. It influences our day-to-day decisions and our long-term planning. Our approach to corporate responsibility strives to create value for both our company and for society as a whole. By using our core skills, risk and investment management expertise, we aim to:

- Be a responsible business as reflected in our corporate governance, our code of conduct, and our respect for human rights
- Have a positive impact through our products and services, our capital, and our investment in communities
- Integrate environmental, social and governance (ESG) considerations into our underwriting, our investment processes, and our operations.

Responsible investment is thus about managing our overall portfolio of assets to create sustainable value or, in other words, to do well and do good. ‘Well’ means generating superior risk-adjusted returns relative to liabilities for the benefit of Zurich’s policyholders and shareholders, and ‘good’ means generating positive impact to benefit society and the communities in which we live and work.

Responsible investment forms a key element of Zurich’s investment philosophy and comprises three elements:

#### Mission

**Achieving superior risk-adjusted investment returns relative to liabilities**

#### Ambition

**We aim to be the best global insurance investment manager as measured by our key stakeholders.**

#### Investment philosophy

- 1. We aim to maximise economic objectives.**
- 2. We aim to minimize unrewarded risks.**
- 3. We believe that capital markets are fairly efficient over time.**
- 4. We are a responsible investor.**

**1. ESG integration:** Proactively integrating ESG factors into the investment process – across asset classes, and alongside traditional financial metrics and state-of-the-art risk management practices – supports us in ‘doing well’ and in achieving our mission to generate superior risk-adjusted long-term financial returns. Successful ESG integration is based on:

- Adequate training to help investment decision makers understand the relevance of ESG factors
- Access to data, research and analysis pertaining to ESG issues to inform investment decision making
- Formal integration of ESG factors into the security, asset and asset manager selection process
- Active ownership practices.

**2. Impact investing:** Through impact investing, Zurich can help fund solutions to pressing social or environmental issues. Zurich is directly exposed to challenges such as climate change, resource depletion, and more. As an insurer we have a direct interest in sustainable global economic growth and supporting communities in becoming more resilient to environmental and social challenges. Impact investments can help address these issues in a targeted way, and also offer a financial return commensurate with risks. In view of that, we have committed to invest up to USD 5 billion into impact investments. Once fully invested, we hope to help avoid the emission of five million tons of CO<sub>2</sub> per year, and make a positive contribution to the lives of five million people in need.

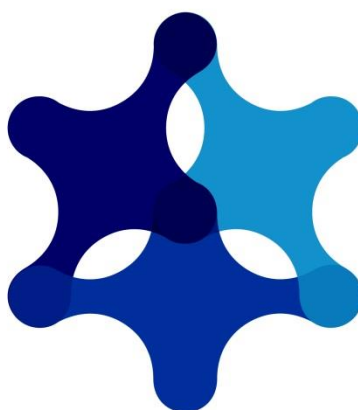
**3. Advancing together:** We believe that responsible investment will only truly have an impact if financial market participants advance together to make responsible investment mainstream. Only by acting collectively can we build markets in which ESG risk is priced efficiently, which provide the right incentives to those seeking to raise capital in the market, and in which impact investments provide capital on the scale needed to tackle the pressing social and environmental issues of our time. Supporting collaborative initiatives, working together with other industry participants, and engaging with policy makers and others to drive the advancement of responsible investment practices thus forms an integral part of our approach.

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## Responsible Investment

### ESG integration

- Training
- Information
- Process integration
- Active ownership



### Impact investing

- Intentionality
- Measurability
- Profitability

### Advancing together

- Innovation
- Collaboration
- Public advocacy

## The basis for responsible investment is a disciplined investment process

At Zurich, Group Investment Management is responsible for managing the Group's own assets. Zurich does not generally provide asset management services to unaffiliated parties. In a few instances, in-house asset management teams manage specific funds that form part of insurance products offered directly to clients. While those investments are small relative to own assets, the same responsible investment approach and processes apply to these funds. Zurich also offers its customers so-called unit-linked products, where customers are responsible for choosing investment strategies from a range of externally-provided investment solutions. At this stage, unit-linked assets are not within the scope of Zurich's responsible investment approach.

Group Investment Management has defined a clear and systematic approach to investing, supported by both industry best practice and academic research. Applying this approach globally to all investment activities is of great value to Zurich. Not only does the approach provide consistency and discipline, it also helps safeguard against investment decisions becoming pro-cyclical, that is, taking on additional investment risk during 'good times' and being forced to reduce risk by selling investments at the worst possible moment during times of market stress.

The starting point in determining the investment strategy in insurance investment management is asset-liability management (ALM). This first step establishes a portfolio of investments that closely replicates the insurance liabilities, and consists primarily of duration-matched government bonds.

Such a minimum-risk portfolio will ensure that market values of assets and liabilities move in line with fluctuations in capital markets.

The optimal mix of asset classes is then determined, one that offers the highest long-term expected investment return given Zurich's liabilities, regulatory framework and allocated capital. To make this asset allocation, Group Investment Management distills all investable asset classes into a small set of easily-understandable and transparent risk factors such as interest rate risk, credit risk, equity risk, etc. Group Investment Management then works to determine the best combination of risk factors to maximize the risk-adjusted return for a given amount of capital.

Insurance investment management is relatively complex. To effectively manage investment risks relative to insurance liabilities, Zurich has a very strong focus on ALM and is required, often also by the regulator, to hold certain assets. For instance, Zurich will have to hold sovereign bonds to back certain local currency liabilities. In addition, requirements to balance investment income and total return, tax considerations and other constraints exist and vary widely across local jurisdictions.

Zurich holds investments in over 800 different portfolios, on over 200 different balance sheets in over 40 jurisdictions, managed by over 30 different external, as well as internal asset managers. This complexity naturally requires exceptions and limits the ability to apply specific processes and approaches in every single instance. More information on Zurich's overall investment approach can be found in [Investment Management: a creator of value in an insurance company](#).

## Creating a responsible investment culture

Navigating the complexity of insurance investment management and practicing responsible investment at the same time can only be achieved by fully integrating these responsible investment practices into the overall investment approach and making them part and parcel of everyday investment decision-making. Strategies and policies alone are not sufficient. Responsible investment must become part of the organization's DNA – its culture. This will take time, leadership and 'learning by doing.' To accelerate and support this process, we are providing incentives to investment professionals to practice responsible investing by reflecting responsible investment in individual objectives across the Group Investment Management organization; we have incorporated responsible investment into Zurich's technical competency framework used to determine job profiles and training requirements; we have established a global group of 'responsible investment champions' representing individual teams; and we have built a small but dedicated responsible investment team that acts as a catalyst and engages with the rest of the organization on an ongoing basis.

See the [appendix](#) for details of these elements.

The remainder of this document describes the three individual elements of Zurich's responsible investment strategy and how they are implemented in the context of the overall approach.

# Section II

ESG integration at Zurich: capturing ESG-related risks and opportunities to enhance returns



“Zurich believes that ESG issues are best reflected at the level of selection of individual securities or assets.”

ESG factors have an impact on the risks and opportunities associated with the assets in which we invest. As a consequence, we believe that proactively including ESG factors in the investment process – across asset classes and alongside traditional financial metrics and state-of-the-art risk management practices – will support us in our mission to achieve superior risk-adjusted long-term financial returns.

As described in [section I](#), the starting point in determining Zurich’s investment strategy is an integrated process used to define the strategic asset allocation according to ALM principles. This allocation is the result of a disciplined process that distills all investable asset classes into a small set of easily-understandable and transparent systematic market risk factors: risk factors that cannot be diversified and exposure to which the market can thus be expected to reward with a risk premium. We have so far found no evidence that ESG issues are associated with a systematic market-risk factor and premium that could be reflected in the ALM and strategic asset allocation processes. Based on this, Zurich believes that ESG issues are best reflected at the level of selection of individual securities or assets. This approach is different from ‘thematic’ allocations, for instance, to so-called impact investments, within a certain asset class – i.e., for a given risk-return profile. Our approach to allocate to thematic investments through impact investing is described further in [section III](#).

Since ESG factors have an impact on the risk and return of assets, including ESG in the asset management process should heighten asset managers’ awareness of the risks and opportunities associated with these factors when making decisions on the securities or assets they select. It should also encourage conscious

choices around exposures to ESG-related issues. As an integral part of managing assets for Zurich, all our asset managers must include the following four basic requirements in their investment approach:

### **1. Training**

A large number of ESG factors can potentially affect risk and return. The channels through which they affect risk and return are sometimes complex, and vary from sector to sector. It is important that portfolio managers receive adequate and regular training to help them understand the economic importance of ESG, especially as ESG has only recently – and partially – been included in business school, finance or continuing education curriculums, such as the chartered financial analyst (CFA).

### **2. Access to information**

To reflect ESG issues in investment decisions, portfolio managers need access to relevant information in the form of ESG analysis, ratings, and data. This can be supplied by specialized external providers, dedicated in-house teams, or broker research.

### **3. Investment process**

A clear understanding is needed about the process by which ESG considerations are reflected in decisions to buy/sell, or overweight/underweight a certain security or asset. This process should be documented and consistently applied.

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## ESG integration



- Training
  - Information
  - Process integration
  - Active ownership
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### 4. Active ownership

At Zurich, active ownership is defined as proxy voting and engagement. Asset managers are required to actively execute proxy votes based on best-practice policies addressing ESG issues, and to integrate relevant ESG issues in discussions with investee companies, either as part of regular company meetings, or through separate channels. Zurich's proxy voting policy and guidelines are available [online](#). More details about our engagement process can be found in the [appendix](#).

For actively-managed portfolios with a focus on underlying fundamentals, these four basic requirements are particularly relevant to determine how ESG issues may impact expected risk-adjusted returns (based on the analysis of an asset's expected cash flows), associated risks, etc. Many of Zurich's investments are managed based on such 'fundamental' investment strategies. But some portfolios use other strategies, for example, a quantitative investment approach, or might passively replicate a benchmark index. For these investments, we decide on a case-by-case basis whether ESG integration can be achieved by using appropriate ESG benchmarks.

Investment Management always aims to appoint the best manager for each portfolio, whether internal or external. 'This ability to 'outsource' provides Zurich access to the world's best asset managers. Currently, Zurich's assets are managed by over 40 internal and external asset managers according to clearly-defined investment management agreements, objectives and guidelines, and we rely on the skill of these asset

managers to build portfolios that achieve our goals. As part of this approach, we expect our asset managers to fully reflect the risks and opportunities associated with ESG factors when choosing assets for our portfolios, based on the requirements described here. It is not our objective to systematically exclude companies or assets from the investment universe. Just as we do not determine exclusion criteria based on traditional financial metrics, such as maximum price/earnings ratios or minimum interest coverage ratios, we also do not specify exclusion criteria such as minimum ESG scores or ratings. We prefer to work closely with our managers to make sure that the requirements for ESG integration are reflected in their investment processes. Having said this, a company-wide process is also in place to assess specific ethical concerns or market failures. It can result in selective exclusions implemented consistently across insurance underwriting and investment activities.

Zurich expects that ESG integration processes will, over time, lead the market to a more efficient pricing of ESG factors. This will provide the right incentives to those seeking to raise capital in the market to deal deliberately and strategically with ESG issues. While the approach is economic in nature, we do believe that ESG integration will eventually also have positive environmental and social impacts.

See the [appendix](#) for a description of the tools, policies, and processes that we apply to make sure that ESG factors are indeed fully integrated in the investment process and in day-to-day investment decision-making.



## How to deal with climate change?

Every business and asset will be affected by climate change and the collective action taken to mitigate or adapt to it. This will be the case even if society successfully transitions toward a climate neutral economy, and, as envisaged by the Paris Accord, succeeds in keeping future temperature increases this century 'well below' two degrees Celsius. The impacts of climate change run through all the elements of our responsible investment strategy. How can we make sure that a proper assessment of risks and opportunities is reflected in investment decisions? How can we help finance measures to mitigate and adapt to climate change? How can we deal with the fact that many consequences of climate change will only materialize over a medium- to long-term time horizon? And how can we help to encourage changes that better enable financial markets to effectively deal with climate change, and approach it as both a risk and an opportunity?

Zurich has defined a clear strategy to reflect climate change in its investment approach and we are committed to action in eight areas:

- 1. Scenarios:** it is hard to take action without context. Zurich's Market Strategy and Macroeconomics team has defined high-level scenarios and is monitoring developments with the help of a scorecard that is updated regularly.
- 2. Strengthen ESG integration:** given its complexity and long-term nature, climate change represents a particular challenge for ESG integration. Additional data and tools are required to raise awareness among investment professionals and to support integration in investment strategies.
- 3. Benchmarks:** ESG integration practices might fail to effectively capture all climate change-related risks and opportunities. We are testing the use of special benchmarks that incorporate a climate risk assessment and will evaluate the application of such benchmarks for new and existing portfolios on a case-by-case basis.
- 4. Finance the transition to a climate neutral economy:** as part of our ongoing commitment to impact investing and our target to help avoid the emission of five million tons of CO<sub>2</sub> per year, we will evaluate green investments across different asset classes on an ongoing basis. See [section III](#) for more details.
- 5. Drive change through advocacy:** public and private sectors need to take decisive action. Zurich has defined clear positions on topics such as transparent risk disclosure, carbon pricing, etc. See [section IV](#) for more details.
- 6. Engagement:** as part of engaging with the companies in which we invest, climate change should be reflected on the agenda and considered in voting practices. See [appendix](#) for more details.
- 7. Selective exclusions:** recognizing the particularly harmful impact of coal on climate Zurich has developed a [Group approach](#) on selectively excluding companies related to the mining of or electricity generation from thermal coal from its underwriting and investing activities.
- 8. Net Zero portfolios by 2050:** working on transitioning our investment portfolios to net-zero GHG emissions by 2050 consistent with a maximum temperature rise of 1.5°C above pre-industrial temperatures, taking into account the best available scientific knowledge.

# Section III

Impact investing at Zurich: how we define and practice impact investing

Zurich is committed to investing up to  
**USD 5 billion**  
 in impact investments.

## Our annual targets



Zurich is committed to investing up to USD 5 billion in impact investments. At this level, we aim to avoid five million tons of CO<sub>2</sub> emissions per year, and, separately, believe we can make a positive contribution to the lives and livelihoods of five million people.

Entrepreneurs, governments, non-governmental organizations (NGOs) and others in both public and private spheres are turning to capital markets to search for – and fund – solutions to many of the pressing social and environmental issues of our time. Impact investments address these issues through the targeted, positive impact they have on society or the environment, while offering a financial return. Whereas **ESG integration** is the primary tool to capture the economic value associated with ESG factors and enhance long-term, risk-adjusted returns, impact investing is about identifying, and allocating capital to, investment opportunities that generate tangible positive impact for a given level of risk and return.

Every investment, regardless of asset class, has an impact on communities, people's lives and the environment. Companies or assets such as buildings and infrastructure are built and operated, and in the process, jobs are created or lost; products are introduced, sold and consumed, or services delivered; natural resources harvested and processed; energy produced and consumed; waste

and emissions created or mitigated. Accordingly, every investment has a footprint, both positive and negative, that affects the real economy, our environment and our communities. Tools have become increasingly available to measure such impacts. Examples are carbon emissions, or the share of 'green' and 'brown' revenues generated by portfolio companies. To better understand how Zurich's investments affect the environment, we strive to apply new data and tools, starting with measuring our carbon 'footprint.'

In contrast, impact investing is centered on positive impacts and focused on smaller, but dedicated parts of the portfolio. At Zurich, we define impact investing as investment opportunities that allow us to **intentionally** target a specific positive social or environmental impact and allow us to **measure** the impact achieved; these are **profitable**, meaning that they generate a financial return commensurate with their risk. Based on our experience as impact investor, we also differentiate between investments that are aligned with increasing our impact and those which serve to play a truly catalyzing role.

Footprinting	Impact investing	
	Impact	Deep Impact
<ul style="list-style-type: none"> <li>✓ Positive and negative impact</li> <li>✓ Measurability</li> <li>✓ Profitability</li> </ul>	<ul style="list-style-type: none"> <li>✓ Positive impact</li> <li>✓ Intentionality</li> <li>✓ Measurability</li> <li>✓ Profitability</li> </ul>	<ul style="list-style-type: none"> <li>✓ Positive impact</li> <li>✓ Intentionality</li> <li>✓ Measurability</li> <li>✓ Profitability</li> <li>✓ Additionality</li> </ul>



## **1. Intentionality – impact is more than just a ‘by-product’**

What sets impact investments apart is that they are carried out with a specific outcome in mind. The impact is not a side-effect; it becomes part of the investment objective. ‘Intentionality’ can be established through allocations to impact investments as part of a dedicated mandate (in which impact objectives are stipulated in portfolio guidelines, the investment management agreement, or in a ‘side letter’ agreement), or by reflecting impact criteria in the process to select investments for an existing portfolio. Intentionality can also stem from a specific project setup that by design targets a positive outcome, such as infrastructure that solely focusses on renewable energy generation, or social enterprises set up to solve a specific issue. Zurich defines the appropriate approach in the context of a specific asset class and investment structure.

## **2. Measurability – understanding what impact achieves**

When impact is part of the investment objective, it should be measured just like other investment objectives, such as risk, return or investment income. Zurich acknowledges that impact is not easy to measure. Data may not be readily available, data quality may be poor, and randomized control groups may be required to establish outcomes with scientific rigor. In most cases, the cost to get proper measurement of the outcomes will be prohibitive. As a result, Zurich is taking a pragmatic approach with respect to impact measurement, assessing approaches on a case-by-case basis. However, Zurich will always require that reasonable attempts are made to measure impact quantitatively. Measurement may be limited to specific indicators that do not cover the full breadth of impact objectives; it may

be supplemented by case studies; it may evolve, or it even may not be in place in the beginning if there is a solid commitment to establish it over time. However, Zurich will not regard any investment as an impact investment if no attempt is made to measure impact.

Standards around impact measurement, such as the Global Impact Investing Network’s (GIIN) Impact Reporting and Investment Standards (IRIS), The Investment Leaders Group’s (ILG) impact framework, or the Green Bond Principles’ (GBP) standardized impact metrics<sup>1</sup> are starting to emerge, complementing approaches established and applied by development finance institutions. Zurich encourages the use of these standards. As data quality improves over time and impact measurement gets more widely adopted, Zurich expects that capital can be allocated more efficiently to where impact is generated most effectively.

## **3. Profitability – generating impact alongside return**

While impact investing is distinct from grant-making philanthropy in that capital is always expected to be paid back to the investor, there is no general rule in the market regarding the return that an impact investment must generate. The return may or may not be a market-rate return. It could be zero, or very low, but it might also be comparable to the return on a non-impact investment of similar risk.

As institutional investors with a fiduciary responsibility to optimize economic returns for shareholders and policyholders, we must be comfortable that the return of an impact investment does, in fact, adequately compensate for the underlying market risks. We acknowledge that many pressing social and environmental issues cannot be solved in purely commercial settings, and that the role of grant funding and other sources of concessionary capital is

hugely important. Venture philanthropists may be willing to forgo any return, seeking only the repayment of principal. Mission-driven investors, high-net-worth individuals, foundations or endowments may accept a below-market return. However, given the massive scale of solutions required to solve issues such as climate change, resource scarcity, global education, global health and many other challenges, Zurich feels it is equally crucial that impact investments attract institutional investors with a fiduciary responsibility to optimize economic returns – even if this requires the use of public or philanthropic capital to de-risk investments. Only institutional investors command a pool of capital large enough to tackle many of the issues at hand.

## **4. Aligning and catalyzing – pushing the borders for even higher impact**

Zurich will target a range of impact investments: those who’s ‘impact’ is aligned with our stated impact objectives, with a focus on actively increasing our investments in assets in which we also have otherwise invested, such as for instance green bonds; and, on the other hand, those investments that are more ‘deep impact’ in nature and, as a result, require further effort in terms of investment processes, such as private market investments in emerging and frontier economies.

While impact investing has enjoyed rising popularity in recent years, both as a term and an investment style, for many decades it has been practiced under different names. Currently no generally-accepted or ‘official’ definition for impact investment exists. However, there is a consensus emerging around some of its key characteristics, and Zurich’s definition of impact investing is very much aligned with this consensus.<sup>2</sup>

<sup>1</sup> Find more information about IRIS (GIIN); see the ILG paper ‘In search of impact’ (2016), ‘In search of impact – Update’ (2019); recommendations on impact metrics are available in the Green Bond Principle’s [resource center](#)

<sup>2</sup> See for instance the Global Impact Investing Network’s [definition](#)

## Impact investing



- Intentionality
- Measurability
- Profitability

### Zurich's impact objectives: mitigating environmental risks and increasing resilience

By pooling risks, insurance helps to protect individuals or organizations from the financial uncertainties of life and the vagaries of our world. Providing insurance protection to individuals frees them from social constraints. Without insurance, individuals remain dependent on the support of the family or community, or risk poverty and destitution. And even in cases where family or community support is available, many shocks will continue to significantly affect the welfare of the poorest. As a global insurance group, serving millions of customers in over 210 countries and territories, and with a rapidly growing footprint in many emerging regions of the world, Zurich and its customers are directly or indirectly exposed to environmental and social challenges. Not all of these can be mitigated through insurance.

Through our impact investments we target positive outcomes in two main ways:

- Mitigating environmental risks by supporting a climate neutral economy and encouraging environmentally-friendly technologies.
- Increasing community resilience by helping to build 'community capital,' and addressing the needs of populations that lack traditional means to achieve such goals (the 'under-served populations'). At the same time, we also acknowledge that the impact-investment market is still in an early stage of development. The universe of impact investment is limited, albeit growing rapidly, and institutional investor commitment is crucial for the market's further development. It is also one of our explicit objectives to support the 'mainstreaming' of impact investing through collaborative engagement and investments. To support market development and achieve scale and portfolio diversification, we may also support investments targeting impacts beyond those already mentioned.



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## The five Cs

### 1 Physical capital

(infrastructure, equipment; etc.);

### 2 Financial capital

### 3 Human capital

(education, health, etc)

### 4 Social capital

(social relationships and networks, etc)

### 5 Natural capital

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## Mitigating environmental risks

There is strong evidence that climate change is happening, that it is influenced by human action and that it is leading to changes in extreme weather and climate events. Zurich recognizes the risk that environmental issues such as climate change pose to its stakeholders and its business performance.

Zurich's mission is to help its customers understand and protect themselves from risks, such as the risks associated with climate change. Mitigating climate change, and environmental protection more generally, is integral to sustainable value creation for both Zurich and society. (Visit our [webpage](#) to learn more about what we are doing to protect the environment, and read Zurich's position statement on climate change [here](#).)

As a signatory to the United Nations Global Compact, Zurich is committed to promoting greater environmental responsibility (UN Global Compact Principle 8) and to encouraging the development and 'diffusion' of environmentally-friendly ('green') technologies (UN Global Compact Principle 9). This includes achieving universal access to modern energy services, improving energy efficiency, and increasing the share of energy generated from renewable resources.<sup>3</sup>

Zurich will consider impact investments that help increase energy efficiency, generate renewable energy or mitigate climate change and/or protect the environment in other ways.

Impact target: avoid the emission of five million tons of CO<sub>2</sub> per year.

## Increasing community resilience

In addition to the pooling of risk, insurance can also help make communities and society more resilient to unforeseen shocks, for instance by sharing expertise on how to mitigate risks. Zurich's efforts to help communities reduce the impact of floods as part of our [flood resilience program](#) are an example of how we use our expertise to increase the resiliency of our communities.

However, resilience should not be viewed too narrowly. A holistic approach is required – one that takes into account communities' needs. In a white paper on flood resilience we find that "to be effective, resilience activities should encourage efforts to maintain and raise the standard of living of those affected by [disaster]." An effective way to supplement more narrow measures of resilience is to look at community capital, or 'the five Cs': physical capital (infrastructure, equipment; etc.); financial capital; human capital (education, health, etc.); social capital (social relationships and networks, etc.); and natural capital. Sustainable economic growth and well-being go hand-in-hand with risk preparedness.

Zurich will consider impact investments that help to build community capital and make goods and services more accessible to populations that are not adequately served by traditional investment means.

Impact target: make a positive contribution to the lives of five million people in need.

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<sup>3</sup> See [www.unglobalcompact.org](http://www.unglobalcompact.org) and the 10 principles



## Investment approach

Zurich believes that impact investment opportunities exist across various asset classes and across a spectrum of investments with more or less catalytic effects. We are committed to evaluating impact investment opportunities across the spectrum and, over time, build a portfolio of impact investments of up to USD 5 billion.

In identifying potential impact investments, we will assess whether the investment meets our definition of impact investing (intentionality – measurability – profitability), supports our impact objectives (mitigating environmental risks and increasing community resilience), contributes to our impact targets (avoid the mission of five million tons of CO<sub>2</sub> per year and make a positive contribution to the lives of five million people in need) and/or, contributes to development of the impact investing market.

However, we also believe that impact investing will only be sustainable as an investment 'style' if it can be integrated into our overall approach to investment management. Opportunistic investments can supplement the portfolio occasionally. But in general, we want impact investments to be an integral

part of the portfolio, not just one-offs. Consequently, in addition to the criteria already described here, we will also assess impact investment opportunities along the following lines:

- **Risk and return profile:** Is the risk/return profile in line with Zurich's risk-factor based approach to ALM and strategic asset allocation? (See [section I](#) or [Investment Management: a creator of value in an insurance company](#) for more details on insurance investment management.)
- **Scale:** Is the universe of assets for a given type of impact investment large enough to define a meaningful allocation, build a diversified portfolio, and re-invest capital over time?
- **Structure:** Does Zurich, or an institutional-quality external asset manager, have the capability and expertise to manage the asset?
- **ESG risks:** As with any other investment, we will assess ESG risks associated with the underlying asset as part of a holistic asset selection process. Note that we do not equate ESG performance with impact (see also [section II](#)).

As a final point, regulation and other constraints that are relevant to an insurance company also need to be weighed.

Footprinting	Impact investing	
	Impact	Deep Impact
<ul style="list-style-type: none"> <li>• Ex-post: measurement</li> </ul>	<ul style="list-style-type: none"> <li>• Ex-ante: dedicated allocation or systematic tilt in portfolio</li> <li>• Limited complexity</li> <li>• Ex-post: measurement</li> <li>• Examples: green and social bonds; overweight in renewable energy assets; health care private equity fund</li> </ul>	<ul style="list-style-type: none"> <li>• Ex-ante: dedicated allocation or systematic tilt in portfolio</li> <li>• More complexity: new and less familiar risks; non-traditional structures; smaller transaction size; increased due diligence effort</li> <li>• Ex-post: measurement</li> <li>• Examples: backing first-time environmental technologies fund; emerging and frontier market private equity or debt; pay-for-performance structures</li> </ul>

## Investing in green, social and sustainability bonds

The unique characteristic of green, social and sustainability bonds (also referred to as use-of-proceeds bonds) is the pre-defined use of proceeds according to criteria to which issuers commit, clearly linking the investment to specific projects that allow the bond issuer to report a result or impact. The market for green bonds has been developing rapidly since broadening from the traditional issuer base of supranational institutions in 2014. Use-of-proceed bonds can take many forms: standard recourse-to-the-issuer debt obligations, revenue bonds, asset-backed securities, project bonds, etc., and are issued by supranational institutions, state agencies, corporates, and municipalities. Through its commitment to this market, Zurich is seeking to capture opportunities across the universe of green, social and sustainability bonds.

### Impact objectives

- Helping communities to protect the environment and mitigate or adapt to climate change.
- Supporting the development and spread of environmentally-friendly technologies.
- Helping communities to become more resilient in the face of environmental and social challenges.

While many green bonds are focused on issues around climate change, Zurich also invests in green bonds that provide financing to other projects that offer benefits to the environment, such as sustainable water use, waste management, biodiversity, etc. Zurich also systematically invests in social and sustainability bonds.

### Structure

To capture the breadth of credit instruments and issuers represented in the green, social and sustainability bond market, Zurich has defined two separate but complementary approaches for investing in them.

#### 1. Dedicated green bond mandate for supranational green bonds issued in U.S. dollars:

Assets with minimum credit risk, such as those issued (or explicitly guaranteed) by national governments or supranational institutions, form a very significant part of Zurich's asset allocation. In line with our established approach to define portfolios along credit sector- and currency lines, Zurich has carved out a dedicated green bond mandate to invest in U.S. dollar-denominated green bonds by these issuers on its North-American balance sheet. This mandate is managed by an external asset manager, BlackRock, and will be funded with up to USD 1 billion.

#### 2. Integrating green, social and sustainability bonds in existing fixed-income portfolios:

Beyond the dedicated mandate just described, Zurich has chosen to capture other credit sectors, issuers and currencies through a complementary approach. Rather than creating multiple green bond portfolios reflecting different credit sectors and currencies, or cross-currency, cross-credit-sector portfolios that would not fit Zurich's established approach to credit investing, an internal green bond expert was appointed to coordinate and facilitate use-of-proceed bond investments across Zurich's many existing balance sheets, portfolios and asset managers. In this way, Zurich has allocated over USD 2 billion to use-of-proceed bonds and is expecting to maintain and potentially further grow this approach.

### Principles

Zurich supports the International Capital Market Association's (ICMA) Green Bond Principles, Social Bond Principles and Guidelines for Sustainability Bonds.<sup>4</sup> To evaluate green, social or sustainability bond investments, supplementing the ICMA's principles and in addition to economic considerations, Zurich applies the following criteria:

#### The quality of impact and direction of travel

- When analyzing use-of-proceeds bonds and deciding whether they should be classified as impact instruments, Zurich focuses primarily on the projects to be financed, and their ex-ante potential for positive impact.
- If the ex-ante potential of the projects to contribute to environmental or social improvements is promising, the proposed projects or selection framework will be evaluated in the context of the issuing entity. Zurich gauges the issuer's sincerity of intent, and analyzes to which degree the projects are anchored in the issuer's overall environmental, social or sustainability strategy. Even initial steps, if rooted in a sound strategy and critical to progress, will be preferred over opportunistic approaches that are divorced from the issuing entity's business model or sustainability strategy.
- Zurich will also carefully analyze potential ESG risks that might be associated with green or social projects, as well as the issuer's track record in implementing projects that do pose such ESG risks.

<sup>4</sup> Visit the [GBP/SBP website](#)



### **Incremental benefits are better than no progress at all**

- Zurich acknowledges that not all activities with environmental benefits are considered equally 'green' by various stakeholders, and that full agreement on the net environmental benefits is not always possible, particularly if taking a full life-cycle view. In general, Zurich believes that incremental environmental benefits are better than the absence of progress, and sees green bonds as a good instrument to engage issuers with less-than-perfect environmental credentials, as long as the trajectory of their actions is promising.
- However, Zurich acknowledges that there are sectors which, by definition, have a challenging role when it comes to addressing the four key areas of environmental concern as spelled out in the Green Bond Principles: climate change, natural resource depletion,

loss of biodiversity, and air, water or soil pollution. When incremental green benefits are targeted within an inherently 'brown' activity, Zurich will pay specific attention to the level of ambition displayed in the proposed improvements in order to classify such a bond 'green' rather than just 'conventional.'

- Zurich believes that, over time, impact reporting is the right instrument to assess the relative environmental as well as social benefits of underlying activities.
- As the green, social and sustainable bond market grows and develops, investors – including Zurich – will learn more about the environmental and social benefits of different activities. Zurich will carefully evaluate the intended use of proceeds of each green, social and sustainable bond and, on a case-by-case basis, assess their quality as an impact instrument.

### **A transparent process is needed to administer proceeds and ring-fence funds**

- The issuer must have a clear and transparent framework to allocate funds from a use-of-proceeds bond to underlying projects use-of-proceeds. Categories of eligible projects must be clearly defined.
- The proceeds from use-of-proceeds bonds should be held in a separate account or be otherwise tracked.
- So-called 'second opinions' on these processes provided by third parties are welcome and encouraged, but are not an absolute requirement if the issuer publicly provides complete and transparent information.

- While Zurich may invest in bonds issued by companies whose whole portfolio of activities could be considered green or social (often referred to as pure plays) in the absence of a clear use-of-proceeds provision and impact reporting, we will not deem such bonds ‘green bonds,’ ‘social bonds’ or ‘sustainability bonds.’

### **The issuer must be committed to impact reporting**

- A complete list of projects receiving funding from use-of-proceeds bonds must be made available to investors once proceeds are disbursed. Where confidentiality requirements limit the amount of details that can be made public, generic descriptions are acceptable.
- Issuers must be committed to make good-faith efforts over time to report on the positive environmental and social impact of the projects. Zurich is fully aware of the challenges and limitations of impact reporting and it is understood that quantitative performance measures may not always be readily available. Zurich expects issuers to report at least one relevant metric per category of projects funded, even if the metric cannot be established for the complete portfolio of projects.
- Zurich welcomes independent third-party verification of impact metrics, but does not require it.

### **Assessing ESG factors at the issuer level – a separate process**

Zurich believes that the defining characteristics of use-of-proceeds bonds include the fact that their proceeds are used in a pre-determined way, are clearly linked to specific projects, and that their impact can be measured. The impact potential of a use-of-proceeds bond is primarily determined through the process described above. The issuer’s

‘ESG’ rating is neither a necessary nor sufficient condition to define a green, social, or sustainable bond. However, ESG factors do provide valuable insights into the potential risks and expected returns across asset classes. Accordingly, Zurich uses the issuer’s ESG rating in a second step after a use-of-proceeds bond has been identified as an impact instrument in order to evaluate risks and opportunities associated with specific ESG factors and using those to determine a bond’s fair value. ESG factors may very well affect the cost of capital, and issuing a green bond may signal lower risks to investors with regards to its overall ESG profile. Zurich would expect these characteristics to reduce cost of capital for all securities of the same issuer, not just that issuer’s green, social or sustainability bonds. (See also [section II](#)).

### **Transparency in environmental finance is a prerequisite for ‘additionality’**

Large investments are needed to counter the threat of catastrophic global warming and tackle other environmental issues. But it is a matter of some debate whether additional investments are necessary beyond those to fund ‘business-as-usual’ – and if green bonds should finance only activities that otherwise would be unable to raise financing.

- Zurich believes that transparency is necessary to make progress and encourage additional investment. Green bonds are an excellent tool to make finance flows into environmentally beneficial projects visible. Zurich encourages market participants to highlight environmental projects through the use of green bonds and is convinced that a transparent market will make it easier to encourage additional projects and investments. To understand what progress is being

made toward closing the climate finance gap, we first need to make the flows visible.

- Refinancing is a crucial activity and the concept of a green bond can be applied to both original funding and refinancing activities. Besides providing a clearer picture of investment volumes, the green bond framework sheds light on the impact achieved. Zurich hopes that, over time, capital can be allocated more efficiently to where the most effective impact is generated.
- A large and liquid green bond market provides a good entry point for mainstream investors, financial intermediaries and issuers, allowing them to take up issues related to environmental sustainability and climate change. We believe that an improved ‘environmental literacy’ in the financial sector through low-risk instruments such as green general-obligation bonds is a pre-requisite for increasing risk-transfer elements, paving the way for green revenue or project bonds, or other, more risky investments.

Zurich considers green bonds to be an important tool to raise awareness – both in the financial community and among the general public – of climate change and other environmental challenges, as well as of the opportunities to provide financing to address these.

### **Engagement**

Zurich is a member of the executive committee that governs the ICMA’s Green Bond Principles. It is also a member of formal and informal working groups that play an active role in helping to develop the green bond market. Its activities reflect Zurich’s particular interest in engaging other market participants in active dialogue on topics related to impact reporting.

### Impact investing in private equity

Impact investing has its roots in providing private – often venture – capital to social enterprises. Over the years the concept spread to other parts of the private equity universe. In many ways, private equity as an asset class is particularly suited to impact investing: the companies receiving capital from private equity investors usually tend to be small and agile, and engage in a more limited number of activities that can be more easily evaluated against impact objectives; a closer relationship between investor and investee also makes it easier

to use innovative approaches, such as impact reporting; and, particularly in emerging and high-growth economies, private equity is often the only capital available to fund growth.

#### Impact objectives

- Making goods and services more accessible to underserved populations.
- Supporting efforts to build community capital.
- Supporting development and diffusion of technology that is environmentally-friendly.
- Helping communities to protect the environment and mitigate climate change.

The following table illustrates some typical activities targeted by impact investing:

	Increasing community resilience		Mitigating climate risk	
	Building community capital	Serving underserved populations	Fighting climate change	Green technologies
Education	✓			
Healthcare	✓			
Housing	✓			✓
Financial services	✓			
Agriculture	✓			✓
Energy	✓			✓
Transport	✓			✓
Green technology	✓			✓
Other	To be assessed on a case-by-case basis			

This table is an illustrative example only and is not an exhaustive list.



What constitutes an impact investment may be determined by the context. A private hospital provider in Western Europe may not be considered an impact investment. But a private healthcare services provider in an emerging or frontier economy, serving parts of the population trying to escape poverty, may contribute significantly to community resilience. Similarly, care for the elderly people in low-income communities in the U.S. may form part of an impact investing strategy. An investment in an industrial company in North America may not be considered an impact investment, but a similar investment in a frontier or emerging economy may create the only available high-quality employment in a specific location. When being considered for impact investment, fund managers' investment strategies will be evaluated with regard to impact objectives on a case-by-case basis.

#### Structure

Zurich typically invests in private equity through fund investments and, in certain specific cases, through co-investments. An in-house specialist team is responsible for selecting private equity fund managers and assessing co-investment opportunities. Investments must be approved by an investment committee overseeing alternative investments. Zurich follows the same process for impact investments, with investments being held as part of existing private equity investment portfolios. Zurich will generally not consider investing with fund managers targeting below-market financial returns, or first-time fund managers with no proven track record of value creation.

#### Principles

**Managers need not identify their offerings as impact investment funds, but their investment strategies must be in line with Zurich's impact objectives**

Zurich will evaluate fund managers' strategies in light of investment theme (e.g., 'environmental technologies' or 'access to finance'), targeted customer segment (e.g., 'emerging consumer' or 'low-income communities'), sector focus (e.g., healthcare or education) and geographic focus (e.g., frontier and emerging markets). Zurich does not expect fund managers to 'brand' and position their fund as an impact investment fund, but the manager must be committed to impact reporting.

**The fund manager needs to show a commitment to impact reporting**

Fund managers must be committed to report on relevant non-financial metrics in line with the manager's investment strategy. Zurich acknowledges the challenges and limitations of impact reporting and it is understood that quantitative performance measures may not always be readily available. But Zurich expects good-faith efforts made over time to report on the positive impact achieved. Zurich welcomes independent third-party verification of impact metrics, but does not require it.

**A solid process to assess ESG factors does not make an impact investment**

ESG factors provide valuable insight into the assessment of risk and expected return of every private equity investment (see also [section II](#)). However, the process to evaluate risks and opportunities

associated with specific ESG factors is separate from generating impact. It is neither a necessary nor sufficient condition to define something as an impact investment. Zurich does, however, consider targeted improvements in ESG practices at the level of investee company operations as impact investing if they form a systematic part of the company's strategy and attempts are made to measure and quantify improvements.

#### Engagement

Zurich is a member of the Emerging Market Private Equity Association's Impact Investing Council.

#### Impact in Infrastructure private debt projects

The long term nature of private debt investments suits impact investment goals well providing a unique opportunity to access assets which have a positive social or environmental impact, such as sustainable infrastructure.

#### Impact objective

- Supporting the development and spread of environmentally-friendly technologies.
- Aiming to address or mitigate a specific social, socio-economic and/or well-being issue and/or seek to achieve positive measurable social, socio-economic and/or well-being outcomes benefiting underserved populations

#### Structure

Zurich invests in infrastructure through direct private debt. Zurich considers all of the main infrastructure sectors including transportation, social, energy and power and we invest in both brownfield and greenfield deals although with restrictions around the latter.

#### Principles

Zurich's definition of 'impact infrastructure' is based on the [Green and Social Bond Principles](#) categorization. In order to facilitate the categorization Zurich differentiates between financing environmental and social impact infrastructure. Project developers must be committed to report on relevant non-financial metrics in line with the manager's investment strategy.

#### Reducing energy use and carbon emissions of our Swiss real estate portfolio

Real estate, including commercial and residential property, consumes a significant amount of energy and is a major source of carbon emissions. Institutional investors are major owners of real estate assets. Zurich has allocated over six percent of its investment portfolio to real estate, about half of which is currently held in Switzerland. We are committed to reducing the energy consumption and carbon emissions of our Swiss real estate portfolio by 20 percent by 2020, and 80 percent by 2050, against a 2010 baseline and we are investing in refurbishing and re-developing our properties to achieve these targets.

#### Impact objective

Mitigating climate change.

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We are committed to reducing the **energy consumption** and **carbon emissions** of our Swiss real estate portfolio by

20%  
by  
2020

and

80%  
by 2050.

### Structure

Impact objectives are reflected in all relevant real estate investment processes:

#### *Asset and property management*

- Energy accounting and controlling for all properties.
- Recording carbon emissions for all properties.
- Reducing carbon emissions through operational improvements.

#### *Transactions*

- Integration of relevant performance indicators into the due diligence process.

#### *Development and refurbishment*

- Carbon emissions reflected in strategic planning and targeted building standards.

### Principles

#### **The optimal measures to reduce energy consumption and carbon emissions must be defined on a case-by-case basis**

Zurich believes that environmental sustainability contributes in an important way to the long-term risk-adjusted performance of a real estate portfolio. However, optimal environmental performance of an asset must be determined within the context of each individual property. Not every property should be certified with the highest possible 'green label.' Not every

property can be equipped with a heat pump. Retail space in a prime business district requires a different approach than a multi-family home in a suburban setting. Measures that can be used to refurbish a property occupied on an ongoing basis by tenants differ from those that can be used in a complete re-development. Rather than setting absolute standards across the portfolio, or building a separate portfolio of particularly green properties, we will determine the optimal measures to achieve our overall targets in the context of each and every property, transaction or development project.

#### **Medium-term targets must be complemented by long-term objectives**

Real estate is a 'slow moving' asset class, and the stock of properties in a portfolio typically does not get turned over quickly. Zurich has defined medium-term energy and carbon-emission reduction targets that can be reached through operational improvements and soft refurbishments. Long-term objectives will be achieved by increased use of renewable energy sources, more significant re-development actions and portfolio transactions.



## Impact measurement

Zurich developed an impact measurement framework to measure the impact across its impact portfolio in terms of two defined impact metrics: 'CO2-equivalent emissions avoided' and 'the number of people who benefited.'

### Why we measure

On top of tracking the exposure and targeted returns, Zurich wants to know what each of the investments achieve in terms of impact, and to measure its contribution toward its impact investment objectives: mitigating environmental risks and increasing resilience. Measurement helps to make better investments decisions and allows communication of Zurich's value to its shareholders. It also demonstrates that financial returns can be balanced with environmental and social returns.

### How we measure: a 2 step approach

The first step is gathering reported impact numbers. Zurich's impact measurement methodology is based on impact numbers reported by the issuers of impact investing instruments. Zurich aims to collect only the impact an impact investor is financing; impact investors are encouraged to report pro-rata shares. As Zurich wants to match the impact to its portfolio's invested dollars for respective years, annualized impact numbers are collected.

The second step requires the aggregation on portfolio level, across the different asset classes. Zurich's impact framework methodology looks only at the impact created by Zurich's share of investments.

## Shaping a more resilient tomorrow

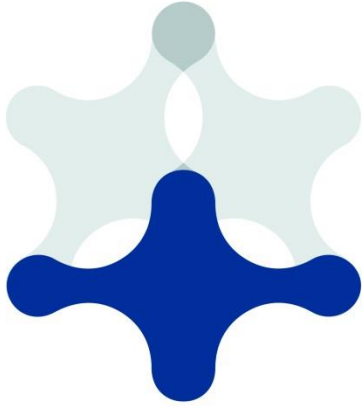


# Section IV

Advancing together: responsible investment  
can make a difference only if it becomes  
truly 'mainstream'

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## Advancing together



- Innovation
  - Collaboration
  - Public advocacy
- 

Responsible investment as a holistic concept is still relatively new, and responsible investment practices have yet to be established firmly within mainstream investment processes. The ultimate objective of responsible investment – to create social and environmental value alongside financial returns – can only be achieved if the various responsible investment practices become truly embedded in mainstream investment management.

This will require:

- High-quality disclosure of ESG data, supported by adequate regulation and policy.
- Effective mechanisms to create cost transparency by internalizing environmental and social externalities (e.g., polluter pays principles; carbon price), supported by sensible and stable regulation and coherent sustainability policy.
- Increased focus on impact metrics that allow policy makers, businesses and investors to align contributions to objectives (e.g., UN Sustainable Development Goals).
- Ongoing investment, both public and private, in education, training, research and tools.

Only by acting collectively can this change be achieved.

ESG factors can be efficiently priced only through collective action, and with a shared understanding of how ESG factors affect risk, opportunity, and economic outcomes both in businesses and society. That pricing signal is the only incentive capable of ensuring those seeking to raise capital in the market to take an effective and strategic approach to ESG issues.

Collective action can spread the spirit of impact investing across markets and mobilize capital on the scale needed to tackle pressing social and environmental issues. Close collaboration is needed to bring investors, businesses, public actors, and NGOs together to design the instruments capable of delivering the full, desired impact.

We don't completely understand how non-financial factors affect assets' performance and how, in turn, our actions affect non-financial value generation. Mutual effort is needed to shed light on these important aspects.

Mindful of the need to share information, Zurich seeks to work with other industry participants. It also supports industry initiatives and engages with stakeholders and policy makers to advance responsible investment practices and to help establish a truly sustainable financial market system. In addition to being a signatory of the Principles of Responsible Investment (PRI), Zurich supports a number of collaborative initiatives and works closely together with many others in the field to help advance responsible investment practices and identify new solutions.

Visit our [webpage](#) to learn more about our engagement.

# Section V

Appendix: creating a responsible investment culture

## Responsible investment in individual objectives

The following objectives are reflected and assessed as part of Zurich's individual objective setting and assessment process:<sup>5</sup>

Objective	Measurement	Who
Achieve impact targets	<ul style="list-style-type: none"> <li>Progress made toward USD 5 billion impact investment target</li> <li>Progress made toward avoiding 5 million tons of CO2 emissions per annum</li> <li>Progress made toward reaching five million people in need through impact investments</li> </ul>	Global Group Investment Management team
Show leadership in responsible investment	<ul style="list-style-type: none"> <li>Supports or, when applicable, leads locally the implementation and ongoing execution of all relevant responsible investment processes, including the interaction with internal or external asset managers as applicable</li> </ul>	Strategy Implementation team
Effectively integrate environmental, social, and governance (ESG) factors into security selection decisions for all in-scope portfolios	<ul style="list-style-type: none"> <li>ESG integration minimum standards achieved for all in house teams with in-scope portfolios</li> </ul>	Strategy Implementation team
	<ul style="list-style-type: none"> <li>Makes active effort to learn about ESG issues and how they affect risk and return</li> <li>Reflects third-party ESG data and analysis in security/asset selection and can provide examples of how this has influenced investment decisions; can discuss ESG risks and opportunities in the portfolio</li> <li>Raises ESG issues when interacting with investment counterparties (analyst; investee company representative; property manager; etc.); provides examples of such interaction</li> </ul>	Portfolio managers
Effectively integrate responsible investment into the asset manager life-cycle process	<ul style="list-style-type: none"> <li>Proactively engages with external asset managers on the topic of responsible investment and can explain asset managers' ESG integration practices</li> <li>Prepares and facilitates discussion of responsible investment practices and ESG factors as part of portfolio review and relationship meetings; provides examples of such interaction</li> </ul>	Strategy Implementation team
	<ul style="list-style-type: none"> <li>Proactively discusses, documents and assesses ESG integration practices in manager searches</li> <li>Prepares and facilitates discussion of responsible investment as part of relationship meetings</li> </ul>	Manager Selection team

<sup>5</sup> Each member of the global Group Investment Management team is expected to be assigned one or multiple objectives related to responsible investment relevant in the context of a specific role. The language in this section serves as a template for line managers to determine individual objectives for their teams as part of Zurich's annual objective setting and performance evaluation process, and may be adapted to reflect individual circumstances. The language refers to objectives for a specific year, shown for 2018, and is updated on an annual basis.

Objective	Measurement	Who
Invest in green bonds	Grow investments in green, social and sustainability bonds, subject to market conditions and portfolio constraints.	Strategy Implementation team
	Evaluates, or supports the evaluation, of green bond investment opportunities in-line with the green bonds investment strategy	Green Bond Coordinator, portfolio managers
Effectively integrate ESG factors into asset selection decisions	Actively supports the implementation of the global real estate ESG integration approach	Heads of Real Estate
Assess climate change-related macroeconomic risks	<ul style="list-style-type: none"> <li>Formulate and review annually high-level climate change macro scenarios</li> <li>Identify and monitor relevant metrics/ actions indicative of progression on a specific scenario pathway</li> </ul>	Head of Macroeconomics, global macroeconomist
Reduce carbon footprint of the real estate portfolio	Steady progress toward reducing CO <sub>2</sub> emissions per m <sup>2</sup> by 20% by 2020 relative to the 2010 baseline	Swiss Real Estate team
Effectively integrate Environmental, Social, and Governance (ESG) factors into the Private Equity investment process	<ul style="list-style-type: none"> <li>Proactively discusses, documents and assesses fund managers' ESG integration practices</li> <li>Proactively engages with fund managers on the topic of responsible investment and can explain fund managers' ESG integration practices</li> </ul>	Private Equity team
Invest in impact private equity funds	<ul style="list-style-type: none"> <li>Identify, evaluate and select impact investment opportunities in-line with impact investing strategy</li> <li>Make steady progress toward allocating 10% of PE NAV to impact investing opportunities.</li> </ul>	
Support team in implementing the responsible investment strategy	<ul style="list-style-type: none"> <li>Participate in regular update calls</li> <li>Provide update to the team</li> <li>Engage in collaborative initiatives</li> <li>Support responsible investment processes</li> </ul>	Responsible Investment Champions

## Responsible investment technical competency

Zurich applies a systematic process to define technical and managerial competency requirements for standardized position profiles used for recruiting and to determine training and development actions. Zurich has assigned the following technical competency requirements to all investment professionals (level depending on respective function):

### 1. Basic

- Understands the relevance of the Zurich Basics in general, and specifically 'sustainable value creation', in an insurance investment management context.
- Has basic understanding of Zurich's overall responsible investment approach.
- Is familiar with the basic terminology of responsible investment.
- Understands the commitment Zurich has made as a signatory of the Principles for Responsible Investment (PRI).

### 2. Intermediate

- Has a good understanding of, and explains, Zurich's overall responsible investment approach.
- Understands the concept of 'impact investing.'
- Understands the concept of 'ESG integration' and the principles underpinning it.
- Understands where and how, ESG factors can be integrated into the investment process for relevant asset classes.
- Where relevant, interacts with fund managers on all aspects of the responsible investment approach.

### 3. Advanced

- Has an excellent understanding of the concept of 'ESG integration' and the principles underpinning it.
- Understands how ESG factors drive investment risk and return and uses ESG data and research.
- Assesses ESG factors and reflects them in investment analysis, recommendations or decisions.
- Is able to discuss ESG-related issues with representatives of investee companies or, where relevant, fund managers.
- Where relevant, evaluates fund managers on all aspects of the responsible investment approach.

### 4. Expert

- Monitors and analyses the marketplace and demonstrates deep knowledge of responsible investment practices, leading the design and implementation of Zurich's responsible investment strategy.
- Has a good understanding of corporate responsibility concepts and an excellent understanding of responsible investment in the context of Zurich's corporate responsibility strategy.
- Builds a relevant network with peers and industry participants and represents Zurich in relevant industry initiatives with the objective to advance responsible investment practices and set the agenda in terms of responsible investment for the industry.
- Communicates and advocates Zurich's responsible investment approach to internal and external audiences.
- Uses contacts and networks to source potential impact investments and supports the implementation of impact investing mandates.

## Active engagement: responsible investment champions

Responsible investment has to be reflected in top-down strategy and processes but, equally importantly, bottom-up engagement is required for responsible investment practices to become part and parcel of everyday investment decision-making. At Zurich, each investment management team has chosen a responsible investment champion. The responsible investment champions:

- support their teams in implementing and improving responsible investment processes
- engage in collaborative initiatives, such as the PRI or others
- share relevant research, news or other information related to responsible investment practices with their teams and
- form part of a global network of over 20 responsible investment champions who exchange views and their experiences in regular conference calls.

# Section VI

## Appendix: ESG integration



## Scope of ESG Integration

For the current implementation phase of Zurich's responsible investment approach, we are considering the following asset classes as **in-scope**:

- Active non-'quant' equity strategies.
- Active credit (financial credit; non-financial credit; municipal debt; direct lending).
- Passive investment strategies for equity and credit.
- Private equity.
- Real estate (direct investments).

The following asset classes are considered to be **out-of-scope**:

- Sovereign bonds<sup>6</sup>
- 'Quant' investment strategies for equity and credit (in-scope for active ownership only)
- Asset backed securities and covered bonds
- Money-market funds and cash
- Hedge funds
- Mortgages
- Certain legacy investments (no further investment decision to be made).

For passive or 'quant' mandates, active ownership practices are the main applicable element of ESG integration. On a case-by-case basis we will decide whether ESG integration can be achieved through the use of appropriate ESG benchmarks for these mandates. Where ownership of voting rights lies with a fund vehicle over which Zurich does not have control, active proxy voting is not applicable.

## ESG integration for in-house securities mandates

The way in which different in-house asset management teams manage equity or fixed income portfolios can vary significantly depending on the

structure and profile of local insurance liabilities (for example, the mix of general and life insurance business, and the specific type of insurance product offered); the size of the portfolio and portfolio management team; local regulatory requirements; local market structure; etc. In a few instances in-house asset management teams also manage specific funds that form part of insurance products offered directly to clients. As a result, the approach to ESG integration will also vary between teams and it is the responsibility of the local Chief Investment Officer to define the optimal approach together with the team. However, while some best practices may not be applicable under all circumstances, minimum standards related to the four basic requirements of ESG integration (described in this text) apply across teams:

### 1. Training

#### *Minimum standard*

- **Responsible investment competency** assigned to asset management team.
- Training modules covering assigned competency levels completed successfully.

#### *Best practice*

- Additional relevant training through seminars, webinars, etc.
- Review of selected academic research; responsible investment publications; etc.

### 2. Access to information

#### *Minimum standard*

- Access to MSCI ESG manager platform for all portfolio managers and investment analysts.

#### *Best practice*

- Use of ESG data from other data providers, such as Bloomberg, etc.
- Use of ESG research and analysis provided by brokers.

- Encouraging brokers to reflect ESG issues in research and analysis.

### 3. Investment process

#### *Minimum standard*

- Review of ESG research before making security selection decisions.
- Other things being equal preference for issuers with superior ESG performance.
- Integration of ESG risk exposure and exposure to controversial business practices in reporting to the local ALM investment committee (ALMIC).
- Discussion of ESG risks and opportunities at investment team meetings.

#### *Best practice*

- Integration of ESG factors into bottom-up equity or credit investment research.<sup>7</sup>
- Integration of ESG factors into industry sector analysis.
- ESG analytics at a portfolio level.

### 4. Active ownership

#### *Minimum standard*

- Execute votes for public equity holdings in line with Zurich's proxy voting policy.
- Reviewing ESG research before interacting with investee company management (through existing channels such as investor meetings or calls, etc.) and discussion of relevant ESG issues besides other material issues.
- Use of PRI clearinghouse platform for engagement activities on priority topics.
- Discuss active ownership examples and progress in annual meetings between local teams and Zurich's Group Responsible Investment team.

<sup>6</sup> Sovereign bonds: disciplined ALM practices and, in some cases, insurance regulation require Zurich to hold substantial amounts of minimum-risk assets denominated in local currency to back local liabilities. Zurich does not generally manage any multi-currency sovereign bond portfolios that would allow ESG factors to influence issuer selection.

<sup>7</sup> Only few Zurich teams conduct bottom-up research in-house

### *Best practice*

- Execute votes for public equity holdings in line with Zurich's proxy voting policy.
- Pro-actively establishing and maintaining dialogue with brokers, ESG data providers, industry bodies, investee companies with material ESG issues, or regulatory bodies to support responsible investment matters Zurich has identified.
- Initiating or joining engagements on priority topics with external asset managers or peers.
- Actively taking on and championing topics for engagement through the PRI clearinghouse platform or other suitable channels.

### **Manager review**

ESG integration practices at in-house investment management teams are reviewed through Zurich's individual objective assessment process (see [Responsible investment in individual objectives](#) for more detail) and each team reports on responsible investment practices on an annual basis through a standardized reporting format.

### **Manager selection for external mandates**

At Zurich, Group Investment Management always aims to appoint the most suitable manager for each portfolio, whether internal or external. Currently roughly two-thirds of Zurich's assets, and an even higher proportion of securities mandates, are managed by external asset managers. A stringent, fact-based manager evaluation process is applied. Selection criteria include the performance track record, investment philosophy and process, responsible investment practices, research and trade execution capabilities, risk management, organization and operations processes and costs. A dedicated manager

selection team is responsible for this process. Zurich's asset manager selection skill and capabilities provide a distinct competitive edge relative to Zurich's major insurance peers, who tend to manage their investments in-house. It allows Zurich to flexibly decide on the best investment management skills available, be it either in-house or outsourced, to manage different mandates.

### **Alignment in investment strategy**

Alignment between an outsourced mandate and Zurich's profile and duration of liabilities is achieved through investment guidelines, which provide a set of rules the portfolio manager has to observe when managing the portfolio. It includes investment objectives, describes the investments universe, benchmarks and outlines investment/risk limits and restrictions. In this set of rules, the duration of a fixed income portfolio is clearly stated and to what degree the manager can deviate from it. As an example: the duration of the portfolio is 5 years and may deviate from this target duration by +/- 1 year. Zurich has investment guidelines for every portfolio and the weighted combination of all the fixed income durations of our portfolios tie into the duration of our liabilities.

### **Considering the long-term financial and non-financial performance of assets**

When selecting asset managers we examine how the manager, more specifically their analysts evaluate securities and how that information is used in the portfolio construction. For more specific information on integrating ESG information refer to the next section.

A mid to longer term horizon / low turnover portfolio is always preferable to us since trading is expensive, both in terms of brokerage fees and use of liquidity. Moreover, in recent years market participants also face decreasing liquidity in credit markets (a large part of our investments) which as a consequence has increased the importance of longer term investment horizons.

However, we do not force or otherwise incentivise our asset managers to mid and long term views, as this is hard to prescribe and measure and could furthermore have effects that negatively impact performance.

### **Performance evaluation and remuneration**

We formally assess all portfolios and asset managers on a quarterly basis on both service and performance. All assessments are recorded and underperforming portfolios are put on a watchlist and treated as is specified in our policies. Consistently underperforming managers are de-selected and portfolios assigned to a new asset manager.

As outlined earlier we direct the asset manager with the investment guidelines which determine how they have to invest the funds. If the liabilities are long, so will be the duration of the portfolios. We do not tie remuneration of asset managers to performance or other portfolio outcomes, as we believe that this sets wrong incentives. We pay our asset managers a management fee which is competitive, considering asset class and size of investments.

### **Monitoring turnover cost**

Costs are very important to us, whether direct (such as asset management or brokerage fees) or indirect (such as market impact, bid-

ask spreads, structuring or other). During the selection process for a new manager we compare these cost as well as the average portfolio turnover and will take these factors into consideration in our final decision. We tend not to select asset managers with high turnover and/or high costs.

Furthermore and depending on the mandate we might set restrictions on turnover per year. In portfolios where there is no turnover restriction, Zurich's responsible CIO of the unit will seek the discussion with the portfolio manager if the turnover or cost is greater than expected and will seek to find a solution if the turnover is needlessly high.

### Duration of manager contracts

At Zurich we believe in long term relationships with our asset managers. Managing insurance assets well needs a lot of specific know-how, capabilities and experience which are not prevalent in every firm. We therefore take great care when selecting a new manager and ensure that they will possess all the resources, knowledge, experience, processes and systems in the quality and quantity that we require. Once they are selected, we work with them closely and keep in constant contact in order to minimise mistakes through miscommunication or misunderstandings. As outlined above, we measure and assess each portfolio and each manager on a quarterly basis and will give feedback if and when suitable in order to counter harmful developments. This philosophy and close cooperation has served us well over the last decades and our turnover of asset managers is very low.

## ESG integration for external mandates

Zurich strives to fully reflect the four basic requirements for successful ESG integration (described earlier) in its asset manager life cycle process for all in-scope assets.

### Manager selection

A set of responsible investment questions is integrated into the request for information (RFI) and request for proposal (RFP) questionnaires, and is evaluated with an explicit weighting:<sup>8</sup>

- Please describe your overall philosophy regarding, and approach to, responsible investment, including how you think environmental, social, and governance (ESG) factors impact risk-adjusted performance. Address how long-term views are generally incorporated into the investment process.
- Are you a signatory of the PRI? If not, please explain your decision.
- Please describe how you integrate environmental, social and governance (ESG) factors into your investment process, particularly with respect to security/asset selection and risk management. Using a specific example of an ESG-related risk or opportunity, describe how the process in place has influenced the decision-making. Your answer should also address: 1) Who is primarily responsible for the analysis of ESG factors? 2) What resources (research, analytical tools, etc.) are available to portfolio managers and analysts to assess ESG factors? 3) If you have a dedicated ESG team, a description of how portfolio managers and equity/credit analysts integrate the input of the ESG team in their work; elaborate on the communication flow (meetings, research reports, etc.).

- If available, please provide a copy of your position statement. If a signatory of the PRI, please provide a brief description of how principles two to six are addressed by your organization.
- As part of your risk management or related processes, do you systematically assess the impact of ESG factors on the financial performance and do you capture exposure to any specific ESG-related risk factors as part of your portfolio-level risk analytics? If so, do you prepare regular reports on ESG risk-factor exposures?
- Please describe your proxy voting process and provide your proxy voting policy as attachment. If you do not actively vote all proxies and/or do not incorporate environmental and social issues in your policy, please explain why.
- Do you discuss specific ESG issues as part of systematic direct engagement with investee company management? If yes, please describe the process and provide three examples. If no, please explain why not.
- Please describe any relevant ESG-related training that portfolio managers and equity/credit analysts receive. If you have a dedicated ESG team, please outline the organization of the team and detail the experience and education of the team members. Use the attached Excel sheet.
- If applicable, please indicate your willingness to share the following materials with clients: selected sections from the PRI questionnaire as prepared for annual PRI reporting, as well as the PRI's analysis of relative performance; portfolio-level report(s) on ESG factor exposure.

The manager selection and responsible investment teams work together to determine the appropriate weight on a case-by-case basis and in evaluating the responses.

<sup>8</sup> The questions shown in this section serve as an internal template for Zurich's RFP process with external asset managers. Language is adapted on a case-by-case basis to take into account the individual nature of each investment mandate. The language used here does not represent a recommendation to any third party to use this or similar wording in RFPs.

## Manager appointment

Zurich expects its asset managers to reflect the four basic requirements of ESG integration (see earlier sections) in their investment approach. To formally express these expectations, Zurich includes the following language in investment management agreements (IMA):<sup>9</sup>

### 1. General Principles

- 1.1. In pursuing the investment objectives set forth in the investment guidelines, the manager will have a process for assessing and monitoring current or potential investments in relation to relevant long-term factors such as environmental, social and corporate governance issues (the 'ESG factors') unless otherwise advised by the client. The manager will ensure that its staff receives adequate training, access to relevant data and information, and applies due care and diligence to applying this process, including considering the extent to which the ESG factors generate investment risks or opportunities.
- 1.2. The manager seeks to act in the best economic interests of the client by taking ESG factors (identified as relevant) into account when making investment decisions. All else equal, the Manager will prefer securities which, in the Manager's assessment, show superior environmental, social, and governance practices.
- 1.3. To the extent the manager engages directly with the management of investee companies as part of its regular investment process, the Manager will discuss ESG factors identified as relevant.

## 2. Exercise of proxy voting rights

- 2.1. The investment manager shall exercise any voting or other ownership rights (whether directly or through directions to a custodian and including but not limited to, conversions, subscriptions, exchanges, stock splits, rights, offerings, tender offers and other corporate actions) attached to any equity investments in the Portfolio in accordance with the manager's voting policies (and subject to any voting guidelines agreed with the client) and in the manner in which the manager believes to be in the best interests of the portfolio and the client, as well as with a view to achieving best practice standards of corporate governance and equity stewardship and with the aim of adding value to, and/or preserving value in the portfolio, as well as reducing unrewarded risk exposures.
- 2.2. Should the manager become aware of a conflict of interest or potential conflict of interest, the manager may vote such proxies only in accordance with the conflicts of interest procedures set forth in its written policies. To the extent the client will in the future have a voting policy of its own, the manager and client shall in good faith negotiate revisions to this provision.

- 2.3. The manager shall keep adequate records of its proxy voting on behalf of client and will make available to the client on a regular basis, but at least annually, both summarized as well as detailed information concerning the exercise of the voting rights, including but not limited to voting decisions by holding position and ballot, in electronic format. In addition, the Manager will promptly provide the client with any amendments or modifications to its proxy voting policies.

## 3. Reporting

- 3.1. The Manager shall at least annually make available to the client a written position statement describing the manager's approach to the inclusion of the ESG Factors in its investment decisions and, upon the client's reasonable request, the Manager shall discuss any achievements in implementing those practices.
- 3.2. The manager will discuss, upon the client's reasonable request, exposures to material environmental, social, and governance risk factors, and a watch list of portfolio investments exposed, if applicable, as identified by the manager, to particularly controversial ESG issues, with an explanation of how the manager has sought to identify, monitor and manage such exposures, including any action taken to directly engage with the management of investee companies.

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<sup>9</sup> The language shown in this section serves as an internal template for Zurich's IMAs with external asset managers. Zurich has started to include responsible investment language in selected mandates. Language is adapted on a case-by-case basis to take into account the individual nature of each investment mandate. The language used does not represent a recommendation to any third party to use this or similar wording in IMAs.



## Manager review

Zurich uses the following elements to formally integrate responsible investment practices into the manager monitoring process:

- Use of a detailed questionnaire to capture responsible investment practices applied specifically to Zurich portfolios.
- Discussion of ESG risks and opportunities at a portfolio level as part of formal performance review meetings.
- Discussion of ESG performance as part of Asset-Liability Management Investment Committee (ALMIC) meetings.
- Discussion of responsible investment practices at formal senior-level relationship meetings.
- Integration of responsible investment practices into Zurich's proprietary asset manager evaluation system.

## ESG in the private equity investment process

As part of a strategic allocation to the private equity asset class, Zurich commits up to USD 400 million annually to private equity investments through a mix of primary fund investments, secondary investments, and selected co-investment. With the exception of selected co-investments, Zurich does not provide equity capital directly to privately held companies. A team of dedicated private equity specialists is responsible to manage Zurich's private equity investments and select private equity fund managers. As with security mandates, Zurich strives to fully reflect the four basic requirements for successful ESG integration (see above) in its private equity investment process. Responsible investment practices are

formally reflected in the private equity investment process manual at the following process stages:

- Investment due diligence
- Investment vetting and approval
- Execution and funding
- Risk management and reporting
- Manager selection.

A set of pre-defined questions are used to guide the assessment of responsible investment practices at the fund manager as part of the due diligence:<sup>10</sup>

- How does the general partner (GP) address ESG issues when analyzing investment opportunities?
- How are ESG issues included in the investment decision process?
- Is there a dedicated team focused on ESG issues?
- Does the GP provide ongoing ESG training for the relevant staff?
- Is environmental and social impact measured?
- Monitoring: How are ESG issues monitored at the portfolio company level? Is there a framework in place?
- Has the GP developed an internal ESG policy?
- Is data on ESG issues systematically collected by the GP?
- Provide specific examples on how ESG issues were addressed.
- Reporting to limited partners (LP): Is there a formal ESG reporting process in place? How often are LPs updated? What data are disclosed?
- Is the GP a signatory of the Principles of Responsible Investing (PRI)?
- The PE and responsible investment teams work together to evaluate responsible investment practices and summarize findings for discussion by the investment committee.

Upon investment, Zurich strives to include the following language in side letter agreements with the General Partner:<sup>11</sup>

Responsible Investing Statement of Policy: The general partner acknowledges that it has read the 'Responsible Investing Statement of Policy' of Zurich Insurance Group, AG ('Zurich'), which is attached to this letter as Annex I. Zurich acknowledges that the General Partner's acknowledgement does not impose any obligations on behalf of the general partner.

Annex I – Statement of Policy: The investor's ultimate parent entity, Zurich Insurance Group Ltd ('Zurich'), strives to manage its assets as a responsible investor and believes that responsible investing requires recognizing certain principles associated with environmental, social, and governance ('ESG') issues. Zurich believes that these principles are embodied in the Principles for Responsible Investing ('PRI'), to which Zurich is a signatory. Zurich believes that these initiatives will ultimately benefit our investors through the creation or manufacture of services or products in ways that minimize environmental impact, the promotion of reasonable treatment for all stakeholders, and ensuring appropriate governance. Zurich also believes that embracing ESG matters enhances the reputation of private equity, which will benefit the industry and our investors. Consequently, it is Zurich's policy to apply the PRI to its own investment practices, and Zurich will encourage those with whom it invests to adopt them as well. As a limited partner in private equity funds, Zurich or its affiliates must delegate the responsibility for selection and management of individual investments to the general

<sup>10</sup> The questions shown in this section serve as an internal template for Zurich's private equity due diligence process with private equity fund managers. Language is adapted on a case-by-case basis to take into account the individual nature of each commitment to a private equity fund. The language used here does not represent a recommendation to any third party to use this or similar wording in due diligence questionnaires.

<sup>11</sup> The language shown in this section serves as an internal template for Zurich's side letter with General Partner. Zurich has started to include responsible investment language in selected agreements. Language is adapted on a case-by-case basis to take into account the individual nature of each investment mandate. The language used does not represent a recommendation to any third party to use this or similar wording in IMAs.

partners of the funds. Zurich recognizes that the PRI are voluntary and do not preclude investment nor require divestment; however, it is Zurich's policy to engage its managers on these issues during due diligence and through subsequent monitoring. Zurich will periodically report on its efforts to gauge the effectiveness of its own efforts and those of its managers with the PRI.

**ESG Dialogue:** The General Partner hereby agrees to use commercially reasonable efforts to discuss environmental, social, and governance ('ESG') issues, risks and opportunities identified by the General Partner as material or otherwise deemed relevant

by the General Partner at the level of the Partnership's portfolio companies on a periodic basis upon the request of the Investor.

#### ESG in the Investment Process

The General Partner shall use commercially reasonable efforts to assess relevant risks and opportunities prior to making investments for the Partnership and shall ensure that its investment process, systems and staff support the identification of ESG factors that may be material to any investment or otherwise deemed relevant by the General Partner.

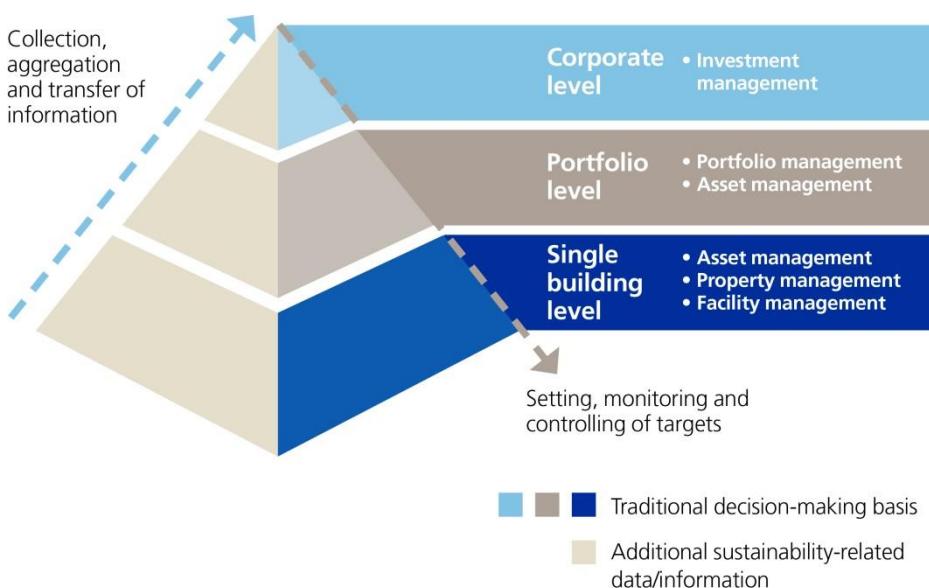
As part of periodic update meetings with fund managers, the PE team reviews any material developments regarding ESG issues.

#### ESG in the real estate investment process

To assure a globally aligned ESG integration approach for real estate investment, the strategy is set, monitored and controlled top-down. Data is collected, aggregated and transferred bottom-up using our global real estate management information system.

As part of the annual review meetings with the property manager, the local asset manager discusses the property manager's approach to include ESG factors in their daily facility and property management decisions.

The local real estate asset manager reports annually to Group Real Estate during the annual strategy review meeting. The basis for this discussion is the ESG scoring of the portfolio which is available in the real estate information system. The local real estate asset manager provides a short overview of the initiatives undertaken and the effects of such efforts on the overall rating of the portfolio and of specific assets.



Extended decision-making basis at all corporate levels (Source: UNEP FI, May 2014, Sustainability Metrics)

The strategy for implementing ESG in real estate is based on three pillars which take into account local best practice and provide a global framework to assess potential acquisitions as well as the existing portfolio.



**1.** ESG risk factors are assessed by the local real estate asset manager using in Zurich's real estate information system. New acquisitions need to achieve an ESG score of at least 3 out of 5. The ESG performance of the existing portfolio is made visible in the 9 box grid where the ESG rating of every property of the portfolio is shown.

**2.** The local real estate asset manager aims to increase the share of labeled properties wherever reasonable and wherever such certificate is expected to improve risk-adjusted long-term financial returns.

**3.** The local real estate asset manager aims to reduce the emission of green-house gas and other consumption resources in close collaboration with the local property and facility manager by setting, monitoring and controlling emission targets and specific initiatives such as waste separation.



# Section VII

## Appendix: Engagement

## Scope

Zurich's investment strategy – incorporating our approach to responsible investing – calls for us to monitor not only the topics traditionally of interest to investors, such as a company's strategy and financial performance, but also environmental, social and governance (ESG) risks and opportunities in our investment holdings as well as apply an active ownership approach. We define active ownership as proxy voting and active engagement with companies in which we invest. Direct engagement with companies we invest in may be used to share general investor feedback with a company in regard to its strategy and both financial and non-financial performance, as well as positively influence decisions related to ESG. Academic research shows that successful engagement with responsive companies can improve corporate governance as well as a company's management of environmental and social issues, and thus lowering downside risks and improving performance.<sup>12</sup> Engagement can also serve to help gather or clarify information. Such information, in turn, informs proxy voting decisions, and helps to integrate ESG factors in valuations. Engaging companies on these topics also allows Zurich to share our philosophy and approach to responsible investment and corporate

governance with them. Significantly, engagement also offers a possibility to share information with the marketplace – not only among companies we invest in, but also with a variety of other market participants, such as organizations providing ESG information, peers, industry networks and regulatory bodies.

Accordingly, at Zurich, engagement is defined as a set of two complementary approaches:

- direct dialogue with investee companies geared toward gathering 'traditional' information regarding strategy and finances and assessing their approaches to ESG issues as well as influencing their behavior in certain instances as part of our ESG integration strategy.
- collaborating with the broader market to achieve desired goals with regard to ESG issues as part of our advancing together strategy.

Zurich believes that direct engagement, done where possible without incurring undue costs, is in our best economic interest and aligned with our desire to safeguard investments. These investments are made with the aim of achieving sustainable financial success and based on prudent, responsible business behavior, including Zurich's Code of Conduct, or equivalent.

Proxy voting is governed under a separate policy and guidelines, which can be found [here](#).

## Objectives

As we implement Zurich's responsible investment approach, we are following a set of specific objectives:

- Engaging on both an individual and collaborative basis with investee companies to on a case-by-case basis either:
  - acquire more information about ESG as well as overall strategy, management and issues of investee companies.
  - encourage improved/increased ESG and/or impact disclosure.
  - exert an influence on investee companies, seeking to improve their overall business practices, including ESG practices and ESG footprint.
- In addition, we engage individually and collaboratively with regulatory bodies and the broader spectrum of financial market participants to:
  - encourage improved/increased ESG and/or impact disclosure.
  - influence and improve broader corporate practice on ESG issues.
  - support the mainstreaming of ESG integration and impact investment.
  - advocate for regulatory frameworks that are supportive to scaling responsible investment with integrity.
  - champion ESG topics identified as material to Zurich.

<sup>12</sup> See: Active Ownership (2012), Dimson, Karakas & Li; Returns to Shareholder Activism: Evidence from a Clinical Study of the Hermes UK Focus Fund (2009), Becht, Franks, Mayer & Rossi; Private ESG Shareholder Engagement and Risk: Clinical Study of the Extractive Industry (2015), Höpner, Oikonomou, Zhou.

## Prioritizing our engagement

We apply both a top-down and bottom-up approach to identify and prioritize engagement topics, allowing investment decision-makers to play an important role in developing our programs. Top-down decisions are based on strategic considerations and driven by Group functions, whereas bottom-up decisions are based on a portfolio level and are driven by investment decision-makers, such as portfolio managers.

### *Top-down:*

- Topics of greatest priority are aligned with Zurich Insurance Group's business strategy, sustainability strategy, responsible investment strategy and existing external commitments (such as the UN Global Compact, The Investor Agenda, and others), or local stewardship codes, to which Zurich voluntarily adheres.

### *Bottom-up:*

- Financially material long-term ESG trends.
- Financially most-material ESG factors in terms of geography/industry sector/company in the portfolio manager's universe.

We aim to efficiently apply these relevant prioritization factors both top-down and bottom-up to companies:

- that breach certain pre-defined norms (external or Zurich-specific).
- which have significant exposure to ESG areas of concern.
- which raise significant concerns in regard to their corporate strategy and financial performance.
- in which Zurich has sizeable holdings.
- whenever a company initiates dialogue as part of the investment process.

On a case-by-case basis, Zurich might also choose to join collaborative engagement platforms. Such decisions are based on the ability of a particular group to maximize the expertise of a knowledgeable organization or a chosen collective platform. This aligns well with Zurich's prioritization approach described here. Where this approach is used, we feel we can add value to the collaborative approach and achieve greater impact collectively.

## Method of engagement

We apply both a top-down and bottom-up approach to conduct our engagement activities using a variety of teams such as:

### *Top-down:*

- Group Responsible Investment Team
- Group Sustainability Team
- Group Public Affairs Team
- Group Sustainability Risk Team
- Investment Management Market Strategy and Macroeconomics Team
- Membership in industry bodies

### *Bottom-up:*

- Investment decision-makers such as portfolio managers, financial analysts, dedicated engagement and stewardship teams

Both internal and external asset managers are required to engage on relevant business and ESG issues in discussions with investee companies, either as part of regular company meetings, or through separate channels.

The following minimum requirements and best practice with regard to engagement have been agreed with in-house asset managers:

## Engagement

### *Minimum standard:*

- Reviewing ESG research before interacting with investee company management (through existing channels such as investor meetings or calls, etc.) and discussion of relevant ESG issues besides other material issues.
- Using the PRI clearinghouse platform for collaborative engagement activities on priority topics.
- Discuss active ownership examples and progress in annual meetings between local teams and Zurich's Group Responsible Investment team.

### *Best practice:*

- Pro-actively establishing and maintaining dialogue with brokers, ESG data providers, industry bodies, investee companies with material ESG issues, and industry or regulatory bodies to support responsible investment matters Zurich has identified.
- Initiating or joining engagements on priority topics with external asset managers or peers.
- Actively taking on and championing topics for engagement through the PRI clearinghouse platform or other suitable channels.

For more information on how Zurich ensures the implementation of its overall responsible investment strategy by external asset managers, please refer to [section VI](#).

## Conflicts of interest

General principles that Zurich adheres to in dealing with potential conflicts of interest are described in the Zurich Code of Conduct and the Group policy governing conflicts of interest and external engagements. All bottom-up engagements, meaning those that are conducted directly by Zurich's investment decision makers, are conducted in line with Group Investment Management's mandate to generate superior risk-adjusted economic returns on the investments for the benefit of policyholders and shareholders. No consideration shall be given to an investee company's potential business relationships with Zurich outside of Group Investment Management. When gathering additional information from investee companies, non-public material information shall not be sought or used in the investment process. Top-down engagements can be conducted by the Group Responsible Investment team in conjunction with other Group Functions as described above. Such engagements may target companies that are Zurich's clients or investees or both, and are subject to Zurich's conflict-of-interest policy.

## Transparency

From a bottom-up perspective, Zurich will prefer private over public engagements, especially when dealing directly with investee companies. Engagements via the PRI clearinghouse platform, or signing investor letters, will by definition be public.

Zurich collects and shares its efforts with regard to engagement and also its successes in such engagements internally, and provides updates from the engagement programs of external asset managers through proprietary questionnaires sent out as part of the annual review process. Engagements can also be discussed in meetings between the Group Responsible Investment team, local responsible investment champions and the portfolio managers where such investments are reviewed. Zurich shares its overall engagement approach as well as selected examples in its annual PRI Transparency Report, which is published on both the PRI and Zurich websites. No full public listing of all engagements is planned due to considerations regarding both the practical ease of reporting, as well as academic literature suggesting that private engagements foster more trust in those companies that investors engage with.

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