

# Appendix C

## Approaches and definitions under SFDR

This Annex sets out the bank's approaches and definitions of some of the key concepts outlined in the Regulation (EU) 2019/2088 of the European Parliament and of the Council of 27 November 2019 on Sustainability-related disclosures in the financial services sector (SFDR): Sustainable Investment, Do No Significant Harm (DNSH), Good Governance Practices and consideration of Principal Adverse Impacts (PAIs).

## 1. Sustainable Investment Framework

SFDR defines "Sustainable Investment" as:

- an investment in an economic activity that contributes to environmental or social objectives;
- provided that such investment does no significant harm to any of the objectives; and
- provided that the investee company follows good governance practices.

As a disclosure regulation, SFDR does not specify (i) which environmental and social objectives must be followed, nor what constitutes (ii) a contribution to an environmental or social objective, (iii) a significant harm or (iv) a good governance practice. Instead, SFDR requires financial market participants to define and disclose their own approach to these concepts.

Pictet Wealth Management's Sustainable Investment Framework builds upon our expertise and convictions in Responsible Investing to define what we consider as "Sustainable Investment" under SFDR across different asset classes. It reflects our current views and interpretation and, as such, may be subject to change at any time.

For corporate investments, we define the concept of "Sustainable Investment" at issuer level, except for use-of-proceeds labelled bonds for which it is defined at instrument level. For third party funds, we adopt the "Sustainable Investment" definition and results provided by the fund manager.

### (I) ENVIRONMENTAL AND SOCIAL OBJECTIVES

We measure contribution of economic activities against the following environmental (E) and social (S) objectives:

1. Decarbonisation (E): Reducing anthropogenic greenhouse gas emissions in line with the objectives of the Paris Agreement;  
*Examples of activities: renewable energy production and equipment, energy storage, low-carbon transportation*
2. Efficiency & Circularity (E): Increasing materials and energy efficiency, extending products lifecycle and reducing waste and pollution;  
*Examples of activities: industry 4.0 technologies, materials and energy efficiency software and technologies, environmental consulting, recyclable or renewable materials, waste treatment services, recycling*
3. Natural Capital Management (E): Ensuring the sustainable use, management and preservation of natural resources, habitats and ecosystems;  
*Examples of activities: sustainable forestry, sustainable or organic agriculture, aquaculture, precision agriculture technology, vertical farming, harvesting and irrigation technologies, livestock health*
4. Healthy Life (S): Promoting health through physical and mental well-being and healthier diets, increasing food safety and reducing food loss and waste;  
*Examples of activities: pharma, biotech, medical devices, telemedicine, care providers, fitness, healthy food products and ingredients, food storage and preservation, grocery and food delivery, professional kitchen equipment*

5. Water, Sanitation & Housing (S): Ensure safe and sustainably managed drinking water, affordable and efficient housing and sustainable urbanization;

*Examples of activities: water supply, treatment and distribution, water technologies, smart building technologies, sustainable building materials, efficient home appliances, homebuilders, property management*

6. Education & Economic Empowerment (S): Promoting life-long learning, education and employment, and improving access to convenient and affordable financial products and services;

*Examples of activities: educational services, edtech, professional training, student accommodation, recruitment assistance, workforce management, digital payments, money transfer, support services and technologies for SMEs*

7. Security & Connectivity (S): Ensuring the security of individuals, businesses and governments in both the physical and digital world, and developing networks and technologies to increase connectivity and access to digital services.

*Examples of activities: work and road safety, access control, IT security, critical data infrastructures, certification and inspection services, network equipment and software, telecom infrastructure, mobile devices*

## (II) CONTRIBUTION TO AN ENVIRONMENTAL OR SOCIAL OBJECTIVE

An investment must meet at least one of the following criteria to be considered as contributing to environmental or social objectives.

**Equities and corporate general bonds:** The issuer has at least 20% combined exposure (as measured by revenue, EBIT, enterprise value or similar metrics) to economic activities that contribute to environmental or social objectives. Exposure is determined through fundamental analysis, through reported revenue alignment with the EU Taxonomy, or through a proprietary rule-based model using third-party revenue classification data to identify revenues derived from relevant economic activities. An issuer exposed to multiple economic activities contributing to several environmental or social objectives is associated with the predominant economic activity and its corresponding environmental or social objective.

**Corporate and sovereign labelled bonds:** The instrument is a Green, Social or Sustainability use-of-proceeds bond. An instrument financing multiple economic activities contributing to several environmental or social objectives is associated with the predominant economic activity and its corresponding environmental or social objective.

## (III) DO NO SIGNIFICANT HARM (DNSH)

We have defined DNSH Thresholds for companies' and countries' behaviour towards international norms and involvement in products and services that have high adverse impacts on society and the environment, and we consider issuers at or above these thresholds as doing significant harm to environmental or social objectives.

**Corporate issuers:** For an investment in a corporate issuer's equity, general bonds or labelled bonds to be considered as doing no significant harm to environmental or social objectives, the corporate issuer must:

- i Remain strictly below all the DNSH Thresholds defined in the following table<sup>16</sup>;
- ii Have the sum of its revenues from products and services with a DNSH Threshold remain strictly below 20%; and

<sup>16</sup> An explanation of how our DNSH methodology takes into account the adverse impacts in Table 1 of Annex 1 of SFDR can be found in section 3) of this annex.

- iii Be aligned with the OECD Guidelines for Multinational Enterprises and the UN Guiding Principles on Business and Human Rights.

CRITERIA	DNSH THRESHOLDS <sup>17</sup>
<b>Energy</b>	
Thermal Coal Extraction	10%
Thermal Coal Power Generation	10%
Oil & Gas Production	10%
Oil Sands Extraction	10%
Shale Energy Extraction	10%
Off-shore Arctic Oil & Gas Exploration	10%
<b>Weapons</b>	
Production of Controversial Weapons <sup>18</sup>	Excluded
Military Contracting Weapons	10%
Military Contracting Weapon-Related Products and/or Services	10%
Small Arms Civilian Customers (Assault Weapons)	10%
Small Arms Civilian Customers (Non-Assault Weapons)	10%
Small Arms Military/Law Enforcement Customers	10%
Small Arms Key Components	10%
<b>Addictive products</b>	
Adult Entertainment Production	10%
Gambling Operations	10%
Gambling Specialized Equipment	10%
Tobacco Products Production	10%
Alcoholic Beverages Production	10%
<b>Agriculture</b>	
Genetically Modified Plants and Seeds Development	10%
Genetically Modified Plants and Seeds Growth	10%
Pesticides Production	10%
Pesticides Retail	10%
Palm Oil Production and Distribution	10%
<b>International Norms</b>	
Breach of or high or severe controversy related to UN Global Compact Principles or OECD Guidelines for Multinational Enterprises	Excluded

<sup>17</sup> Where relevant, thresholds are set as a proportion (%) of issuers' revenues.

<sup>18</sup> Controversial weapons include anti-personnel mines, cluster munitions, biological & chemical weapons (including white phosphorous) and nuclear weapons

**Sovereign issuers:** For an investment in a sovereign issuer's labelled bond to be considered as doing no significant harm to environmental or social objectives, the sovereign issuer must meet the conditions laid out in the following table:

CRITERIA	DNSH THRESHOLD
Countries (i) listed as State Sponsors of Terrorism as defined by the Office of Foreign Assets Control <sup>19</sup> or (ii) subject to EU financial sanctions targeting central banks and/or State-Owned enterprises (SOEs)	Excluded
Countries (i) listed under "high alert" or "very high alert" in the Fragile State Index or (ii) affected by violent conflict as defined by the World Bank	Excluded
Countries (i) listed under "alert" on the Fragile State Index or (ii) subject to export related sanctions by the EU	Excluded
Countries subject to social violations as referred to in international treaties and conventions, United Nations principles and, where applicable, national law	Excluded

#### (IV) GOOD GOVERNANCE PRACTICES

The issuer of a corporate investment must meet the criteria defined in section 2. Good Governance Practices of this annex to be considered as following good governance practices.

<sup>19</sup> "State Sponsors of Terrorism" is a designation applied by the United States Department of State to countries that repeatedly provided support to acts of international terrorism.

## 2. Good Governance Practices

The Good Governance Practices criteria apply to issuers of all corporate investments of SFDR Article 8 and Article 9 products. To determine whether a company meets minimum requirements for good governance practices under SFDR, Pictet Wealth Management ensures that companies it invests in do not have severe controversies or breaches to UN Global Compact Principles that are linked to topics including sound management, employee relations, remuneration of staff and tax compliance. How breaches to UNGC Principles and severe controversies map to good governance practices is set out in the table below.

	Severe Controversies										Breaches to UNGC Principles			
	Operations Incidents	Env Supply Chain Incidents	Prod. & Service Incidents	Business Ethics Incidents	Governance Incidents	Public Policy Incidents	Employee Incidents	Social Supply Chain Incidents	Customer Incidents	Society & Community Incidents	Human Rights	Labour	Environment	Anti-Corruption
Sound Management Structures				* Bribery and corruption * Business ethics	* Corporate governance	* Lobbying and public policy			* Anti-Competitive Practices * Data Privacy and Security		* Principle 1: support and respect the protection of internationally proclaimed human rights; and * Principle 2: ensure no complicity in human rights abuses			" Principle 10: work against corruption in all its forms including extortion and bribery
Employee Relations							* Employees – Human rights * Labour relations * Occupational Health & Safety	* Employees – Human rights (Supply chain)				* Principle 3: Uphold the freedom of association and the effective recognition of the right to collective bargaining * Principle 4: Eliminate all forms of forced and compulsory labour * Principle 5: Abolish child labour * Principle 6: Eliminate discrimination in respect of employment and occupation		
Remuneration of Staff					* Corporate governance		* Labour relations							
Tax Compliance				* Accounting and taxation										

### 3. Consideration of Principal Adverse Impacts

Principal Adverse Impacts (PAI) refer to those impacts of investment decisions that significantly harm environment or society. Specific indicators have been defined by the European Union to measure, consider and avoid those adverse impacts.

At Pictet Group level, we aim to reduce the most significant negative impacts of our investments and have a group wide exclusion policy in place with regards to controversial weapons, thermal coal and oil & gas activities<sup>20</sup> that is applicable to actively managed funds, certificates, discretionary mandates, investment recommendations and proprietary investments for all entities of the Group.

Furthermore, we address principal adverse impacts on the environment and society through active ownership activities, including voting and engagement.

With regards to our discretionary portfolio management activities, we do actively consider PAIs in our SFDR Article 8 responsible investing solutions:

- When investing directly in securities (equity and fixed income) we use a combination of approaches to consider and, where possible, mitigate material adverse impacts of our investments on society and the environment. The degree and the way these impacts are considered depend on factors such as the investment strategy, the specific context of the investment that is causing the adverse impact, or the availability of reliable data. As a starting point, we identify and mitigate principal adverse impacts through the application of our exclusion framework.
- When investing in funds, we do consider PAI by ensuring that the majority of funds selected meets SFDR Article 8 or 9 requirements and do themselves consider PAI. Such information about whether or not a fund considers PAI is collected directly from the fund managers (through the European ESG template (EET), which is the industry standard used by fund managers to exchange information electronically about the ESG characteristics of their funds). This complements the comprehensive ESG due diligence we apply to assess fund managers.

For corporate issuers, PAIs are considered through our exclusion framework (appendix B), sustainable investment DNSH principle (appendix C) and, where relevant, entity-level initiatives.

For sovereign issuers, PAIs are considered through exclusions, DNSH Thresholds and Sustainable Investments eligibility criteria.

How exclusions, sustainable investment DNSH principle, entity-level initiatives and Sustainable Investments eligibility criteria map to PAIs and their related indicators is set out in the tables below.

<sup>20</sup> For oil & gas activities, group exclusion applies to investments that involve Pictet Group balance sheet.

CORPORATE ISSUERS			Exclusions (as per appendix B)														How Pictet Group-Level initiatives contribute (Engagement and voting activities conducted at product level where relevant)								
			Do No Significant Harm' (part of sustainable investment framework in appendix C)																						
			Thermal Coal Extraction	Thermal Coal Power Generation	Oil & Gas Production	Oils Sands & Shale Energy	Off-shore Arctic Oil & Gas Exploration	Production of Controversial Weapons	Military Contracting Weapons	Military Contracting Weapon-Related Products & Services	Small Arms	Adult Entertainment Production	Gambling Operations	Tobacco Products Production	High or Severe Controversies	Breach of UNGC Principles or OECD Guidelines		Gambling Specialized Equipment	Alcoholic Beverages Production	Genetically Modified Plants and Seeds	Pesticides Production and Retail	Palm Oil Production & Distribution			
Topic	Indicators																				Climate Action Plan & Group Engagement Focus (Climate)	Group Engagement Focus (Water)	Group Engagement Focus (Nutrition)	Group Engagement Focus (Long-termism)	Group Engagement Focus (Breaches of Global Norms)
Greenhouse Gas Emissions	PAI 1	GHG Emissions	✓	✓	✓	✓	✓														✓				
	PAI 2	Carbon footprint	✓	✓	✓	✓	✓														✓				
	PAI 3	GHG intensity of investee companies	✓	✓	✓	✓	✓														✓				
	PAI 4	Exposure of companies to fossil fuels	✓	✓	✓	✓	✓														✓				
	PAI 5	Share of non-renewable energy consumption and production	✓	✓	✓	✓	✓														✓				
	PAI 6	Energy consumption intensity per high impact climate sector	✓	✓		✓	✓														✓				
	PAI 4 (additional)	Investments in companies without carbon emission reduction initiatives																			✓				
Biodiversity	PAI 7	Activities negatively affecting biodiversity-sensitive areas	✓		✓	✓	✓							✓				✓	✓	✓			✓		✓
Water	PAI 8	Emissions to water				✓								✓					✓			✓			✓
Waste	PAI 9	Hazardous waste and radioactive waste ratio				✓								✓											✓
Social and Employee matters	PAI 10	Violations of UNGC principles												✓	✓										✓
	PAI 11	Lack of processes and compliance mechanisms to monitor compliance with UN Global Compact principles and OECD												✓	✓										✓
	PAI 12	Unadjusted gender pay gap*																					*		
	PAI 13	Board gender diversity																					✓		
	PAI 14	Exposure to controversial weapons (anti-personnel mines, cluster munitions, chemical weapons and biological weapons)						✓																	
	PAI 15 (additional)	Lack of anti-corruption and anti-bribery policies												✓	✓										
	Other	Exposure to conventional weapons							✓	✓	✓														
	Other	Exposure to addictive products										✓	✓	✓			✓	✓							

\*We do not systematically take into account PAI 12 due to the very low data availability. We do however use it as an engagement point when speaking with Board or management at investee companies as appropriate.



SOVEREIGN ISSUERS		Exclusions (as per appendix B)		Portfolio construction / Universe definition if relevant for the strategy			
		DNSH Thresholds					
		State Sponsors of Terrorism by OFAC or under EU financial sanctions	“High alert” or “very high alert” in the Fragile State Index or affected by violent conflict			“Alert” in the Fragile State Index or under EU export- related sanctions	PAI 16 - Countries subject to social violations
Topic	Indicators						
Environmental	PAI 15 - GHG intensity				✓		
Social	PAI 16 - Countries subject to social violations	✓	✓	✓	✓		