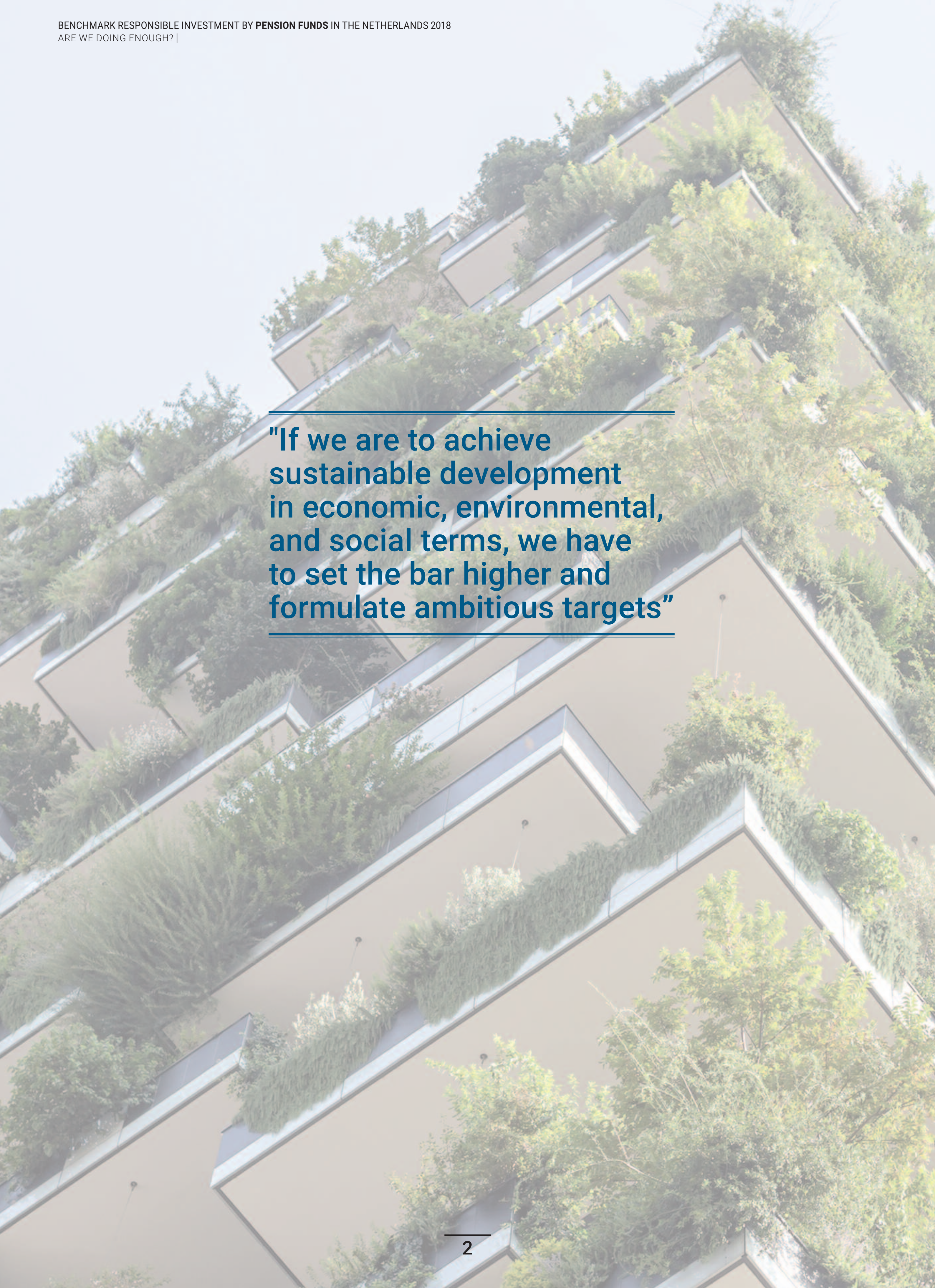
VBDO

Benchmark Responsible Investment by Pension Funds in the Netherlands 2018

Are we doing enough?



"If we are to achieve sustainable development in economic, environmental, and social terms, we have to set the bar higher and formulate ambitious targets"

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Are we doing enough?

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to thank the participating pension funds
and their asset managers for their valuable contributions.

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Dutch Association of Investors for Sustainable Development
Vereniging van Beleggers voor Duurzame Ontwikkeling (VBDO)

Star ranking

★★★★★

ABP

Bedrijfstak-pensioenfonds voor de Bouwnijverheid (Bpf Bouw)

BPL Pensioen

PFZW

★★★★

Pensioenfonds Metaal en Techniek (PMT)

Pensioenfonds van de Metal-ektro (PME)

Pensioensfonds voor Woning-corporaties (SPW)

★★★

Ahold Delhaize Pensioen

Bpf Schilders

Pensioenfonds KPN

Pensioenfonds PNO Media

Pensioenfonds PostNL

Pensioenfonds Progress (Unilever)

Pensioenfonds SNS Reaal

Pensioenfonds Werk en (re)Integratie (PWRI)

SBZ Pensioen

Stichting Pensioenfonds Openbaar Vervoer (SPOV)

Spoorweg-pensioenfonds

★★

Bedrijfspensioen-fonds voor de Koopvaardij

Bedrijfstak-pensioenfonds voor het Levens-middelenbedrijf

Bpf Schoonmaak

Heineken Pensioenfonds

Pensioenfonds Achmea

Pensioenfonds APF (AkzoNobel)

Pensioenfonds Detailhandel

Pensioenfonds DSM Nederland

Pensioenfonds PGB

Pensioenfonds TNO

Pensioenfonds Vervoer

Pensioenfonds voor Huisartsen

Pensioenfonds Wonen

Philips Pensioen-fonds

Rabobank Pensioenfonds

★

ABN AMRO Pensioenfonds

Pensioenfonds Hoogovens

Pensioenfonds Horeca en Catering

Pensioenfonds IBM Nederland

Pensioenfonds ING

Pensioenfonds Medewerkers Apotheken (PMA)

Pensioenfonds UWV

Stichting Pensioenfonds Medisch Specialisten (SPMS)

Shell Pensioen-fonds

Stichting Pensioenfonds voor de Architecten-bureaus

Stichting Pensioenfonds voor Fysio-therapeuten (SPF)

☆

Algemeen pensioenfonds KLM

Bakkers Pensioenfonds

Bpf MITT

Pensioenfonds KLM Cabine-personeel

Pensioenfonds Meubel

Pensioenfonds Vliegend Personeel KLM

Figure 1. Ranking 50 largest Dutch pension funds (per star, alphabetically sorted).

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Preface

VBDO's twelfth benchmark study once again offers valuable insight into the status of sustainable investment in the Dutch pension sector. DNB welcomes the developments in sustainable investment, and sees it as an opportunity to increase the involvement of pension fund participants and to strengthen the support for the whole pension system. DNB therefore considers it important for Dutch pension funds to maintain the positive trend of recent years, and to further develop their sustainability policy. Making decisions that also take environmental, social and governance factors into account is part of robust risk management, and helps us capitalise on opportunities for a more sustainable economy. This will not happen by itself, and calls for all stakeholders to take concerted steps to further develop sustainable investment. This will keep momentum going, and will foster efforts to build a sustainable financial system.

Else Bos
Executive Director of Supervision
De Nederlandsche Bank

At DNB, as part of our remit to maintain financial stability, we are also working towards achieving a sustainable financial sector. On the international front, we have joined forces with other central banks and supervisory authorities in the Network for Greening the Financial System. Our efforts are directed towards strengthening risk management of climate risks, and we widely share the results of our studies in this area. On the European front, we have seen the publication of the Action Plan on Sustainable Finance, which sets out steps to establish a unified classification system and to promote transparency. Closer to home, through the Sustainable Finance Platform, we work with the sector on initiatives to further develop sustainable investment, such as establishing a methodology to measure the impact of investments in terms of the UN Sustainable Development Goals. As of 2019 we will also be the first central bank in the world to commit to the Principles for Responsible Investment (PRI) for the investments of our own funds and reserves.

In our supervisory capacity, we engage with pension funds about their sustainable investment policy and focus on the challenges of implementing such a policy. The overall impression that emerges from this research is that there is no one standard approach that is suited to all pension funds. In implementing sustainable investment policy, it is important for pension funds to ensure there is clear support for policy, that they make choices for suitably applying this policy, and that they select an asset manager that is aligned with this approach. Greater cooperation in the sector can also make knowledge and experience more widely available, which is vital, particularly for the smaller pension funds. Above all, it is important that pension funds continue to take steps forward. This is because shaping and implementing a sustainable investment policy happens step-by-step. Efforts made not only result in progress for the pension fund's own organisation, but for the market as a whole. This VBDO benchmark study is helpful in this respect because it presents a transparent picture of the sector's status, identifying where there is room for improvement and which ambitions can be defined. In this manner, the benchmark contributes to the dialogue about sustainable investment, and that is the basis for progress.

Else Bos, Executive Director of Supervision
De Nederlandsche Bank

Executive summary

This report, published by the Dutch Association of Investors for Sustainable Development (VBDO), provides a detailed overview of the current status quo and trends relating to the responsible investment practices of the 50 largest Dutch pension funds. The pension funds are assessed based on how they govern, formulate, implement and report on their responsible investment policy. The report covers a one-year period, the calendar year 2017. The assessment resulted in a zero to five star rating and into a ranking in order of performance.

There has been little change in the responsible investment practices of the 50 largest Dutch pension funds compared to 2016. The average total score increased by a mere 0.1, showing a deceleration of the improvements that have been achieved in previous years. The top 10 performing pension funds have all improved their total scores, and for the first time four pension funds achieved a five star rating based on their improvements in the implementation category. Besides some of the major players, which have more capacity and resources to expand and improve their responsible investment policies, there are also smaller funds in the vanguard.

Several steps could be taken to further integrate responsible investment in the overall strategy of the pension fund. From formulating a clear long-term strategy and vision, to selecting an asset manager which is aligned with the pension fund's own principles and beliefs. To harness the potential of responsible investing, pension funds can choose from several investment solutions that are being developed. Only a few pension funds explore, for example, possibilities to integrate ESG information and sustainability themes in their strategic asset allocation or ALM-modelling. As sustainability issues are becoming more mainstream in the investment process, a great deal of new information needs to be retrieved and processed. It is very challenging for a single pension fund to keep up with all these new insights, methods and metrics. Collaborating with other pension funds or experts can make the process much easier.

Partnerships and dialogue with peers and wider society could be used to jointly address developments and topics such as climate change, human rights and other themes, also related to the Sustainable Development Goals. This approach also helps pension funds to stay better aligned with the priorities of beneficiaries and stakeholders. To ensure transparency, pension funds should explain their responsible investment policy and monitor and report on progress in a clear and consistent way. This gives stakeholders an understanding of which topics have been focused on, what steps have been taken, and what (environmental and societal) impact the investments have had.

Methodology

The research and scoring methodologies are based on an iterative process, which has developed and improved over the twelve years that VBDO has been running the benchmark 'Responsible Investment by Pension Funds'. Every year, a review is undertaken on the relevancy of the assessed criteria and necessary additions are discussed with participants of the benchmark. More detailed information about the methodology, categories and scores can be found in the appendices.

Outline of the report

The report is structured as follows: the following chapter discusses the introduction, the overall results and details how the funds have scored on the different categories; chapter three states the most important conclusions of this research; and, finally, chapter four contains VBDO's recommendations for how pension funds can further improve.

Introduction

As our economies, societies and environment are intertwined, all depend on each other for stability and sustainability. In recent years, pension funds have begun to take a more holistic view to global wellbeing in their investment policies. On top of "doing less harm" they also aim to "do good" for society by providing capital to companies with favourable Environmental, Social, and Governance (ESG) features, without compromising risk-adjusted returns. Meanwhile, we are now seeing funds taking advantage of the opportunities available to them, in order to generate long-term benefits while fulfilling their fiduciary duty.

Angélique Laskewitz
Executive Director VBDO

This benchmark shows that the overall performance of Dutch pension funds regarding responsible investment has gradually increased over the past twelve years. For the first time, four pension funds achieved a five star rating based on their improvements in the implementation category.

I specifically encourage pension funds in the zero to two star ranking to further implement their responsible investment policy. If they manage to do so, this will substantially improve sector-wide sustainability performance. Such improvement is more and more enhanced by international, European and sector-wide initiatives.

A gradual increase also shows that embedding sustainable investment practices into investment processes is a long-term endeavour. The majority of the pension funds in scope use at least some of the responsible investment instruments available to them. However, societal developments and stakeholders, urge financial institutions to do more to ensure the future quality of life of pension funds' participants and our society as a whole. If we are to achieve sustainable development in economic, environmental, and social terms, we have to set the bar higher and formulate ambitious targets.

Several pension funds struggle to adapt or find solutions themselves. From defining an approach for an investment strategy, an ongoing dialogue with participants and society, partnerships with peers, through profound portfolio construction and risk modelling, and reporting outcomes to stakeholders, will all be crucial to help more pension funds to exploit the potential and necessity of responsible investing. In order to support pension funds to further develop their sustainability strategies, this study provides a detailed overview of pension funds' performance, and also touches upon specifics relating to responsible investment instruments. We hope to create a dialogue between pension funds, asset managers and financial regulators to develop further understanding an broader long-term responsible investing issues.

I would like to thank our sponsor FNV and hereby also take the opportunity to thank the participating pension funds and their asset managers for their valuable contributions.

Angélique Laskewitz
Executive Director VBDO

1. Overall performance

This chapter presents the overall results of this study and the scores per category. First of all, attention is given to the scores that were achieved this year. The overall performance is detailed, along with any notable changes in the star rankings compared to last year. For a more detailed quantitative ranking, please see appendix I. The second part of this chapter focuses on the results of the different categories – governance, policy, implementation and accountability. In addition, the chapter provides recommendations and practical examples to assist pension funds with improving their responsible investment practices. More information on the methodology can be found in the appendices.

Overall responsible investment performance of Dutch pension funds slightly improved

The total average score of 3.0 is similar to last year, with just a small increase of 0.1. The pension funds in the top quintile have all scored better than last year, and some individual notable improvements have been seen in the midfield.

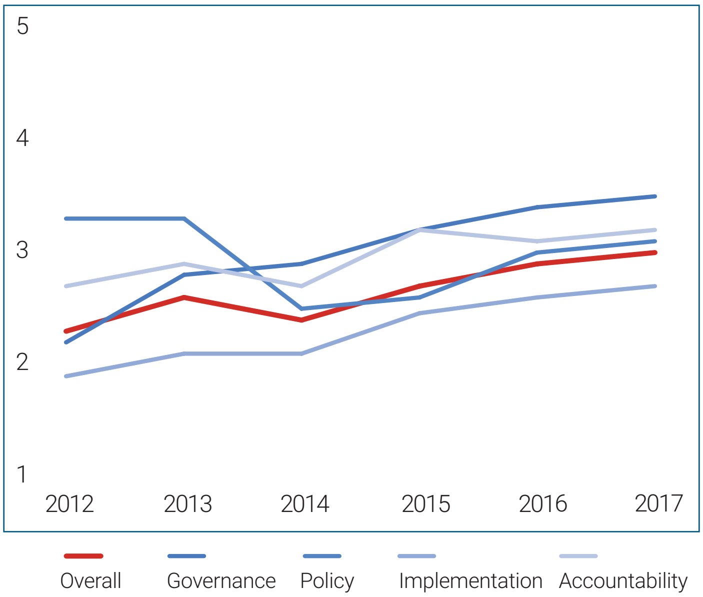

Figure 1.1 Average scores of the benchmarks in responsible investment by pension funds since 2012.

Some individual pension funds have risen sharply in their ranking, putting more pressure on the ones remaining in the lower categories. Other funds have seen a notable decrease in their ranking. Competition between the pension funds is increasing as more pension funds are paving their way to the top. Overall, it can be concluded that Dutch pension funds improved and further substantiated their responsible investment practices in 2017. This can be seen in figure 1.1, which demonstrates the average results per category since 2012. Similar to the overall average score, the scores of the governance, policy, implementation and accountability categories have increased by 0.1 since 2016. The figure shows that implementation results have improved by a similar amount as other categories, but is not improving quickly enough. The implementation category is valued highly by VBDO, because the implementation activities show the actual steps that have been taken, and it therefore has the most impact of any category. Developments in the governance, policy, implementation and accountability categories will be further elaborated on in the 'Results per category' section.

Star ranking

★★★★★	★★★★	★★★	★★	★	☆
ABP	Pensioenfonds Metaal en Techniek (PMT)	Ahold Delhaize Pensioen	Bedrijfspensioenfonds voor de Koopvaardij	ABN AMRO Pensioenfonds	Algemeen pensioenfonds KLM
Bedrijfstakpensioenfonds voor de Bouwnijverheid (Bpf Bouw)	Pensioenfonds van de Metalektro (PME)	Bpf Schilders	Bedrijfstakpensioenfonds voor het Levensmiddelenbedrijf	Pensioenfonds Hoogovens	Bakkers Pensioenfonds
BPL Pensioen	Pensioensfonds voor Woningcorporaties (SPW)	Pensioenfonds KPN	Bpf Schoonmaak	Pensioenfonds Horeca en Catering	Bpf MITT
PFZW		Pensioenfonds PNO Media	Heineken Pensioenfonds	Pensioenfonds IBM Nederland	Pensioenfonds KLM Cabinepersoneel
		Pensioenfonds PostNL	Pensioenfonds Achmea	Pensioenfonds ING	Pensioenfonds Meubel
		Pensioenfonds Progress (Unilever)	Pensioenfonds APF (AkzoNobel)	Pensioenfonds Medewerkers Apotheken (PMA)	Pensioenfonds Vliegend Personeel KLM
		Pensioenfonds SNS Reaal	Pensioenfonds Detailhandel	Pensioenfonds UWV	
		Pensioenfonds Werk en (re)Integratie (PWRI)	Pensioenfonds DSM Nederland	Stichting Pensioenfonds Medisch Specialisten (SPMS)	
		SBZ Pensioen	Pensioenfonds PGB	Shell Pensioenfonds	
		Stichting Pensioenfonds Openbaar Vervoer (SPOV)	Pensioenfonds TNO	Stichting Pensioenfonds voor de Architectenbureaus	
		Spoorwegpensioenfonds	Pensioenfonds Vervoer	Stichting Pensioenfonds voor Fysiotherapeuten (SPF)	
			Pensioenfonds voor Huisartsen		
			Pensioenfonds Wonen		
			Philips Pensioenfonds		
			Rabobank Pensioenfonds		

Figure 1.2 Overall results for responsible investment by Dutch pension funds in 2017 (per star alphabetically sorted).

Performance per star rating

★★★★★

This year for the first time, five stars have been awarded. Algemeen Burgerlijk Pensioenfonds (ABP), Pensioenfonds Zorg en Welzijn (PFZW), Bedrijfstakpensioenfonds voor de Bouwnijverheid (Bpf Bouw) and BPL Pensioen have all been able to exceed the fourstar mark. A score of at least 4.5 in all categories is required to achieve five stars. The funds mentioned have been promoted because their implementation score has increased to above 4.5. On page 12, "New five star performers" gives a brief overview of the differences in scores between the best performing pension funds. This year, ABP slightly outscored PFZW.

★★★★

This ranking contains all the funds that have a score of at least 4.0, but did not score above 4.5 in all categories. The average score in this ranking is 4.3. The four star pension funds, on average, score best in the governance category, while last year the accountability category came out on top. New to achieve a four star rating, are Pensioenfonds van de Metalektro (PME) and Pensioenfonds Metaal en Techniek (PMT). PME has increased its score from 3.8 to 4.3, mainly due to improvements in implementation. PMT has increased its score from 3.6 to 4.1, thanks to improvements in its responsible investment policy. Pensioensfonds voor Woningcorporaties (SPW) remained in this category and improved its total score from 4.1 to 4.4.

★★★

In last year's benchmark, 13 pension funds were given three stars. This year there are only 11. The average total score in this category remains at 3.7, while the average result for governance and accountability has decreased. Bedrijfstak-pensioenfonds voor de Media (PNO Media) and Bedrijfstakpensioenfonds Schilders have both increased their overall place in the ranking with nine places compared to last year to a total score of 3.9.

Pensioenfonds KPN and Pensioenfonds PostNL have increased their score to 3.5, which puts them just above the threshold for three stars. Heineken Pensioenfonds dropped down to two stars, while Pensioenfonds Architectenbureaus dropped to one star.

★★

15 Pension funds have scored two stars, all of which have a total score between 2.5 and 3.5. The average score in this section is 2.9. It is notable that the average results in the governance category (3.5) are significantly better than for policy (3.0), implementation (2.6) and accountability (3.1). The policy performance has decreased from last year's average of 3.2.

The two pension funds with the largest overall improvement compared to last year are both in this section for the first time: Pensioenfonds PGB has increased to 2.9 and gained 14 places, and Pensioenfonds Detailhandel has increased to 3.0 and gained 15 places. Also new in the two star section is Pensioenfonds TNO, which has gained six places and improved its score to 2.6. Stichting Pensioenfonds Medisch Specialisten, Stichting Pensioenfonds voor Fysiotherapeuten, and Pensioenfonds Horeca en Catering have all dropped to a one star rating.

★

The pension funds in the one star section all have a total score higher than 1.5, with an average score of 2.3. This year, 11 pension funds have scored one star. Similar to the two star rating, the governance category outscores the others. The average score for governance in this section is 3.1, while for implementation the average is 2.0. It is clear where room for improvement lies.

Pensioenfonds Horeca en Catering has achieved an overall score of 2.9, with an increase of six positions in the quantitative ranking. However, their 4.0 score in policy is offset by a 1.9 in accountability. Likewise, Pensioenfonds Architectenbureaus has achieved a total score of 2.8, but the score of 1.7 for governance and 1.9 for accountability fail to meet the minimum 2.0 required for each category that a fund needs to progress to a two star rating. The earlier mentioned SPMS was one of the pension funds that showed a large decline in their overall performance and dropped 13 places to 36th. New to achieve one star are Pensioenfonds Hoogovens, with an improvement in its total score of 0.7 and Pensioenfonds Medewerkers Apotheken, with an improvement of 0.5.

☆

The pension funds who did not obtain a star all have a total score of less than 1.5. These pension funds have not yet been able to implement a comprehensive responsible investment policy. This category includes the three non-respondents but also includes pension funds that have indicated improvements are expected.

New five star performers

This is the first time pension funds have achieved a five star ranking. Also, for the first time in the 12-year history of the benchmark “Responsible investment by pension funds in the Netherlands”, ABP has surpassed PFZW. With a total score of 4.8 compared to 4.7, the differences are marginal. Both have shown improvements in the implementation category: ABP improved from 4.5 to 4.8 and PFZW from 4.2 to 4.5. Both pension funds have further substantiated their responsible investment practices in the following ways: they have increased their green bond portfolios, jointly published the “Sustainable Development Investment Taxonomy”[1] and set targets aligned to the Sustainable Development Goals. What stood out in the responsible investment practices of ABP was its inclusion policy, which it started in 2017 by assessing the first 600 companies of its portfolio and classifying them as leaders or laggards. Bpf Bouw and BPL Pensioen have also been able to exceed the four star mark. Bpf Bouw has been able to achieve an increase in every category and BPL Pensioen has also managed a sufficient increase in the implementation score to comply with the minimum standards for five stars.

Size does not always matter

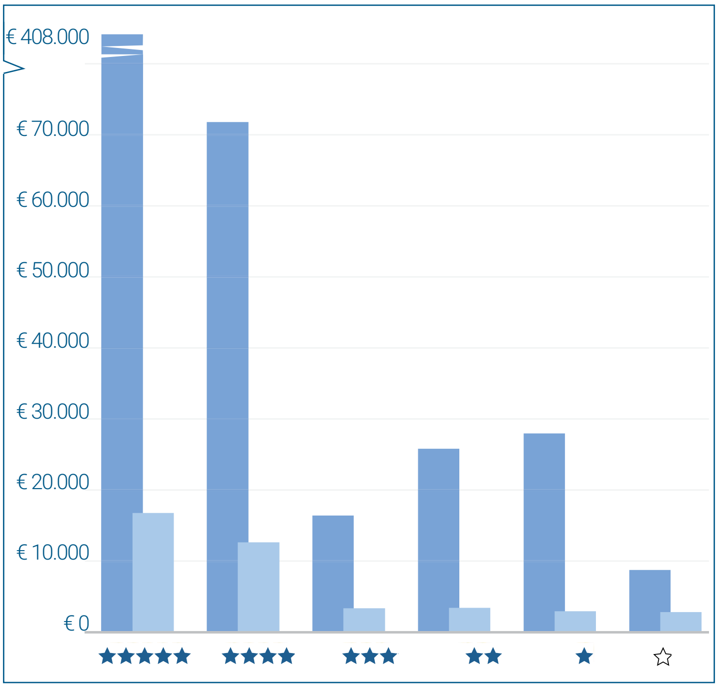

Figure 1.3 Largest and smallest pension funds (in terms of AuM) in the five to zero star categories (x 1 million euro).

[1] APG and PGGM (May 2017), Sustainable Development Investments (SDIs) Taxonomies, https://www.apg.nl/-en/publication/SDI%20Taxonomies/918.

Figure 1.3 shows the difference in size, in terms of assets under management (AuM), between the different star ratings. It shows the biggest and smallest pension fund per section. The largest two pension funds (who are also the best performers) have almost as much AuM as the other 48 combined (€606 billion compared to €620 billion). As well as some of the biggest pension funds (in terms of AuM), which have more capacity and resources to expand and improve their responsible investment policies, a select number of smaller pension funds (in terms of AuM) have also achieved a three, four or even five star rating.

For example, BPL Pensioen (€16.8 billion) achieved five stars, putting it alongside the two biggest pension funds, ABP (€408.8 billion) and PFZW (€197.2 billion). Another example is Pensioenfonds SNS Reaal (€3.4 billion), which is the 46th pension fund in terms of AuM and achieved three stars, clearly outperforming Pensioenfonds Shell (€28.0 billion and 6th in terms of AuM), which lags behind with one star. Clearly, size does not always determine how well a pension fund performs on responsible investment.

Most improved

Looking at the quantitative ranking (appendix I), Pensioenfonds Detailhandel has gained 15 places compared to last year and Pensioenfonds PGB has gained 14 places. Pensioenfonds Detailhandel, in particular, has shown significant progress in the categories governance (+1.5), policy (+1.1) and accountability (+1.1). This shows promising signs for the coming years as other pension funds state that they are working on improving their responsible investment for their entire portfolio.

2. Results per category

To provide better insight into the underlying factors that determine the overall results, each researched category is analysed separately in the following sections.

2.1 Governance

In this benchmark, governance refers to the role and responsibility of the board and senior management regarding an organisation's responsible investment policy. Good governance is crucial if the policy is to be successfully implemented. Effective governance relies on several factors, such as the level of involvement of senior management and the board, the frequency of discussions regarding responsible investment at board level, the presence of sufficient knowledge about responsible investment at board level, insight into the preferences of policyholders, and clear guidance from the board towards the asset manager in terms of targets or impact measurement.

Performance on governance slightly improved

The overall score for governance slightly improved from 3.4 in 2016 to 3.5 in 2017. PFZW, ABP, BPL Pensioen, PME, and PMT obtained the highest possible score, making them the highest performers on governance in the sector. Post NL and Rabobank Pensioenfonds showed the highest increase (+1.7). The following figures relate to the most relevant results on governance performance.

Responsibility for the responsible investment policy mostly at board level

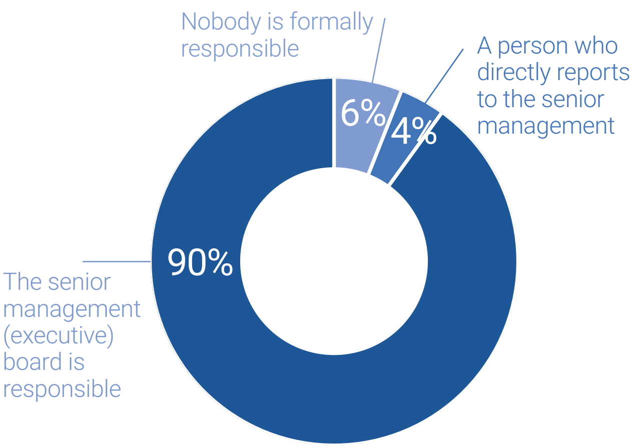

Figure 2.1 Responsibility for the development and approval of the responsible investment policy.

The responsibility for the development and approval of the responsible investment policy progressed upwards towards the senior management board, as has been the trend in previous years. As can be seen in figure 2.1, the board bears responsibility for the responsible investment policy at 90% of the pension funds. Related to this question is the frequency of discussions of responsible investment matters, as shown in figure 2.2.

Most boards discussed the responsible investment policy

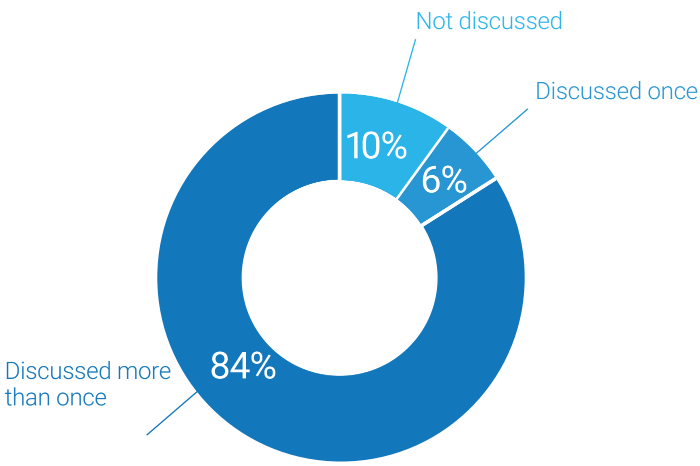

Figure 2.2 Frequency of discussions on responsible investment policy at senior level.

As can be seen in figure 2.2, 90% of the senior boards discussed the responsible investment policy in 2017; 84% discussed it at least twice. A word of caution for this result is that the pension funds that did not score points also include the non-respondents. Because it is often not possible to assess this question with publicly available documentation, pension funds who failed to provide minutes or agendas of board meetings have automatically not received points. In our experience, frequent discussions about responsible investment at board level is a good indicator for responsible investment performance, because it tends to result in a policy being comprehensively developed, evaluated and expanded. In some cases this is done by boards who have organised or attended workshops on how to implement Environmental, Social and Governance (ESG) criteria into their responsible investment policy. It should be noted that, rather than the quantity of discussions, pension funds should focus on the quality of these discussions. Sometimes the responsible investment policy is only briefly touched upon, and the discussion lacks depth or a concrete roadmap.

More than half of the pension funds do not set sustainability targets for their asset managers

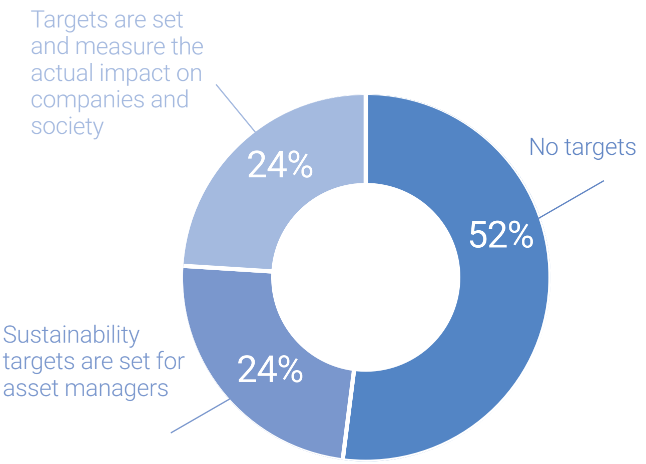

Figure 2.3 Sustainability targets for asset managers (2017).

Most pension funds have an external asset manager who acts as a trustee based on the investment mandate given by the pension fund. Setting targets on responsible investment for external asset managers enables the board to successfully improve, evaluate and shape the responsible investment policy. VBDO's view is that the asset owner, rather than the asset manager, should set the targets. Targets can be set for the external manager in the selection and monitoring process.

In total, 48% of the pension funds set sustainability targets for their asset managers (figure 2.3). Half of those funds set targets that measure the actual impact of the investments. The most common way of measuring the impact an investment has, is by measuring the carbon footprint. VBDO also encourages targets that are applicable to the entire portfolio such as the Sustainable Development Goals (SDGs). By measuring the impact of these targets on companies and society, pension funds will obtain more insight in the effect of their policies. Compared to previous years, no improvement can be seen here. This indicates that it remains challenging for the pension funds to set clear and measurable targets for their asset managers.

Consultation with stakeholders remains stable

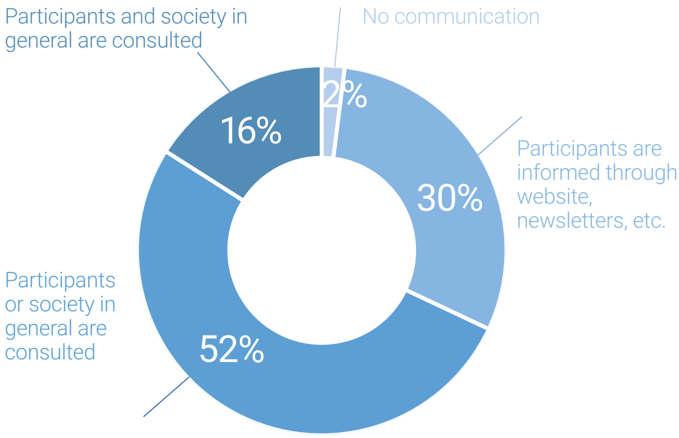

Figure 2.4 Communication and consultation with participants and other stakeholders regarding the responsible investment policy.

Responsible investment is based on acknowledging that institutional investors have a responsibility to decrease negative effects on society and improve positive effects. Therefore, a pension fund not only needs to be aware of economic developments, but also of the preferences of its stakeholders, e.g., participants, and any developments regarding sustainability. Seeking constructive dialogue with, for example, participants or non-governmental organisations (NGOs) on how the pension fund can assume its responsibilities, is a positive step. This way, pension funds are able to align their operations to the preferences of their stakeholders.

The number of pension funds that consulted either participants or society in general (e.g., NGOs or academics) remains quite stable at 68%. 16% consulted both participants and society in general. Even though a third of the pension funds did not consult participants and/or society in general, it is common practice for funds to at least inform stakeholders about their responsible investment policy.

Methods of consulting participants and wider society

Constructive dialogue helps to ensure that pension funds are kept up to date with new developments in sustainability, and reduces the distance between pension funds and their participants. The most common way participants are consulted is through participants' councils.

One way to reach a larger share of participants is through online surveys. There are differences in how pension funds frame questions about their responsible investment policies. In 2015, the VBDO published a report that investigated how pension funds consult their participants.[1] One of the recommendations was that pension funds should not frame responsible investment as if there is a trade-off between sustainability and returns. Still, in 2017 some pension funds ask whether participants prefer sustainability or profit to be prioritised in investment decisions. As this report shows, making decisions that also take ESG factors into account is part of risk management and identifying investment opportunities.

Another method through which participants are consulted is with open meetings. Even though this does not necessarily attract a representative share of participants, it does provide the opportunity to increase the quality of the conversation. The consultation of society in general is still less common than the consultation of participants, which offers opportunities for improvement.

[1] VBDO (2015), Raadplegen deelnemers pensioenfondsen over duurzaam beleggen.

2.2 Policy

This section refers to the responsible investment policy of pension funds. A comprehensive responsible investment policy describes, in detail, how sustainability themes are addressed. Therefore, a policy needs to cover the right areas in sufficient detail, in order to improve and increase the level of sustainable investments.

Firstly, prior to formulating a responsible investment policy, it is essential for pension funds to formulate their basic principles for investment, the so-called investment beliefs. The investment beliefs stand above the responsible investment policy and guide its content. It has become the norm for responsible investment to be mentioned in the investment beliefs. Secondly, the pension fund should formulate a long-term vision, which includes responsible investment strategies and specific targets relating to sustainability. Clear and measurable targets should be included in the responsible investment policy. These track progress and enable the evaluation and improvement of the policy. Thirdly, the responsible investment policy needs to be defined as clearly as possible and be available in publicly accessible documentation (which is discussed in section 2.4 'accountability'). Fourthly, the policy should cover the three ESG themes (Environment, Social and Governance) and be applicable to all asset classes. The next step is the integration of ESG information and sustainability trends in strategic asset allocation decisions and the asset liability modelling.

Performance on policy improved

Performance on policy improved from 3.0 (2016) to 3.1. In this category, no significant change in the average score has been observed for any of the questions. There were, however, still a number of individual fluctuations. The highest increase was shown by SBZ Pensioen (+1.5). The only, and first ever, maximum score was achieved by PME. The results of the policy category are outlined in this chapter.

All pension funds cover responsible investment in their investment beliefs

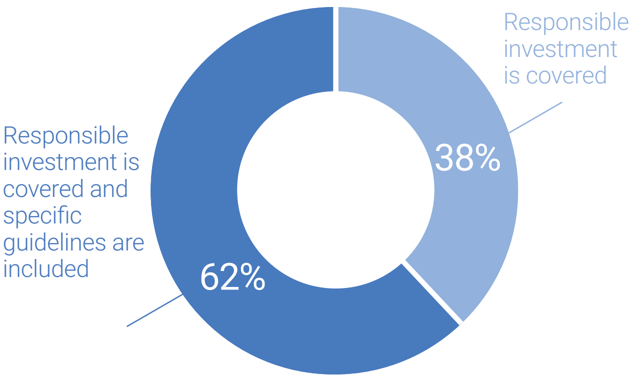

Figure 2.5 Responsible investment covered in the investment beliefs.

VBDO asked pension funds whether or not responsible investment is integrated into their investment beliefs. The investment beliefs are unique to each pension fund and contain the pension fund's beliefs on the highest abstraction level. Investment beliefs covering responsible investment can have different forms, such as, "We want our participants to retire in a world that is sustainable", "To prevent negative societal effects and, where possible, contribute to positive societal effects", and, "Both financial as well as environmental and/or social value are equally as important".
(Examples given by respondents.)

As of this year, every pension fund covers responsible investment in their investment beliefs (figure 2.5). More than half, i.e. 62% of all pension funds, provide guidelines specifying more clearly how the impact of investment beliefs is to be realised. A guideline can be, for example, that a pension fund specifies the sustainability themes to focus on. Even though the number of pension funds that incorporate responsible investment has steadily increased over the past three years, the amount of specific guidelines lags behind.

Setting targets remains challenging

Given their long-term liabilities, pension funds should be concerned with long-term investment performance, to provide and monitor investment mandates that reflect such an investment horizon. Sustainability should be part of the long-term strategy and vision of the pension fund. For the second year in a row, VBDO asked questions about if, and to what extent, sustainability is embedded into target setting. Specific targets help pension funds to take concrete actions and can be used to evaluate progress and improve performance. This year, VBDO has put more focus on whether targets contain an actual required improvement and if they are time bound.

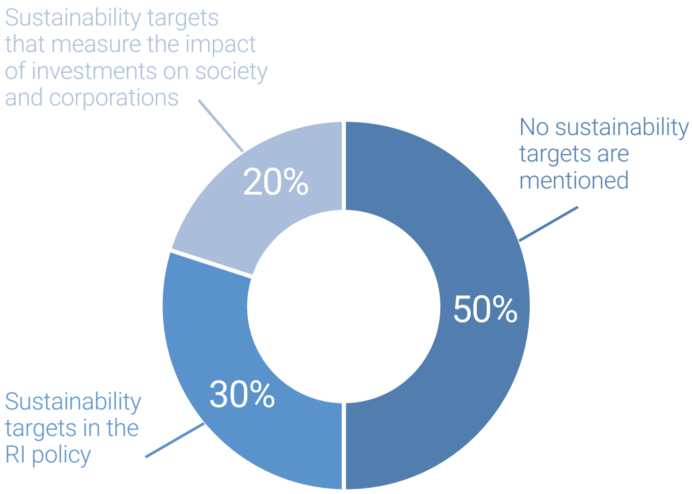

Figure 2.6 Sustainability targets mentioned in the long- term strategy and vision.

30% of the pension funds have set sustainability targets in relation to their responsible investment policy. Another 20% have set targets that actually measure the impact of investments on society and corporations. This is a similar result to the previous benchmark. However, most pension funds (50%) have not mentioned sustainability factors in their current target setting at all. Therefore, it can be concluded that it remains challenging for pension funds to set clear and measurable sustainability targets.

Sustainability targets can take different forms. A climate change mitigation target, e.g., "To reduce CO_2 emissions by X% through investments compared to [year]", was most frequently mentioned. However, with a 1.5 ºC rise already inevitable, pension funds also need to address how to adapt to the effects of climate change. Other targets are set for investments in renewable energy, sustainable real estate, or investing in themes that connect the pension fund to the industry (e.g. investments in affordable housing, healthcare or safe working conditions). Another development is that there is an increase in targets that have been set in terms of SDG investments. VBDO encourages this development, as the SDGs create a common language for all actors involved.

VBDO acknowledges the lack of widely agreed-upon standards in measuring and reporting on environmental and societal incomes. It also shows in figure 2.6 that measuring impact remains challenging. Of the pension funds that do measure impact, most use carbon emission measurements. This method is presently most developed and a CO_2 reduction target implicitly requires a measurement of the emissions. Including a **timebound** aspect to a target (e.g., 25% CO_2 reduction in five years), makes the achievement of the target measurable and stresses the importance of a long-term strategy. Currently, only a handful of pension funds have done this, and even fewer have set targets that go beyond the scope of 2020.

Responsible investment instruments are widely covered

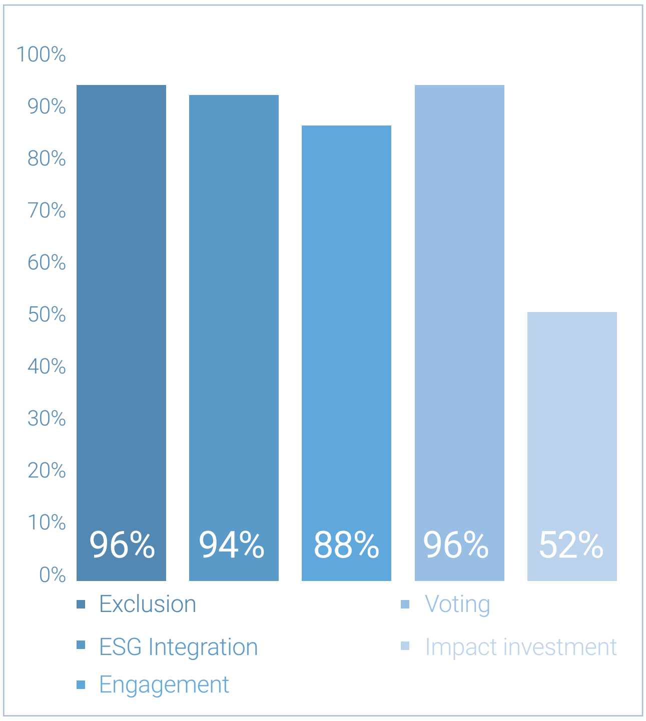

Figure 2.7 Responsible investment instruments used.

VBDO selected the widely accepted ESG themes as a basis for assessing the content of the policies. The translation of the ESG themes into responsible investment instruments, such as exclusion, ESG integration, engagement, voting, and impact investing, is vital in order to achieve the goals that are outlined in the responsible investment policy. Despite an overall high score, as figure 2.7 shows, differences remain in the quality and depth to which responsible investing is integrated in the asset classes. This will be discussed in the implementation section, 2.3.

Similar to last year, 52% of the pension funds implement all five responsible investment instruments. Strikingly, as figure 2.7 shows, the other half of the pension funds have not yet started using impact investing as a responsible investment instrument.

Use of ESG information for strategic asset allocation remains uncommon for most pension funds

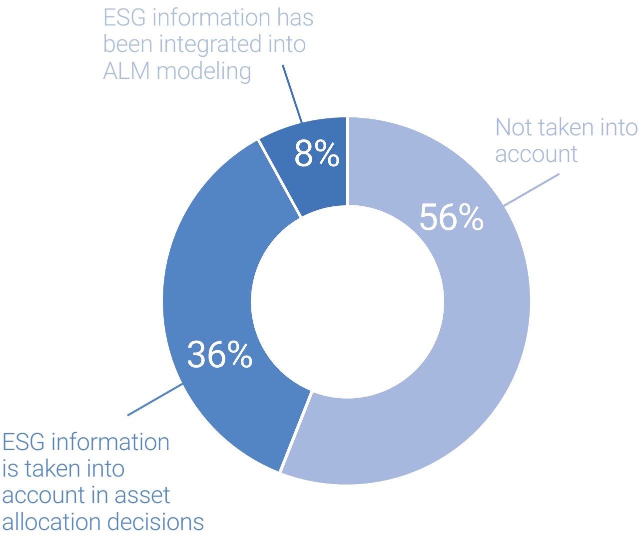

Figure 2.8 ESG information in strategic asset allocation.

ESG information could also be taken into account in strategic asset allocation. Information relating to renewable energy or fossil fuels (e.g., the discussion on the "Carbon Bubble") can, for example, be integrated into the investment process and lead to a larger or smaller exposure to the fossil fuel sector in all asset classes. Figure 2.8 shows that 44% of the pension funds use ESG information and sustainability trends in strategic asset allocation. Compared to the previous study, these results remained stable. Yet, an increasing number of pension funds express their intention to explore the possibility of integrating ESG information into asset allocation decisions. The highest attainable score is awarded to pension funds that integrate ESG information and trends into their asset and liability management (ALM)-modelling. Despite the fact that for most pension funds ALM-modelling is a common practice, only 8% of the pension funds integrated ESG information and sustainability themes.

Is ESG already 'factored' in?

New benchmarks, metrics and investment solutions are being developed that make ESG investing more accessible across asset classes and regions, and analyse to what extend investments are exposed to ESG risks.

Some pension funds consider ESG information in the strategic asset allocation; others take ESG information into account for their ALM-modelling. Another metric measures how a pension fund's portfolio is exposed to various climate scenarios. A 'business as usual' climate scenario will have a completely different impact on certain sectors than a scenario where e.g., commitments to the Paris Climate Agreement are successfully implemented. It is still exceptional for a pension fund to actively analyse how a 2°C, 3°C and 4°C climate scenario will each affect the risk/return of their investment portfolio.

Various market parties indicate that there are obstacles in this aspect as ESG and climate risks data are incomplete and are not always comparable. Nevertheless, steps should be taken. The adoption of IORP II by the European Parliament is a regulatory change which aims to improve knowledge, data and data-gathering methods regarding climate risks in the European pension sector. Pensions funds are required to:

a) improve their risk management so that potential vulnerabilities in relation to the sustainability of the pension scheme can be properly understood and discussed with the competent authorities,
b) include consideration of new or emerging risks (e.g. climate change) in their risk evaluations, and
c) ensure that members or beneficiaries are informed about how environmental, climate, social and corporate governance issues are considered in the investment approach.

2.3 Implementation

The creation of a comprehensive policy is a vital aspect of responsible investment. The implementation score then demonstrates how well the responsible investment policy is actually being implemented. Implementation is analysed by looking at the various asset classes and the applicable responsible investment instruments. For each asset class, several specific instruments have been identified, as shown in figure 2.9. The actual implementation of the responsible investment practices accounts for 50% of the total score of the benchmark.

This paragraph analyses:

A. Overall implementation results.

B. Results per instrument, based on the various asset classes: public equity, corporate bonds, government bonds, real estate, private equity and alternative investments (e.g., hedge funds, commodities and infrastructure).

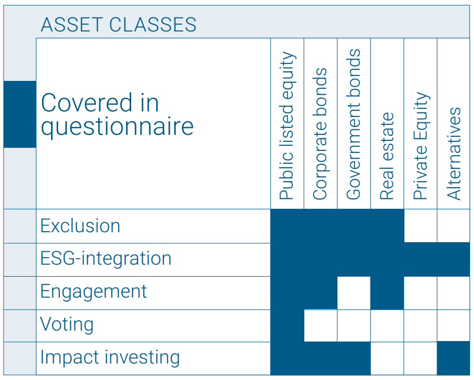

Figure 2.9 Responsible investment instruments and the different asset classes included in the benchmark.

A. Overall implementation results

Implementation performance slightly improved

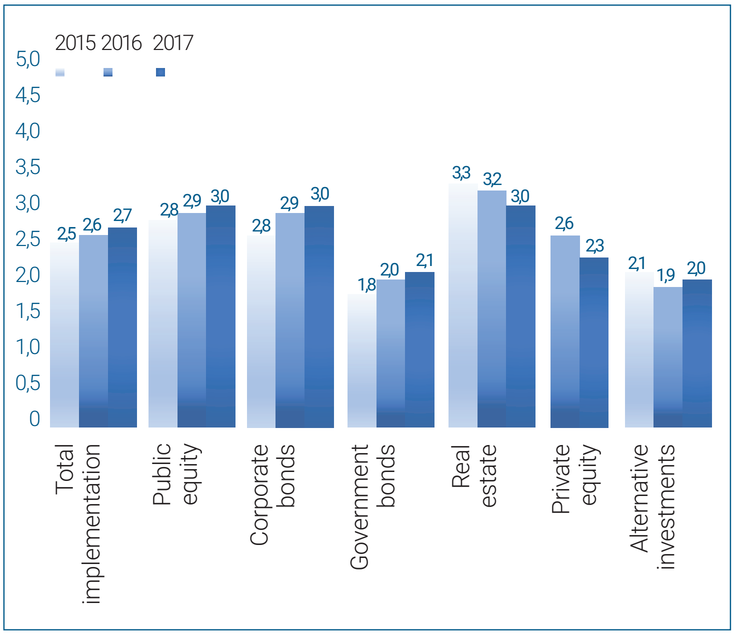

Figure 2.10 Total average score of implementation and per asset 2015 – 2017.

Figure 2.10 shows a slight increase in the overall implementation score (+ 0.1) compared to the 2016 results. Overall, results are similar or slightly improved for most asset classes, except for a decrease in real estate and private equity. The maximum score that can be achieved for implementation is 5.0, meaning the current total implementation score is still only 52% of the maximum score. As implementation has had the lowest score of all categories for seven years in a row, it can be concluded that it remains challenging for pension funds to implement their sustainability objectives.

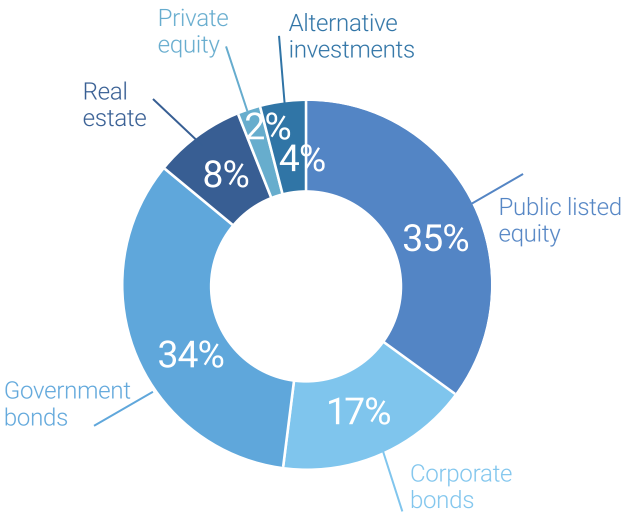

Figure 2.11 Average asset allocation of 50 largest Dutch pension funds in 2017.

Figure 2.11 shows the weight of the asset classes in the total portfolio of the pension funds in 2017. The allocation of assets determines the final score on implementation. Allocating more assets to an asset class that has a comprehensive responsible investment policy will positively affect the total implementation score. Although it is an individual case by case situation, it can be concluded that, in general, the scores on public equity and government bonds will strongly determine the final score on implementation. While the scores of the asset classes real estate, private equity and alternative investments will have less effect on the final score.

Within the implementation category, ABP and Bpf Bouw are the new best scoring pension funds, with an average score of 4.8. These are closely followed by Stichting Pensioenfonds voor de Woningcorporaties (SPW) (4.6), PFZW (4.5) and BPL Pensioen (4.5) The biggest growth was realised by ABN Amro Pensioen-fonds (+1.1).

B. Results per responsible investment instrument

VBDO distinguishes five different responsible investment instruments. Performance on these instruments is measured separately and the results are detailed in this chapter. The following instruments are covered: Exclusion, ESG Integration, Engagement, Voting, Impact Investing.

Exclusion

An exclusion policy indicates what types of investments the pension fund chooses not to make. This can either be done based on legal grounds, from a reputational standpoint, an ethical belief, or a sustainability perspective. The tool is utilised to systematically exclude companies, sectors or countries with certain characteristics or behaviours, from the universe of possible investments. Although exclusion is a relatively basic instrument, it does require a vision on controversial issues, such as corruption scandals, human rights violations and the manufacture of certain arms. Since 2013, exclusion of investment in cluster munitions is legally binding in the Netherlands. VBDO only assesses exclusion strategies that go beyond legally binding criteria. The most common criterion of exclusion encountered during the study was the exclusion of investments into controversial weapons (other than cluster munitions). Maximum points were awarded if pension funds are demonstrably excluding companies based on multiple criteria. The most mentioned exclusion criteria areas other than controversial weapons are human rights, environment/ climate, tobacco, UN Global Compact violations and business ethics such as corruption or fraud. Other criteria that were mentioned less frequently include fur, genetically modified organisms (GMOs) and pornography.

The exclusion policy for government bonds is analysed in a slightly different way than for the asset classes of public equity and corporate bonds. For government bonds, exclusion based on official sanction lists (e.g., EU, UN) equals one criterion; exclusion that is more extensive, by excluding based on the pension fund's own sustainability-related country considerations, equals multiple criteria. Pension funds can only receive the maximum score if they are demonstrably excluding companies based on multiple criteria. An often mentioned newly included country on the exclusion list is Venezuela because of the repressive nature of its regime.

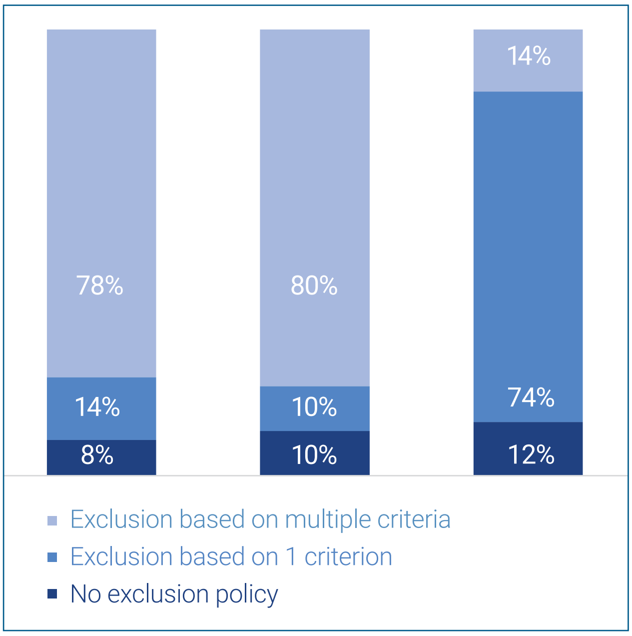

Figure 2.12 Extent of the exclusion policy per asset class.

As can be seen in figure 2.12, an exclusion policy was addressed in the three major asset classes. Both public equity and corporate bonds typically have a far-reaching exclusion policy, while implementation in government bonds lags behind. If an exclusion policy is implemented in public equity and corporate bonds, the majority exclude companies based on multiple criteria. This differs for government bonds, where the majority only use the UN and EU sanction lists. Excluding based on a pension fund's own sustainability criteria - related to country considerations - is in its infancy.

ESG Integration

ESG integration refers to the process by which Environmental, Social and Governance (ESG) factors are being integrated into the investment decision making process, complementary to financial data. It is a holistic approach that ensures ESG factors are identified and assessed to form an investment decision. Asset managers integrate ESG criteria for several reasons. A key component of applying ESG integration is to uncover hidden risks that might remain undiscovered without the analysis of ESG information and trends. ESG integration can also be done to identify investment opportunities that are likely to outperform competitors as a result of proper ESG management. It is therefore a misconception that ESG integration techniques might sacrifice portfolio return. Another common misconception is that ESG integration might prohibit investing in certain companies, sectors or countries. The fundamental difference between ESG integration and exclusion is that exclusion reduces the investment universe, whereas ESG integration does not necessarily.[2]

In this benchmark, three levels have been distinguished for the extent of ESG integration:

- Pension funds integrate ESG in some initial form - for example, they require their asset managers to be a signatory to the United Nations Principles for Responsible Investment (PRI).
- Pension funds use ESG information in a structured manner - for example, by using ESG information in the composition of an ESG index or through the use of one pagers regarding company sustainability performance.
- Pension funds integrate ESG criteria systematically with ongoing effects on individual holdings - for example, an automatic under or overweighting in company stock based on ESG criteria.

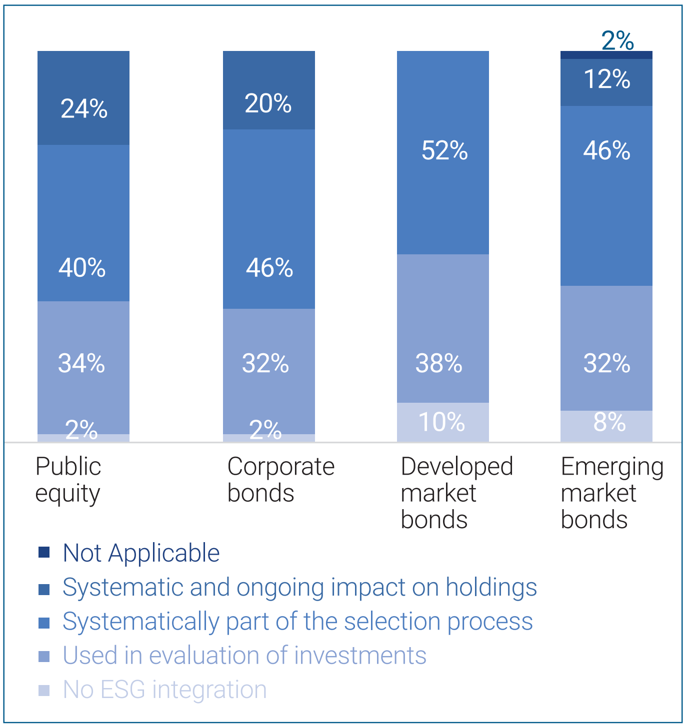

Figure 2.13 Extent of ESG integration per asset class.

[2] UN PRI (2018), *Guidance and case studies for esg integration: equities and fixed income*, https://www.unpri.org/download?ac=5398

Figure 2.13 shows that the level of ESG integration among the different asset classes differs. It can be concluded that, integrating a basic form of ESG information in the evaluation of investments is almost mainstream. Most of the pension funds do this by setting the requirement that their asset managers are PRI signatories.

Pension funds are improving their ESG integration practices in most asset classes

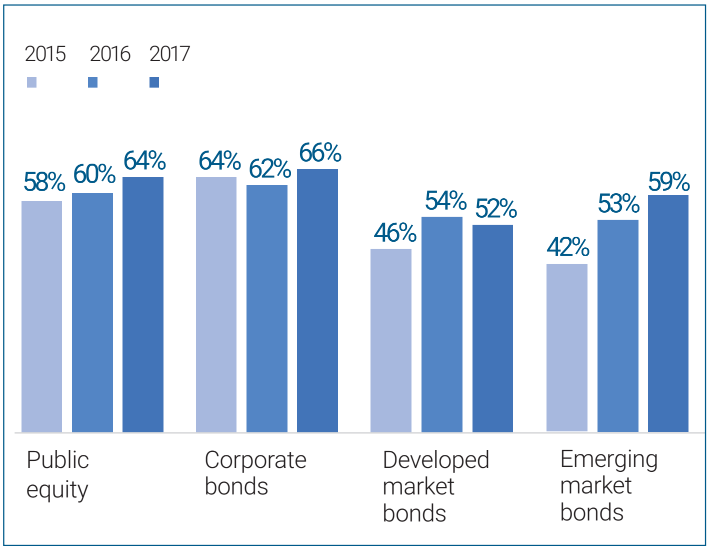

Figure 2.14 Systematic ESG integration in public asset classes.

Performance of ESG integration in public equity and corporate bonds improved

The next stage, where ESG information is systematically used for every investment in the portfolio, increased for most asset classes. This is e.g. done by ranking how ESG related risks potentially influence a company or how the management of a company has the capacity to limit these risks. As can be seen in figure 2.14, 64% of pension funds systematically take ESG issues into account up to this level for public equity and 66% for corporate bonds.

There are multiple ways of integrating ESG criteria into the investment decision. The ESG analysis can be the deciding factor between otherwise identical companies or countries. A way that has more potential impact is by creating an ESG analysis alongside the investment analysis to make a potential buy or sell decision, for instance if a holding fails to meet certain ESG criteria. For this, it is necessary that the investor creates an ESG score for all securities in the portfolio. More basic is when securities with high ESG risk are red flagged in lists or databases. The most common way ESG analysis has been done is by the composition of an ESG index or through the use of one pagers regarding company sustainability performance. In this benchmark, the third level of ESG integration shows that ESG analysis of a company or country has a systematic, verifiable impact on individual holdings. Examples include; implementing an inclusion policy, divesting in holdings that fall below a certain ESG threshold, accomplishing an improved average ESG rating through allocation changes. This policy should have an impact on every investment decision. A quarter of pension funds are able to show this for public equity and 20% for corporate bonds, as can be seen in figure 2.13.

ESG integration in government bonds remains challenging

ESG integration scores for government bonds are still lagging compared to corporate bonds and public equity. As can be seen in figure 2.14, ESG is systematically part of the selection process for only 52% of the pension funds for developed markets bonds and for 59% for emerging market bonds. Nonetheless, some pension funds have been able to develop detailed ESG country screenings, the following characteristics are all examples that can potentially influence the ESG score of a country:

- macro- economic developments such as unemployment rates
- elections or the changing influence of labour unions
- governance effectiveness factors
- vulnerability to natural disasters
- energy and food sovereignty

For the third level, pension funds still find it difficult to show that ESG can have an ongoing influence on investment decisions, especially if pension funds have only invested in a couple of western European bonds where ESG score differences are small. 12% of the pension funds have been able to demonstrate that their country ESG ratings have an impact on individual holdings for emerging market bonds, as seen in figure 2.13. This has been done, for instance, by showing that they do not invest in the bottom 25% of their

ESG ranking per category or because a country has suddenly plummeted in their ESG rating. This is seen as more difficult for developed markets, as they are considered "ESG proof", as they are often top performers on ESG issues. However, there is still a potential that ESG criteria will become an issue in the future. None of the pension funds have been able to show that a decline in ESG ratings will influence the selection of individual holdings. For this (third) level of ESG integration, it is unclear if this information leads to a change in investment decisions.

ESG integration in real estate, private equity and alternatives

The following section discusses the most notable developments for ESG integration in real estate, private equity, and alternatives including commodities and infrastructure.

Real estate

Responsible investment in real estate was measured by the degree of integration of ESG issues in (1) the maintenance or purchase of direct real estate, and (2) in the selection and evaluation of real estate managers. Real estate is a common asset class for pension funds to invest in; all of the pension funds have allocated at least some assets to this asset class, on average 8%. In direct real estate, ESG integration tends to involve energy efficiency and require the use of sustainable building materials. Of the 15 pension funds that invest in direct real estate, 11 have demonstrably considered ESG issues in the selection/development of new direct real estate investments and in its maintenance. Of the 48 pension funds that have invested in indirect real estate, 45 have been able to show that they take ESG criteria into account in the selection and evaluation of real estate fund managers or publicly listed real estate companies. Of these, 19 have been awarded a green star rating in the Global Real Estate Sustainability Benchmark (GRESB) for all of their real estate fund managers or have in some other way been able to prove that they only select the most sustainable real estate managers.
Some pension funds have even stricter criteria. One pension fund, noticed that an increasing number of real estate funds qualify for a green star, so they have made their policy more stringent. Since 2017, GRESB has added a 1 - 5 star rating. While a green star is awarded to real estate funds that have a satisfactory sustainability policy and implement it properly, the new star rating reflects how the funds are performing relative to each other. A fund that is clearly more sustainable than the others will be awarded five stars. This pension fund has taken the decision to only select real estate funds with four or five stars from now on, thereby only selecting the top 40% in the GRESB ranking.

Private equity

Since last year, VBDO paid special attention to the implementation of responsible investment policies in private equity. Despite private equity's controversial reputation, VBDO believes that private equity investment plays an important role in the transition towards a more sustainable society due to the considerable influence a private equity investor has on a company's strategy. Accordingly, private equity is being analysed as a separate asset class. A distinction has been made between indirect and direct private equity. With indirect private equity investments, the investor's primary moment of influence is at the manager and fund selection stage.
Sometimes pension funds invest directly in private equity, for instance through co-investing. For this type of investments, ESG criteria can be considered when the pension fund decides on the proposed (co-)investment. Of the pension funds that have investments in private equity, 83% considered ESG issues in their indirect private equity investments. The majority of them have done so by formalising their policy in deal documentation such as a side letter. However, sustainability in direct private equity is less advanced. Only six of the 11 pension funds that reported investments in direct private equity, considered ESG issues.

Commodities

In 2017, 19 pension funds invested in commodities, of which 12 demonstrably considered ESG issues in the selection/evaluation of those investments. Several pension funds stated that, because of ESG criteria, investments in commodities were excluded. Investments in commodities can be seen as controversial because of the financial speculation involved, particularly in the case of agricultural commodities on futures. Another alternative investment is hedge funds, in which only 12 pension funds invest and seven consider ESG issues in some of their hedge fund investments. Six pension funds consider ESG issues in the selection/evaluation of all of their investments in hedge funds.

Infrastructure

This year, an additional question has been asked which relates to ESG integration in infrastructure investments. Given its importance for the economy and society, infrastructure has a strong connotation to climate change. Infrastructure investments are suitable for pension funds, due to their size and long- term focus. It is important that ESG criteria are considered in the investment process, as these are relevant for most infrastructure investments. Areas for consideration include:

- low emission development and climate adaptation
- biodiversity impact
- labour, health and safety standards
- resource scarcity and degradation
- extreme weather events
- supply chain sustainability

ESG considerations in infrastructure also positively affect Sustainable Development Goal (SDG) 9, which states that investments in infrastructure and innovation are crucial drivers of economic growth and development.[3] The outcomes of the questionnaire indicate that 20 pension funds demonstrably take ESG issues into account in infrastructure investments and 13 do not (the other 17 do not invest in infrastructure). This clearly shows that this asset class shows room for improvement also.

Active ownership: engagement

Engagement practices

Engagement can help to optimise long-term value and manage reputational risk. It can also be done for the express purposes of bringing about positive social change, which is known as activist engagement. Effective engagement requires thorough preparation. It is important to monitor and increase the effectiveness of engagement and to prevent it from becoming an exercise in box-ticking, particularly given that most pension funds outsource engagement activities to specialised parties. The pension funds' engagement occurs in various forms. In a few cases the asset owner undertakes focused engagement with certain core companies. More commonly, engagement is outsourced to parties such as BMO, Hermes EOS, and GES. Sometimes engagement activities happen collectively, facilitated by organizations as Eumedion or PRI.
Pension funds often choose engagement themes that are linked to the profession of their participants, for example; a healthcare related pension fund practices engagement to encourage product reformulation and innovation to reduce the use of sugar in food production.

Another development is that engagement is now more frequently done through an SDG framework, usually by highlighting which SDGs align with the fund's engagement efforts. Other funds choose one or two SDGs that connect well to their theme and choose engagement projects that contribute to this SDG.

Increase in number of pension funds that practise engagement

As shareowners of the companies they invest in, pension funds can actively influence the policies of these companies by entering into a dialogue. A total 89% of all pension funds actively engage with some of the companies they invest in in the public markets (90% public equity and 88% with regard to corporate bonds). Most of the funds engage on each of the three ESG themes (Environmental, Social, Governance) for their public equity portfolio. These figures show that practicing engagement has become the norm.

[3] UNDP, Goal 9: Industrial innovation and infrastructure, http://www.undp.org/content/undp/en/home/-sustainable-development-goals/goal-9-industry-innovation-and-infrastructure.html

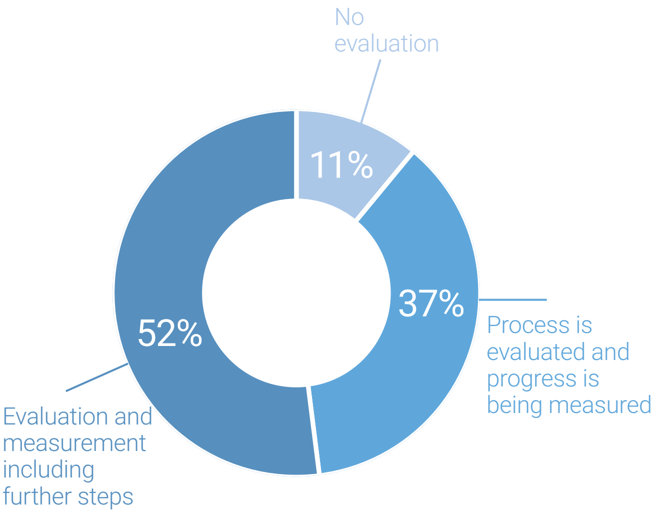

Figure 2.15 Engagement process for public equity and corporate bonds.

Half of the pension funds (52%) are taking further steps as a result of engagement with companies regarding their assets in public equity and corporate bonds. The most common way of taking further action is to exclude companies when the engagement process has failed to lead to any improvement. Although many pension funds have written in their policy that exclusion is a possible result of failed engagement projects, it is notable that this is not yet visible in the exclusion lists of several pension funds. Figure 2.15 shows the percentage of pension funds that practice engagement and take further steps. The percentage shown is the average of the two asset classes, public equity and corporate bonds.

Engagement in real estate

As mentioned in figure 2.11, the share of real estate in the total asset allocation is small. Nevertheless, engagement can be an important instrument in this asset class. Of the 48 pension funds that invest in indirect real estate, one third do not practice engagement, and only one third show demonstrable results of their engagement efforts. Examples of possible improvements include enhanced ESG screenings by real estate managers or an improvement of GRESB ratings.

Active ownership: voting

Pension funds hold a strong position in the companies they invest in. By voting at annual shareholder meetings they can influence and steer corporate policies. Therefore, incorporating sustainability into their voting policies can foster sustainable business practices. Publicly initiating and supporting shareholder resolutions that promote sustainability can increase the positive influence of pension funds even more. As is the case with engagement, most pension funds outsource the practice of voting to external parties. This practice is called proxy voting, whereby a pension fund delegates its voting power to a representative.

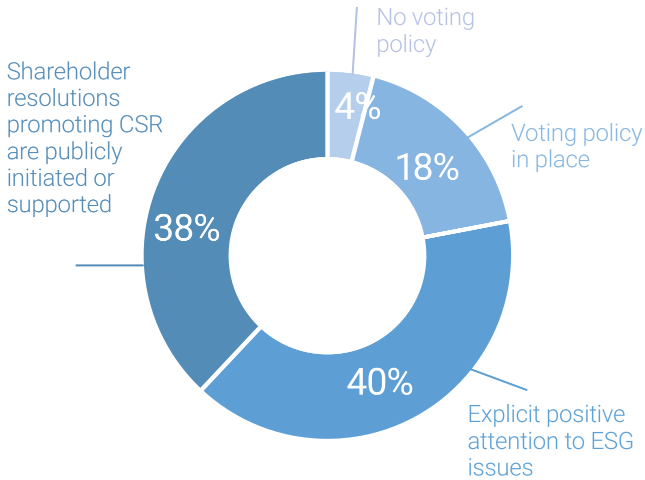

Figure 2.16 Extent of the voting policy.

As can be seen in figure 2.16, 96% of the pension funds demonstrably vote on at least some of their public equity holdings. Out of those, 78% vote while paying explicit attention to ESG issues, and 38% publicly initiate and/or support shareholder resolutions promoting CSR or sustainability. While almost all of the pension funds have a voting policy, no overall improvements can be seen in the level of depth (incorporating ESG issues or publicly initiating or supporting relevant shareholder resolutions) of voting policies since 2015. It must be stressed that no points have been awarded for pension funds that have an ESG voting policy that is limited to remuneration issues.

The most often mentioned publicly supported shareholder resolution was ‘Follow This’, a group of shareholders that tries to push Shell to commit to specific targets regarding the Paris Climate Agreement. Another example of a successful shareholder resolution that was initiated by one of the pension fund's asset managers was the 'As You Sow' resolution to McDonalds, which resulted in the fast food giant agreeing to reduce plastic pollution by ending the use of polystyrene packaging in its restaurants around the world by the end of 2018.

Impact investing

Impact investments are done with the intention of achieving a positive societal impact whilst also generating a competitive financial return. Institutional investors in particular can have an impact in reducing the impact of climate change. They can catalyse climate adaptation and mitigation by channelling their investments from carbon intensive industries to renewable energy and use their influence in nudging companies into a transition process.[4]

The practice of directing capital towards business or governmental activities that also generate positive environmental and/or societal results is becoming more common. To be more effective, it is essential that the actual impact on society and environment of the investments is measured and monitored. VBDO believes a well-balanced investment mix should include impact investing. In this study, impact investments were measured for all asset classes. The impact investments in private equity were measured under alternative investments.

Examples of impact investments include:
- Affordable housing
- Healthcare
- Microfinance funds, which create business and development opportunities for society
- Renewable energy
- Green and social bonds

In some cases, it is difficult to assess whether an investment can be categorised as an impact investment as there is no universal definition. An increasing amount of pension funds regard impact investments from a SDG perspective, which are referred to as Sustainable Development Investments (SDIs). Some pension funds only call an investment an SDI if it relates to a newly invested SDG cause. Others reassess their portfolio to determine what percentage can be deemed as positive investments aligned to the SDGs.

Impact investing per asset class

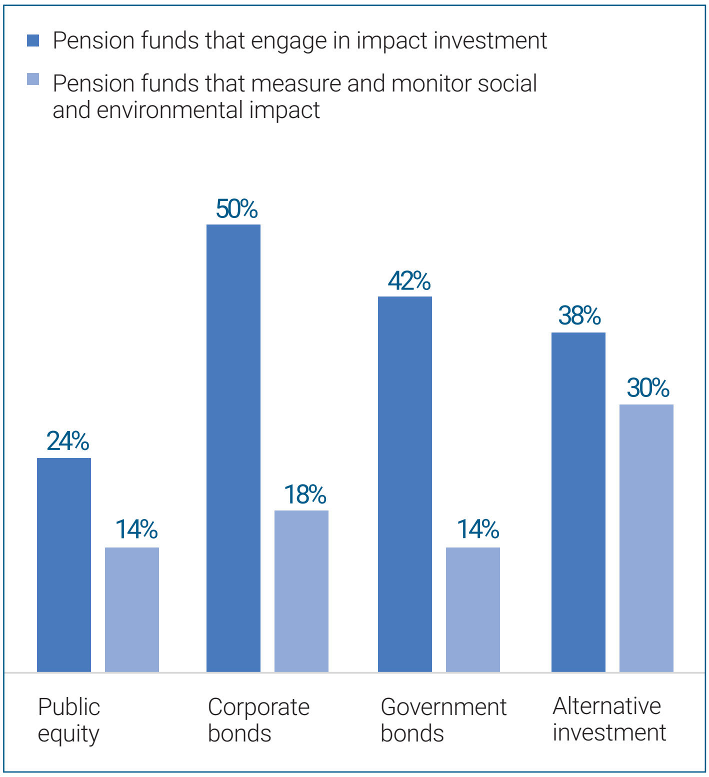

Figure 2.17 Impact investment and measurement per asset class (2017).

Figure 2.17 shows what percentage of the pension funds that intentionally engage in impact investments, measure and monitor social and environmental impact of those investments. It shows that not all of the pension funds that engage in impact investments have a process in place where they measure the actual impact of their investments. Compared to 2016, the percentage of pension funds that have impact investments in their public equity and corporate bonds portfolio has remained stable, impact investments in government severely increased, and the impact investments in alternatives decreased.

[4] VBDO (2017), White paper Institutional investors and climate change.

Growing market in green and social bonds

Green and social bonds are issued by companies and governmental institutions to finance specific projects that have a positive environmental or social outcome. As these are fixed income products, it gives mainstream investors access to climate-related investment opportunities. Until recently, most bonds were issued for renewable energy projects, but the market has developed and expanded to several other sectors. Consequently, demand for such bonds is steadily growing and most issues are oversubscribed.

The growing appetite for green bonds is driven by institutional investor who have committed to making their investment portfolios greener. At the same time, the absence of generally accepted definitions and standards (on whether bonds are actually green) is hampering credibility and the development of the green bond market. An increasing number of investors have stricter considerations for the evaluation of green bonds than previous years and are, therefore, demanding greater transparency. Some pension funds analyse in detail the impact of different green bonds and use "green" methodologies to filter out the best companies within a sector and exclude "light-green or dirty" companies. VBDO believes an open but stringent approach could provide more transparency on the various green, low-carbon definitions in use which support the development of internationally harmonised green standards in the market place.

Significant increase in green and social bonds

Perhaps the most significant increase of this year's study is the volume of green and social bonds that have been bought by the pension funds. Half of the pension funds invest in corporate green or social bonds and 42% invest in governmental or supranational green or social bonds, as can be seen in figure 2.18.

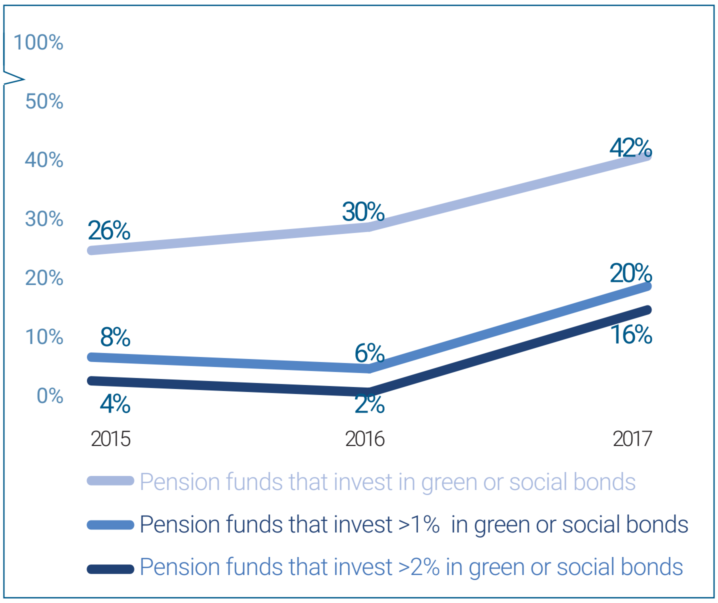

Figure 2.18 Volume of governmental or supranational green or social bonds.

Compared to previous studies, there has been a significant increase in the number of pension funds that hold governmental or supranational green or social bonds. The total amount of pension funds that invest in these bonds has increased from 26% in 2015 to 42% in 2017. Similarly, the volume of green and social corporate bonds has increased significantly. 18 pension funds invest more than 2% in green or social corporate bonds, compared to five last year. The increase is not caused by a decrease in total asset allocation towards corporate or government bonds signifying an absolute increase in the amount of investments in green or social bonds.

2.4 Accountability

Transparency on responsible investment strategies is essential for pension funds, as is the frequent reporting of changes, results and impacts. Information given in the report is the starting point for communication with and accountability to the participants of the fund. The annual report also serves as the source for communication with other interested stakeholders, such as the government and civil society. Since 2014, The Pension Act requires pension funds to state in their annual report 'how the investment policy takes account of the environment and climate, human rights and social relations'. The Pension Fund Code further specifies: "The board determines its considerations regarding responsible investment and ensures that these are available to stakeholders" and "The board ensures that there is support among stakeholders for the choices about responsible investment".[5]

With this in mind, both the responsible investment policy and reports about the implementation of the policy should be easily accessible, and either published in a responsible investment report or integrated in a fund's annual report. Ideally, these reports should be verified by an external auditor.

It is important for pension funds to actively inform participants through the fund's website and various other communication channels, to give updates on how the responsible investment policy is guiding investments. Digital communications such as magazines, short movies, newsletters and social media enable pension funds to reach a wider audience.

Accountability performance slightly improved

The results of this category showed that in 2017, for the first time, every single pension fund mentioned its responsible investment policy on its website. Out of a maximum of five points, the average score on accountability slightly increased from 3.1 (2016) to 3.2 (2017). ABP, PMT and PME became the first pension funds to score the maximum five points on accountability. PFZW and BPL Pensioen followed closely with 4.9 and 4.8, respectively. Pensioenfonds Huisartsen (+1.2), Pensioenfonds Detailhandel (+1.1), and Pensioenfonds UWV (+1.0), all showed significant improvements in this category. The following figures present the most significant results.

A third of all pension funds published a standalone responsible investment report

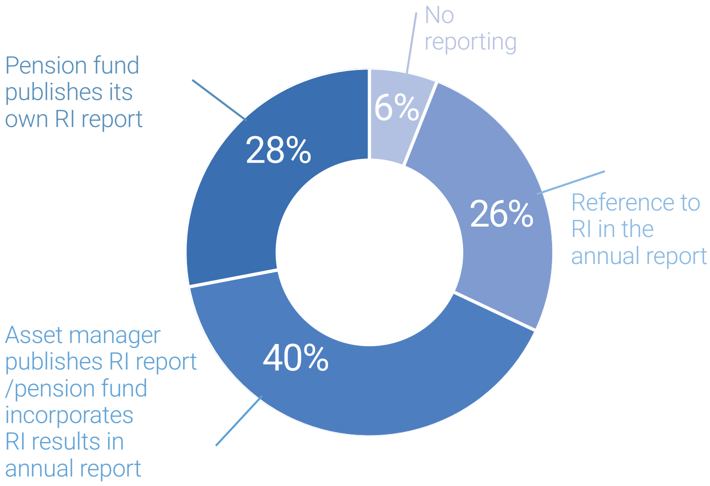

Figure 2.19 Reporting of the responsible investment policy and results.

Of the pension funds in scope, 94% report annually on responsible investment, as can be seen in figure 2.19. However, the level of detail and the extent of reporting vary significantly. The statement 'reference to responsible investment in the annual report' is quite broad; some pension funds that selected this response dedicate only a single paragraph to sustainability. Other pension funds (or their external asset manager) publish a comprehensive responsible investment report. 28% of the pension funds publish a standalone responsible investment report themselves, figure 2.19.

Transparency per investment strategy

It is encouraging to see that pension funds continually increase their score on transparency. For most instruments, it is already quite common to refer to the policy on the pension funds website. However, there is room for improvement: greater depth in reporting on the use of responsible investment instruments, including their results.

[5] Art 135 (4) Pensions Act. 'Code Pensioenfondsen', Pensioenfederatie en Stichting van de Arbeid, 2013.
http:// www.pensioenfederatie.nl/actueel/persberichten/Pages/Pensioensector_legt_ambitieuze_ doelen_over_bestuurlijk_functioneren_vast_in_Code_28.aspx

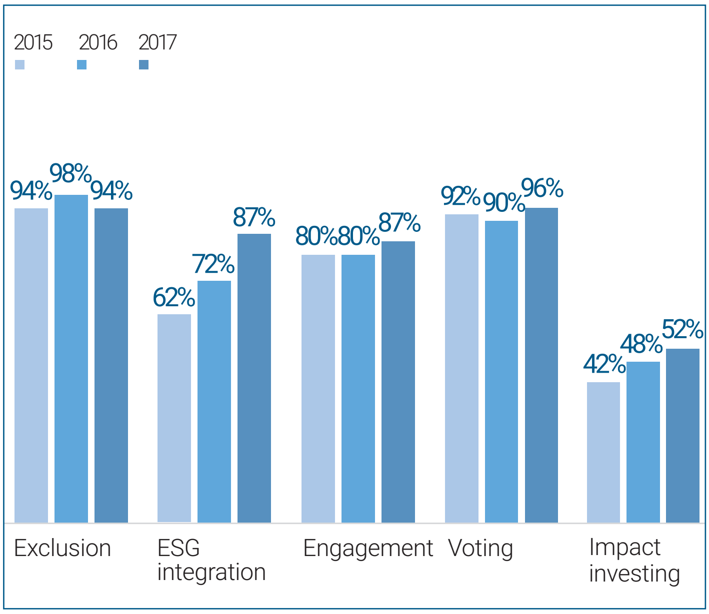

Figure 2.20 Transparency on implementation.

Level of detail and extent of reporting vary significantly

Over the years, substantial improvement has been made with regards to the level of detail and extent of reporting. In the case of exclusion policies, 94% of the pension funds publicly explained their policy in 2017, shown in figure 2.20.
The majority of these funds published the exclusion policy, including a list of countries and companies and the reason(s) for their exclusion. This is a decrease compared to the previous study, which saw 80% of funds publish an exclusion list. With regard to ESG integration, however, an encouraging increase is observable. The percentage of pension funds that explain their methodology for ESG integration has increased by 20% in two years, as seen in figure 2.20.

With a slight increase of 4%, pension funds are almost equally transparent on their engagement policy, shown in figure 2.20. Taking further steps, as a result of engagement activities, improves the effectiveness of the engagement policy. In 2017, 70% of funds published an overview of their engagement activities, with for instance the amount of engagement activities and ESG themes they are based on, or sectors they are focused upon. This is the same percentage as in 2016 and 2015, showing that there is no improvement in the detail of reporting.

Pension funds further increased transparency on their voting policy. Half of the pension funds published a detailed voting activity report, which contained additional comprehensive information (i.e., the number of meetings, agenda items, votes by region and/or votes by topic). As can be seen in figure 2.20, the percentage of pension funds that explain their considerations for impact investing, and report and measure impact investing, has increased to 52%. To conclude, there is some increase in reporting on responsible investment instruments, however the depth to which pension funds report on the outcomes leaves room for improvement.

Half of all pension funds disclose a list of investments

By publishing a publicly available list of investments, pension funds provide an overview of all the investments made and disclose the names of the companies and the funds invested in. As is done by front-running pension funds which publish a list of their investments as well as their exclusion lists. Providing such an overview publicly is highly valued by VBDO and recommended for other parties. 26 pension funds (52%) do not disclose their list of investments. 24 pension funds do publish a list of investments on their website, of which 17 funds disclose 76-100% of their total portfolio.

Distinctiveness through stakeholder transparency

Actively informing stakeholders about the responsible investment policy and outcome is regarded as the next step for full accountability. This should exceed publishing sustainability information and a report on the website, and should include disclosing information about responsible investment (e.g., through face-to-face meetings, newsletters, information packages and social media). In 2017, 66% of the pension funds surveyed actively informed participants by means of at least one of the aforementioned communication tools, with 36% of the total number using more than one communication tool, as seen in figure 2.21.
A third of the pension funds do not actively inform their participants about their responsible investment policy.

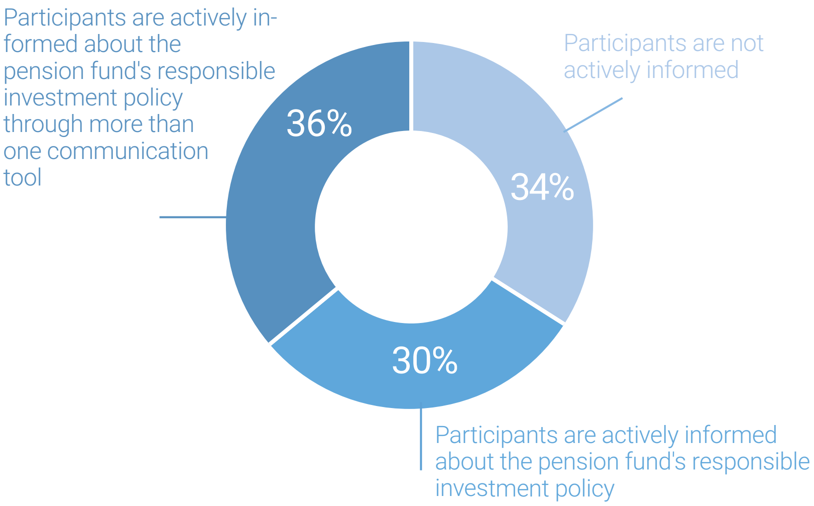

Figure 2.21 Informing stakeholders about the pension fund's responsible investment policy.

It is notable that many pension funds limit their active transparency to just their newsletter, which often includes only a few paragraphs about responsible investment. Surprisingly few pension funds use modern communication tools such as social media.

Example of informing participants

A form of active engagement with participants is a pension fund that communicated with participants by driving a bus through the country. Participants were invited to enter the bus and ask questions about the fund's responsible investment policy. This is an excellent example of a pension fund actively communicating with its participants.

3. Conclusion

This chapter presents the final conclusions based on analysis of the results presented earlier. Overall conclusions are given first, followed by more detailed conclusions for the performance categories governance, policy, implementation and accountability.

I. Overall conclusions

Overall responsible investment performance remained stable
The responsible investment performance of the 50 largest Dutch pension funds remained stable in 2017 compared to 2016. The average total score increased by a mere 0.1, showing a deceleration of the improvements that have been achieved in the previous years.

Top performing pension funds continue to improve
The top 10 performing pension funds have all improved their total scores (as can be seen in appendix 1). For the first time, the top four (ABP, PFZW, Bpf Bouw and BPL Pensioen) has achieved a five star rating based on their improvements in the implementation category. Pensioenfonds Detailhandel and Pensioenfonds PGB showed most progress compared to last year.

Performance of pension funds in the midfield varies significantly
Several individual substantial improvements were made in the midfield. These improvements have, however, been offset by other pension funds that were not able to maintain the same score as in the previous benchmark. Even though many pension funds have indicated that their policy is developing, this has not yet resulted in enough actual improvements. This observation is further backed by the fact that for the zero to two star categories, the implementation scores are significantly lagging. This means that, in spite of some positive exceptions, on the whole there is no improvement in the total scores of the pension funds in the zero to two star category.

Size does not always matter
As well as some of the biggest pension funds (in terms of AuM), which have more capacity and resources to expand and improve their responsible investment policies, a select number of smaller pension funds (in terms of AuM) are also in the vanguard. The smallest pension fund in the five star category has a significantly smaller amount of AuM than the largest pension fund in the one star category. Clearly, size does not always determine how well a pension fund performs on responsible investment.

II. Conclusions in specific performance categories

Pension funds remain hesitant to reach out to their stakeholders
Actively informing participants and seeking constructive dialogue with, e.g. NGOs or other experts, on how the pension fund can assume its responsibilities, remains challenging. Only a third of pension funds use various communication tools to actively reach out to their participants.

Setting sustainability targets is not common practice
Only half of the pension funds did set long-term sustainability targets. As the majority of pension funds focus on climate mitigation targets (e.g., carbon reduction targets), more attention should be directed to broader issues such as climate adaptation and living wages. Setting targets that are time bound and measure actual impact is still exceptional. Likewise, half of the pension funds remain hesitant to impose sustainability targets on their asset managers.

ESG integration improved in most asset classes
Translating the responsible investment policy into the instruments exclusion, ESG integration, engagement and voting is common practice. Each of these instruments has been used by almost all the pension funds. ESG screening seems to be becoming more extensive and detailed. However, it is still challenging for pension funds to ensure that ESG criteria have a systematic and ongoing impact on individual holdings, especially for government bonds. Despite this, an increasing number of pension funds express their intention to explore the possibilities of ESG information and themes (e.g. by creating climate scenarios) and integrate them into the fund's strategic asset allocation and ALM-modelling.

Growing appetite for green and social bonds
There is a significant increase in the amount of pension funds that buy green or social bonds. Almost all pension funds that were already investing in corporate green or social bonds

significantly increased their volume in these specific bonds. Another encouraging improvement is that pension funds are increasingly demanding greater transparency on the use of the proceeds of green and social bonds.

Level of detail in reporting varies

Some pension funds publish comprehensive responsible investment reports, whereas others limit their reporting to a few paragraphs in the annual report. A growth can be seen in the number of pension funds that publish an explanation of their ESG integration, whereas the level of detail and the extent of reporting on other separate instruments did not improve.

4. Recommendations

This chapter sets out VBDO's main recommendations.

Be clear and bold

With a fiduciary duty to serve the interests of participants in a broad sense, all pension funds should develop a clear vision on how they can best contribute to a sustainable society. This vision should be the backbone of the responsible investment policy. From there on we urge pension funds to be bold and formulate ambitious and smart targets, for themselves and the asset managers they work with, on how they are facing up to their fiduciary duty.

Improve ESG integration

Responsible investing is more effective when it is primarily integrated into existing processes, rather than carried out in parallel. An increasing number of pension funds use ESG indicators for their investment processes to identify additional sources of risk and opportunity. The use of ESG integration is still not common place, however, and could be further improved and expanded in portfolio management to address specific criteria and cover a broader range of issues. Examples are climate adaptation, plastic, living wages, biodiversity, tax transparency, and so on.

Look outwards

It is becoming increasingly important for pension funds to be in touch with their participants and understand their interests in a quickly changing society. There are various ways in which pension funds can engage with their participants and also seek constructive dialogue with other stakeholders. This external orientation can provide important input for pension funds to develop their vision on sustainability.

As sustainability issues are becoming more mainstream in the investment process, a great deal of new information needs to be retrieved and processed. It is very challenging for a single pension fund to keep up with all these new insights, methods and metrics. Collaborating with other pension funds or experts can make the process much easier.

Top performing pension funds, which often have more resources available, are well positioned to take leadership and initiate the conversation between pension funds. Pension funds, participants, NGOs, regulators and governmental agencies could use platforms to jointly address developments and topics such as climate change, human rights and other themes related to the Sustainable Development Goals. This approach also helps pension funds to stay better aligned with their participants and wider society, and could in turn provide input to further shape and improve pension funds' visions and responsible investment policies.

Offer clarity through clear reporting, and by adhering to guidelines and regulation

To ensure transparency, pension funds should explain their responsible investment policy and monitor and report on progress in a clear and consistent way. This gives stakeholders an understanding of which topics have been focused on, what steps have been taken, and what (environmental and societal) impact the investments have had.

To a large extent, reporting on responsible investment is encouraged by voluntary codes, guidelines and standards. However, mandatory legislation is also on the rise. Pension funds should ensure that they comply with relevant environmental regulatory standards and recommendations. These could include:

- The European Directive IORP II requires that pension funds and providers assess the ESG risks of their investments following a specific set of criteria and that ESG risks acquire an equal level of attention compared to operational, liquidity or asset risks. The transposition into Dutch legislation will take place in January 2019.
- EU Action Plan, action 7 requires asset owners and asset managers to clarify how sustainability considerations are considered as part of their fiduciary duty.
- EU Directive: Disclosure of Non-financial Reporting requires to disclose certain non-financial information, including non-financial key performance indicators on environmental matters and human rights.
- The Task Force on Climate-related Financial Disclosures (TCFD) guidelines recommend that reporting on material climate risks is integrated into companies' ordinary financial reporting. The TCFD divides its recommendations into governance, strategy, risk management, and metrics and targets.
- The Pension Fund Code requires pension funds to define a responsible investment strategy and disclose it publicly. In addition, the Dutch central bank is also examining how

asset owners and managers integrate climate risk into their investment decisions.
- The anticipated voluntary agreement IMVO Covenant on Pension Funds, on which pension funds aim to contribute to multiple goals, i.e. guaranteeing a good and affordable pension and also contributing to a stable economy and a sustainable, safe and just world.

As this report shows, addressing sustainability on a fundamental level and translating it to responsible investment strategies requires pension funds to constantly evolve. There has been a lot of improvement, however pension funds need to ask themselves whether they are doing enough and what more they could do. VBDO hopes to create a dialogue between pension funds, asset managers and financial regulators to develop further understanding and broader long-term responsible investing issues.

Appendix I: **Quantitative ranking**

Ranking 2018	Change	Ranking 2017	Pension fund	Overall score 2017	Overall score 2018	Gover-nance	Policy	Implemen-tation	Accoun-tability	Star ranking
1	= 0	1	ABP	4,5	4,8	5,0	4,5	4,8	5,0	★★★★★
2	▼ -1	1	PFZW	4,5	4,7	5,0	4,5	4,5	4,9	★★★★★
3	▲ 1	4	Bedrijfstakpensioenfonds voor de Bouwnijverheid (Bpf Bouw)	4,3	4,6	4,6	4,5	4,8	4,5	★★★★★
3	▼ -2	1	BPL Pensioen	4,5	4,6	5,0	4,5	4,5	4,8	★★★★★
5	= 0	5	Pensioenfonds voor de Woningcorporaties (SPW)	4,1	4,4	4,6	4,0	4,6	4,1	★★★★
6	▲ 1	7	Pensioenfonds van de Metalektro (PME)	3,8	4,3	5,0	5,0	3,6	5,0	★★★★
7	▲ 8	15	Pensioenfonds Metaal en Techniek (PMT)	3,6	4,1	5,0	4,0	3,5	5,0	★★★★
8	▲ 9	17	Pensioenfonds PNO Media	3,5	3,9	4,4	3,5	3,7	4,5	★★★
8	▼ -1	7	Pensioenfonds SNS Reaal	3,8	3,9	4,0	4,0	4,1	3,2	★★★
8	▲ 3	11	Pensioenfonds Progress (Unilever)	3,7	3,9	4,0	4,0	4,0	3,3	★★★
8	▲ 9	17	Bpf Schilders	3,5	3,9	4,0	4,5	3,3	4,6	★★★
12	▼ -6	6	Spoorwegpensioenfonds	3,9	3,8	4,0	4,0	3,4	4,6	★★★
13	▼ -6	7	Ahold Delhaize Pensioen	3,8	3,7	4,6	4,2	3,2	4,0	★★★
13	▼ -6	7	Stichting Pensioenfonds Openbaar Vervoer (SPOV)	3,8	3,7	4,0	4,0	3,2	4,6	★★★
15	▼ -4	11	SBZ Pensioen	3,7	3,6	4,6	4,0	2,8	4,5	★★★
15	▼ -4	11	Pensioenfonds Werk en (re)Integratie (PWRI)	3,7	3,6	3,5	3,5	3,3	4,3	★★★
17	▲ 2	19	Pensioenfonds KPN	3,3	3,5	4,2	4,0	3,3	3,3	★★★
17	▲ 4	21	Pensioenfonds PostNL	3,1	3,5	4,6	4,0	3,1	3,3	★★★
19	▼ -8	11	Heineken Pensioenfonds	3,7	3,3	4,0	2,7	3,2	3,7	★★
20	▲ 1	21	Rabobank Pensioenfonds	3,1	3,1	4,6	2,7	3,1	2,4	★★
20	▲ 9	29	Pensioenfonds Vervoer	2,8	3,1	4,0	3,0	2,6	3,9	★★
20	▼ -1	19	Pensioenfonds voor Huisartsen	3,3	3,1	3,3	3,5	2,7	3,9	★★
23	▲ 15	38	Pensioenfonds Detailhandel	2,3	3,0	4,4	3,3	2,2	4,1	★★
24	▲ 14	38	Pensioenfonds PGB	2,3	2,9	3,3	2,9	2,7	3,0	★★
24	▲ 6	30	Pensioenfonds Horeca en Catering	2,6	2,9	3,8	4,0	2,6	1,9	★
26	▼ -11	15	Stichting Pensioenfonds voor de Architectenbureaus	3,6	2,8	1,7	2,8	3,6	1,9	★
26	▼ -3	23	Philips Pensioenfonds	3,0	2,8	2,9	3,2	2,7	2,8	★★
26	▲ 4	30	Pensioenfonds Wonen	2,6	2,8	3,3	2,8	2,9	2,2	★★
26	▼ -3	23	Bedrijfstakpensioenfonds voor het Levensmiddelenbedrijf	3,0	2,8	3,5	2,7	2,8	2,2	★★
26	= 0	26	Bpf Schoonmaak	2,9	2,8	2,9	3,3	2,7	2,5	★★
26	▲ 7	33	Pensioenfonds DSM Nederland	2,5	2,8	3,3	3,5	2,1	3,6	★★
26	= 0	26	Pensioenfonds Achmea	2,9	2,8	3,3	3,3	2,3	3,1	★★
33	= 0	33	Pensioenfonds APF (AkzoNobel)	2,5	2,7	3,3	2,4	2,5	3,2	★★
33	▼ -5	28	Bedrijfspensioenfonds voor de Koopvaardij	2,9	2,7	2,5	3,2	2,6	2,6	★★
35	▲ 6	41	Pensioenfonds TNO	2,1	2,6	3,3	2,4	2,4	2,8	★★
36	▼ -6	30	Stichting Pensioenfonds voor Fysiotherapeuten (SPF)	2,6	2,4	3,3	1,9	2,4	2,0	★
36	= 0	36	Pensioenfonds IBM Nederland	2,4	2,4	4,0	3,2	1,7	2,4	★
36	▼ -13	23	Stichting Pensioenfonds Medisch Specialisten (SPMS)	3,0	2,4	3,3	2,2	1,9	3,1	★
36	▲ 7	43	ABN AMRO Pensioenfonds	1,7	2,4	2,9	2,2	2,2	2,5	★
40	▼ -2	38	Pensioenfonds UWV	2,3	2,2	2,9	2,2	1,9	2,6	★
41	▲ 5	46	Pensioenfonds Hoogovens	1,4	2,1	3,3	2,4	1,6	2,3	★
41	▼ -5	36	Pensioenfonds ING	2,4	2,1	3,3	2,2	1,6	2,3	★
41	= 0	41	Shell Pensioenfonds	2,1	2,1	2,9	2,2	1,8	2,0	★
44	▲ 3	47	Pensioenfonds Medewerkers Apotheken (PMA)	1,2	1,7	2,3	2,5	1,2	1,9	★
45	▲ 4	49	Algemeen pensioenfonds KLM	1,1	1,5	2,3	1,7	0,8	2,3	☆
46	▲ 1	47	Pensioenfonds KLM Cabinepersoneel	1,2	1,2	2,3	1,7	0,6	1,7	☆
46	-	-	Bpf MITT **	*	1,2	0,4	1,2	1,3	1,7	☆
48	▼ -3	45	Pensioenfonds Meubel **	1,6	1,0	0,4	1,7	0,6	2,3	☆
49	▼ -6	43	Bakkers Pensioenfonds **	1,7	0,9	0,4	1,2	0,9	1,3	☆
50	= 0	50	Pensioenfonds Vliegend Personeel KLM	0,3	0,6	1,3	1,0	0,2	1,0	☆

* New
** Non respondent

Appendix II: **Methodology**

Over the years, the benchmark has developed significantly and it has become a relevant tool to measure responsible investment by pension funds in the Netherlands. The study is impartial and its most important aim is to, together with the Dutch pension funds, enhance the sustainability performance of individual pension funds, but also sector-wide.

Underlying presumptions

The most important underlying presumptions in this benchmark are:

I. The scope of the benchmark is determined by selecting the 50 largest Dutch pension funds derived from the figures of the Dutch Central Bank.

II. The assets that are included in this benchmark are the assets of Dutch pension funds, independent of where these are being managed.

III. The implementation of the responsible investment policy is considered to be the most important element, because here the actual impact is being made. Therefore, this receives 50% of the total score. Governance, Policy and Accountability amount for the remaining 50%.

IV. The topic 'Governance' is to be considered from the viewpoint of the management of the pension fund, not from the asset manager's perspective.

V. The total score for 'Implementation' is dependent on the different scores of the asset classes (public listed equity; corporate bonds; government bonds; real estate; private equity and alternative investments). The weight of the asset classes in the determination of the implementation score is dependent on the asset allocation.
Other assets, such as cash, interest swaps and currency overlays, are not included in this benchmark study.

VI. Within each asset class it is determined which ESG instruments are (reasonably) implementable. Each question receives an equal weighting.

VII. VBDO is indifferent if an investor takes an active or passive and direct or indirect investment approach and assesses what responsible investment strategies are being applied.

The abovementioned underlying presumptions are based on VBDO's consultation with the pension funds participating in this study. This consultation is based upon an annual physical meeting with a selection of participating pension funds.
Key in this meeting are the quantified survey results.

In numbers:	
50	Dutch Pension funds
4	Categories
53	Questions
5	Max. total score
94%	Response rate

Figure 4.1 Benchmark responsible investment by pension funds in numbers.

The benchmark

The VBDO Benchmark 'Responsible Investment by Pension Funds in the Netherlands 2018' compares the responsible investment performance of the 50 largest pension funds in the Netherlands based on data of 2017. VBDO assesses responsible investment through detailed profiles of each pension fund. This year, the methodology has remained the same compared to last year. One question regarding ESG criteria in infrastructure, has been added as a result of the above-mentioned consultation with pension funds.

Approach

The benchmark is set up to stimulate pension funds to inform themselves about their current status of responsible investment. The research process consists of two phases:

I. VBDO executes a preliminary analysis, which is shared with the pension fund after completion.
II. In the second phase, the pension fund comments on the preliminary analysis and substantiates it with evidence which VBDO interprets, integrates, further elaborates upon and finalises.

Setup

The questionnaire is composed of four themes:

I. Governance

The first theme regards the governance of pension funds on responsible investment, including the role of the board, the frequency of board meetings about responsible investment, targets set to asset managers and the consulting of participants.

II. Policy

This theme focuses on the responsible investment policy in place. Its applicability to the entire portfolio, its depth, and its quality are surveyed.

III.Implementation

The implementation of the responsible investment policy applies to six different asset classes. Figure 4.2 shows the asset classes with the corresponding responsible investment strategies that are covered in the study. VBDO believes that the asset owners should take responsibility for the investments made on their behalf. Therefore, all implementation questions include the whole investment chain from pension fund to asset manager or fund of a fund manager. They are directed towards the state of implemented strategies in 2017.

IV.Accountability

This section discusses transparency about responsible investment policies, strategies, results and reports.

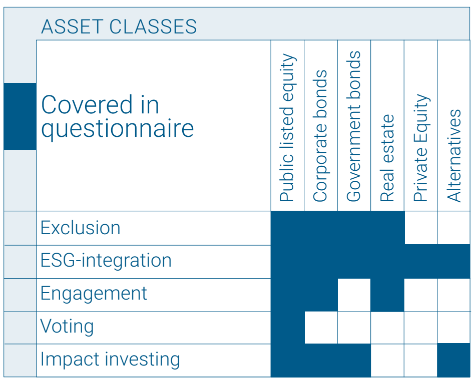

Figure 4.2 Responsible investment instruments and the different asset classes included in the benchmark.

Scoring model

The categories are weighted differently. Governance, policy, and accountability each account for 16.7%, and implementation for 50% which makes a 100% in total. The weighted percentage for implementation is 50% because this theme determines the final output and quality of the responsible investment practices of a pension fund. In the governance and policy category, all questions are weighted equally.

The final score for implementation is determined by multiplying the score of each asset class by the percentage of the portfolio invested in this asset class. All question are weighted equally within asset classes. In the accountability category, 5 sub categories are distinguished. Publication of the responsible investment policy, list of investments, active transparency and the responsible investment report each account for 16.7% of the accountability score. Transparency on implementation accounts for the other 33.3% and is assessed per responsible investment instrument. Figure 4.3 gives an overview of the scoring model.

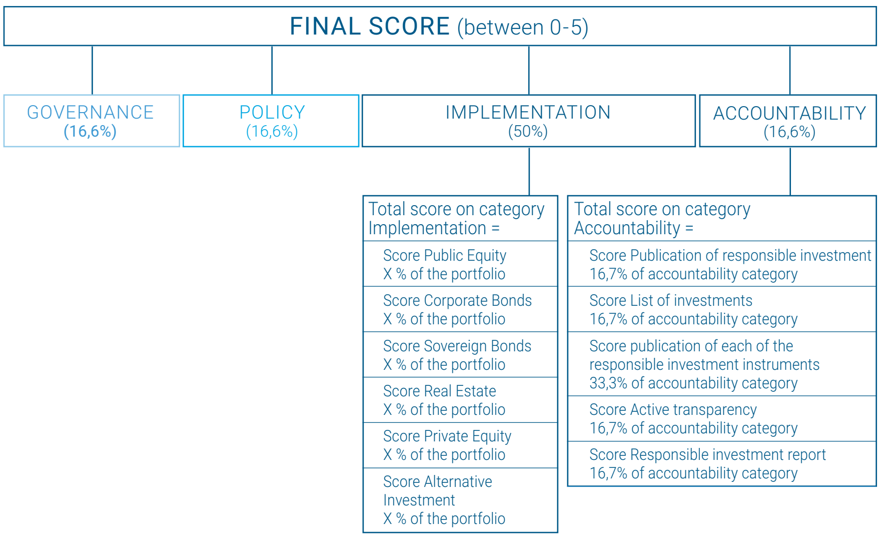

Figure 4.3 Overview of the scoring model.

Star ranking

This is the second year VBDO uses the star ranking based on a 0 - 5 star range instead of only a 1-50 ranking in numbers. In consultation with the sector it was decided that the use of a star ranking shows a more realistic depiction of the sustainability performance of pension funds.

The star ranking is based on the total score and on the scores of the individual categories of the pension fund; governance, policy, implementation and accountability. However, next to this, VBDO aspires to also base the star ranking on additional minimum standards. The bold faced standards mentioned below are minimum standards to the star rankings. This year, only the bold faced standards were decisive in awarding the stars. The other standards will be gradually applied over the coming years.

The following scores and minimum standards determine the number of stars awarded:

5 stars ★★★★★

Minimum standards:

- **A score of at least 4.5 on all categories (governance, policy, implementation, accountability)**
- Demonstrably takes a leadership position in the sector, by being a pioneer in one or more areas (such as impact investing)
- Responsible investment instruments are widely implemented. All responsible investment instruments are in effect for every single asset class
- Considers sustainability targets as an important way to measure impact and take responsibility. Sustainability targets are set for both asset managers and the fund itself
- All below mentioned standards are in place

4 stars ★★★★

Minimum standards:

- **A total score of at least 4.0**
- **A score of at least 3.5 on all categories (governance, policy, implementation, accountability)**
- There is a long-term vision in place and related sustainability targets are set
- ESG themes are translated into at least five responsible investment instruments (exclusion, ESG-integration, voting, engagement, impact investing)
- Impact is being measured and results and further steps taken are reported
- There is transparency regarding the responsible investment policy, investments, and the responsible investment instruments

3 stars ★★★

Minimum standards:

- **A total score of 3.5 up to and including 3.9**
- **A score of at least 2.5 on all categories (governance, policy, implementation, accountability)**
- ESG themes are translated into at least five responsible investment instruments (exclusion, ESG-integration, voting, engagement, impact investing)
- The responsible investment policy is implemented into all asset classes
- There is transparency regarding all responsible investment instruments

2 stars ★★

Minimum standards:

- **A total score of 2.5 up to and including 3.4**
- **A score of at least 2.0 on all categories (governance, policy, implementation, accountability)**
- A responsible investment policy is in effect and is discussed more than once a year at a senior management board meeting
- If applicable, the responsible investment policy is implemented into all asset classes

1 star ★

Minimum standards:

- **A total score of 1.5 up to and including 2.4**
- **A score of at least 1.0 on all categories (governance, policy, implementation, accountability)**
- A responsible investment policy is in effect

0 stars ☆

- **A total score below below 1.5**
- No responsible investment policy is in place, or:
- If there is a responsible investment policy in place, this policy does not cover all asset classes and this policy is not implemented thoroughly
- The score on implementation is the lowest compared to the other categories (< 1.0)

Appendix III: **Responsible investment strategies and asset classes**

Responsible investment strategies

Based on reviews of implementation practices by investors worldwide and its own vision on responsible investment, VBDO has identified a range of responsible investment instruments that are applicable to one or more asset classes:

- Exclusion

Certain products, processes or behaviour of some companies and governments, are at such odds with international agreements and treaties that they should be excluded from the investment portfolio. Merely taking general issues such as human rights violations into consideration offers insufficient means of judgment for the exclusion of specific companies. It is important to specify these issues and use well defined Environment, Social and Governance (ESG) criteria or international guidelines, in order to exclude companies and governments.

While some investors do take more than one criterion into account for the exclusion of companies from their investment portfolio, their list of excluded companies only shows (controversial) weapon producers, which raises questions about the use of ESG criteria. Especially because in January 2013 the legal ban of investments in cluster munitions came into force in the Netherlands. Concerning the exclusion of government bonds, pension funds can exclude countries based on official sanction lists of, for example, the EU and UN or based on other criteria. In the opinion of VBDO responsible investment should be a practice that goes beyond merely following legal obligation. Therefore, the pension funds can only receive points for exclusion criteria that go further than merely excluding on the basis of cluster munition.

- ESG integration

Even when the excluded companies are left out, large differences in terms of corporate responsibility sometimes remain between companies in which institutional investors invest. Where one company may only abide by the current environmental and social laws of the country in which it operates, the other may pursue high social and environmental standards in every country in which it is active. Institutional investors should consider this in developing their investment policy and should give preference to companies that perform well in relation to corporate responsibility.

VBDO defines ESG integration as the process by which ESG criteria are incorporated into the investment process. This involves more than screening the portfolios against exclusion criteria, but does not mean that an investor merely selects the best-in-class companies. ESG integration can go one step further by identifying and weighing ESG criteria, which may have a significant impact on the risk return profile of a portfolio. Therefore, VBDO distinguishes between investors making ESG information available to the portfolio manager on the one hand and investors systematically incorporating ESG criteria into each investment decision on the other hand. The latter is rated higher because this truly meets the idea behind ESG integration. An example of ESG integration is positive selection, this is defined as choosing the best performing organisation out of a group of corresponding organisations (sector, industry, class) with the use of ESG criteria. In this case, ESG criteria do not guide the investment decision process, but form the basis for selecting companies that perform above average on ESG issues. Integration of ESG criteria in the investment selection can be applied to all of the selected asset classes in this research. Regarding publicly listed equity and bonds, the assessment in this benchmark takes into account both the extent and the volume of ESG integration.

- Engagement

Pension funds can actively exert influence on companies in which investments are made by entering into dialogue with them. If the policy and behaviour of a company are at odds with the responsible investment policy, pension funds should to some extent use their influence to alter the conduct of companies in which investments are made. Institutional investors that have formulated an engagement policy, actively seek dialogue with companies outside the shareholder meeting. In order to obtain optimal engagement results, it is essential to evaluate and monitor the engagement activities and take further steps based on the outcome of the engagement activities. Engagement can be used to publicly listed equity as well as corporate bonds and real estate funds.

- Voting

Institutional investors can actively exert influence on companies in which they invest by voting during shareholder meetings. Many institutional investors vote at shareholder meetings, but their voting policy is limited to subjects regarding corporate governance. This might push companies towards a better sustainability policy, but that is in itself not enough. A clearly defined voting policy is required, one that explicitly emphasizes social and environmental issues. By pro-actively introducing or supporting resolutions about sustainable development and corporate social responsibility, companies can be pushed towards improvement and corrective action. Voting is examined only at the asset class publicly listed equity.

- Impact investing

Impact investing implies active investments that are made in companies or projects, which lead in terms of sustainability or clearly offer added value for sustainable development. Examples are investments in sustainable energy sources, innovative clean technology, affordable medicine against tropical diseases, microcredit and sustainable forestry. Impact investing might look like positive selection, because it may be using the same positive ESG criteria and can be done by investing in specially constructed funds, but it is not a best in class approach. Rather, investors choose a specific theme or development and search for companies or projects that contribute to this development and thus create added value for society in a way that can hardly be compared with mainstream industry or solutions. VBDO values the measurement and evaluation of the actual environmental and social impact of the investments. The instrument is applicable to publicly listed equity, corporate and government bonds, real estate, and alternative investments which include private equity.

Asset Classes

- Publicly listed equity

The public equities market consists of the publicly traded stocks of large corporations. The risks and opportunities connected to ESG issues are important for the analysis and adjustments of an equity portfolio. Both exclusion and selection of companies within the portfolio, as well as voting and engagement gives the investor many ways to integrate ESG issues into its investment decisions. Emerging markets deserve special attention from investors, since these are increasingly reported as interesting opportunities because of their economic growth. Due to the growing demographic and resource challenges, and the potential dangers for the environment, a more sustainable approach to economic development is crucial for emerging markets. In many sectors economic development shows that these countries are already responding to the abovementioned challenges (think of, for example, the leading role in solar power of China). Nevertheless, extracting the relevant ESG data on emerging market companies can require a large amount of research. It is also possible to take ESG criteria into account with passive investments, by following a sustainable index or by using an engagement overlay.

- Corporate (including covered) bonds

For corporate bonds responsible investment activities can be similar as for equities, however corporate bonds do not have voting rights and bring a fixed return. This reduces the financial risk, but also offers fewer opportunities to take advantage of high returns and to influence the policies of a company. Because bondholders lack the voting power shareholders have, most ESG integration activity has been in equities. But with growing client demand, bond managers are working to integrate ESG factors in fixed-income portfolios.

- Government / sovereign bonds

Like corporate bonds, government bonds (together often referred to as fixed-income) are generally regarded as one of the safer, more conservative investment opportunities. They are issued to fund public services, goods or infrastructure. The first association about responsible investment and this asset class may often be exclusion of countries with dictatorial regimes, because of their human rights violations. This is a

clear example of the results of an ESG risk analysis.
ESG rating agencies increasingly offer products to screen bonds portfolios on corporate governance regulatory practices, environmental policies, respect for human rights and international agreements. Investors can also seek those government bonds that support the creation of public goods, such as needed infrastructural improvements, support for schools, or the development of sustainable energy sources and purchase government debt targeted to a specific activity.

- Real estate

Real estate investments encompass a wide range of products, including home ownership for individuals, direct investments in rental properties and office and commercial space for institutional investors, publicly traded equities of real estate investment trusts, and fixed-income securities based on home-loans or other mortgages. This assessment is limited to direct investments in buildings and indirect investments via real estate funds. Investors could screen their portfolio by developing ESG criteria for the construction of new buildings, their locations and the maintenance of existing buildings, machines and other facilities within buildings, such as environmental efficiency, sustainable construction and materials and fair labour practices. For real estate (investment) that is managed externally, the selection of fund managers based on experience with and the implementation of ESG is an important tool. Additionally, the managers of real estate funds can be engaged to improve their social and environmental performance.

- Private equity

With regard to private equity, an institutional investor can stimulate innovative and sustainable companies because it can directly influence management, encourage entrepreneurs to focus on developing business with high-impact social and/or environmental missions. This can be done especially in regions and communities that are underserved, and promote creation of local business and jobs. With this in mind, integrating the responsible investment policies in the selection process can be an important tool for institutional investors.

- Alternative investments

Depending on the asset allocation and definitions of an investor, alternative investments can include many kinds of assets, while at the same time experiences with and strategies for responsible investments are in their infancy. Also because the investments are a small part of total investments, this research limits this asset class to hedge funds, infrastructure, commodities and impact investments. Information provided on other asset classes will not be taken into account. The following opportunities were derived from literature:

I. Although hedge funds are often handled as a separate asset class, the underlying assets are generally publicly listed securities (stocks and bonds) and their derivative products. Thus, investors could consider an ESG analysis of underlying assets and theoretically use the same tool for ESG management as for public equity and fixed income. Likewise, integrating the responsible investment policies in the selection process can be an important tool.

II. Infrastructure is widely considered to have a positive social impact. Infrastructure investors should take into account a broad range of material ESG issues that these investments might face over the assets' lifetime. Examples of ESG issues could involve; biodiversity impact, labour-, health and safety standards, resource scarcity and degradation, extreme weather events and supply chain sustainability. It is therefore relevant to monitor how ESG is integrated in infrastructure investments.

III. Regarding commodities, investors could direct capital to commodities with better ESG profiles and consider the source (region) of the commodity. As there are few ways to foster positive ESG changes, investors may advocate change on a broader level within commodities exchanges. Also integrating the responsible investment policies in the selection process of commodity investments or asset managers can be an important tool for this category.

About VBDO

The Dutch Association of Investors for Sustainable Development (VBDO) is a not for profit multi-stakeholder organisation. Our mission is to make capital markets more sustainable. Members include insurance companies, banks, pension funds, asset managers, NGOs, consultancies, trade unions, and individual investors. VBDO is the Dutch member of the international network of sustainable investment fora. VBDO's activities target both the financial sector (investors) and the real economy (investees) and can be summarised as follows:

Engagement

Since more than 20 years ago, the core activity of VBDO has been engagement with 40+ Dutch companies listed on the stock market. VBDO visits the annual shareholders' meetings of these companies, asking specific questions and voting on environmental, social and governance (ESG) themes. The aim of this engagement is to promote sustainable practices and to track progress towards the companies becoming fully sustainable, thereby providing more opportunities for sustainable investments.

Thought leadership

VBDO initiates knowledge building and sharing of ESG-related issues in a pre-competitive market phase. Recent examples of this include: three seminars on climate change related risks for investors; the development of guidelines on taking Natural Capital into account when choosing investments and organizing round tables about implementing human rights in business and investor practices. Also, we regularly give trainings on responsible investment both to investors as well as NGOs.

Benchmarks

Benchmarks are an effective instrument to drive sustainability improvements by harnessing the competitive forces of the market. They create a race to the top by providing comparative insight and identifying frontrunners, thus stimulating sector wide learning and sharing of good practices. VBDO has extensive experience in developing and conducting benchmarking studies. VBDO has conducted annual benchmarking exercises, for example, since 2007 about responsible investment by Dutch pensions funds, and since 2012 responsible investment by Dutch insurance companies.

This has proven to be an effective tool in raising awareness about responsible investment and stimulating the sustainability performance of pension funds and insurance companies. VBDO is one of the founding partners of the Corporate Human Rights Benchmark, which ranks the 500 largest companies worldwide on their human rights performance, and makes the information publicly available, in order to drive improvements. VBDO's Tax Transparency Benchmark ranks 64 listed multinationals on the transparency of their responsible tax policy and its implementation.

For more information about VBDO, please visit our website: http://www.vbdo.nl/en/

"We need to continue constructive dialogue between pension funds, asset managers, academics, NGOs and financial regulators"

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