A Case For: Sustainable Climate Bond Strategy

State Street Global Advisors has developed a breakthrough climate bond strategy. Our climate-aware investment process enables you to immediately improve your portfolio's carbon profile and reduce climate risk, while maintaining target returns.

Key Features of the Sustainable Climate Bond Strategy

- **Targets Paris-aligned Reductions in Carbon Emissions and Fossil Fuel Exposure.** Avoids exposure to companies associated with high ESG controversies and commonly screened environmental, social and governance (ESG) issues (e.g. controversial weapons and UNGC violations).
- **Fund the Transition.** Increases exposure to green bonds, adapting companies and bond issuers investing in the solutions needed to achieve net zero by 2050.
- **Keep the Returns.** A systematic and transparent approach that delivers cost effective, diversified corporate bond exposure comparable to standard market-weighted corporate bond indices. Minimises active exposures that are not expected to outperform, such as currency, country, sector and industry exposure.

The above targets are estimates based on certain assumptions and analysis made by State Street Global Advisors. There is no guarantee that the estimates will be achieved.

The Slow-Burning Crisis

The scientific evidence for man-made climate change is incontrovertible. The last seven years were the hottest on record.

Recent years have been marked by disaster caused by more frequent and extreme weather events brought about by climate change.

Warming has also led to unprecedented melting of ice and snow at the north and south poles. Sea level rise will mean coastal communities are much more exposed to flooding and extreme storms, leading many to migrate inland, putting pressure on infrastructure and resources. And with greater carbon dioxide in the oceans comes ocean acidification, degradation of marine ecosystems and reduction in marine biodiversity.

Research suggests that 'tipping points' such as the melting of huge ice sheets or the loss of the Amazon rainforest are much more likely to occur than previously thought.[1]

Tackling the Climate Threat

In recognition of the severity of climate risks, countries have committed to reducing carbon emissions in line with the 2015 Paris Agreement of limiting global warming to 2° Celsius or less over the 21st century. The European Union, UK and several other countries have committed to be carbon neutral by 2050. In advance of regulation, many companies are proactively taking steps to reduce their carbon footprints and disclose their exposure to climate risks. Below are three trends in the global response to climate change that investors will have to address.

1 The Seismic Energy Transition

Recent years have seen a sustained shift in energy use away from fossil fuels and towards renewable energy, driven largely by acknowledgement of the impact of fossil fuel pollution and the need to reduce carbon emissions. The falling costs of solar and wind energy has further increased their attractiveness compared to fossil fuels. The COVID-19 crisis has acted to hasten the decline in fossil fuel demand and by the time the global economy recovers, it is possible that most of the *growth* in energy demand may be met by renewable energy sources.[2] The transition to the low-carbon economy will require companies in all sectors to decrease their carbon footprint.

2 Regulatory Tipping Point

In order to meet the Paris Agreement goals and reach net zero carbon emissions by 2050, a growing number of countries and local jurisdictions are making climate disclosure mandatory across the investment chain — from companies, to financial services firms, to end-investors.

The European Parliament approved the EU Taxonomy Regulation, which will be fundamental to the realisation of the European Green Deal, which aims to boost private sector investment in green and sustainable projects. The European Insurance and Occupational Pensions Authority has stated that pension funds and insurers can play a key role in the transition towards a low carbon economy and that they should actively incorporate climate change risks in their own risk management frameworks.

The European Commission is also seeking to integrate sustainability risks and sustainability factors into Undertakings for the Collective Investment in Transferable Securities (UCITS) schemes, the Alternative Investment Fund Managers Directive (AIFMD) and the Markets in Financial Instruments Directive (MiFID). This, in turn, will drive investment in more sustainable projects and activities.

3 Capital Allocations

High-quality disclosures about how organisations and assets will both impact and be impacted by environmental change is encouraging better-informed pricing and capital allocation.

Many of the world's largest pension schemes expect to increase their allocations to climate-related index funds over the coming years.

A potential driver for the increased adoption of climate considerations in investment portfolios is the perceived robustness of sustainable investment strategies.

Portfolio Impact

Investors are recognising that climate risks are financial risks. Climate change is the highest priority among UN PRI[3] signatories, representing over 5,000 signatories and US $121 trillion of assets under management.[4] For investors, climate change and its impact on asset valuations are becoming important criteria for investment decisions. The risks from climate change can be split into four broad categories:

Figure 1 **Climate Change Risks**

Systemic Risk to financial markets as they seek to digest impact on economic growth, societal disruption and energy-mix change	**Country Risk** to petro-states that fail to reinvent themselves in time
Corporate Risk in sectors across the world, from drilling to diesel engines and from transport to banks	**Asset Value at Risk** as investors digest vast amounts of potentially stranded fossil fuel assets Fossil fuel and related sectors comprise about a quarter of all equity and debt markets

Companies face a multitude of climate-related risks, including supply chain disruptions and shortage of raw materials, falling demand for products and services, and carbon taxes and other regulations.

Accepting that climate risks must be addressed, what should an optimal climate-aware approach look like? Limiting carbon emissions is clearly necessary but insufficient on its own.

Asset owners must also build long-term resiliency into their portfolios. Resiliency is critical in a world that will be shaped by climate change for decades, perhaps centuries, to come.

A 'Mitigation and Adaptation' Approach

We believe in an investment approach that incorporates both **mitigation** of greenhouse gas emissions, and **adaptation** to the future impacts of climate change. These are complementary approaches to reducing climate risks and correspond with asset owners' need to balance short- and long-term risks and opportunities.

- Mitigation aims to reduce the flow of heat-trapping greenhouse gases into the atmosphere and increase exposure to new energy and green companies.

- Adaptation aims to increases exposure to companies working proactively to minimise their exposure to the actual or expected physical, economic and regulatory impacts of climate change and the transition to a low-carbon economy.

Introducing the Sustainable Climate Bond Strategy

Imagine if you could drastically improve your portfolio's carbon profile and reduce climate risk, all while keeping risk and return characteristics broadly in place.

This is the rationale behind the State Street Sustainable Climate Bond Strategy, which adopt a systematic mitigation and adaptation approach that targets Paris-aligned reductions in carbon emissions and fossil fuel exposure and reallocates capital towards companies benefiting from low-carbon technologies.

The Strategy aims to achieve the following objectives in relation to the following five climate categories utilised in the portfolio construction process:

Figure 2 **Sustainable Climate Bond Strategy: Key Metrics and Targets**

	Mitigation				+ Adaptation	
	Current and Future Risk Exposure				Resiliency	Opportunities
Objectives	**Minimise** Carbon Emissions	**Minimise** Fossil Fuel Reserves	**Minimise** Brown Revenues	**Minimise** ESG Risks	**Build** Resilient Portfolio	**Maximise** Green Bonds & Green Proceeds
Metrics	Carbon Intensity Direct + First Tier Indirect Emissions	Total GHG emissions from fossil fuel reserves in million tonnes CO_2	Revenues from extractives activities	Norms-based and controversial product involvement screening	Adaptation Score on climate change preparedness	Certified Green Bonds
Units	Metric tons CO_2e/$m revenues	Metric tons	%	—	Scaled range 0–1	—
Definition	Greenhouse gas emissions over which the company has direct control or derives from suppliers, divided by revenue	Total embedded CO_2 emissions for the company in a financial year	Percentage of revenues from brown sectors and extractive sectors with high embedded carbon emissions	Adherence to international norms in relation to ecological protection, human rights, labour standards, anti-corruption, controversial weapons and tobacco	Position on Climate Change Greenhouse Gas Reduction Action Plans	Bonds which qualify as green according to the Climate Bonds Initiative Taxonomy
Target	↓ **≥70%***	↓ **≥95%**	↓ **≥95%**	↓ **100%**	↑ **0.167****	↑ **≥2.5x**

Source: State Street Global Advisors, as of September 30, 2022. The information contained above is for illustrative purposes only.
*The framework applies "zeros" for carbon intensity, brown revenue and fossil fuel reserves metrics associated for bonds identified as green bonds. **0.167 is the 'Adaptation Score' below which a company will be ineligible for inclusion. The Adaptation Score scale is 0 (lowest) to 1 (highest). The above targets are estimates based on certain assumptions and analysis made by State Street Global Advisors. There is no guarantee that the estimates will be achieved.

Our approach follows a four-step process:

1 Start with the Right Universe

Clients can select any standard investment grade or high yield credit or aggregate benchmark which include corporate bonds. For each exposure, we first incorporate a set of screens that are aligned with our climate and ESG objectives. If a client has their own climate metrics they would like included then we can potentially accommodate this in a separately managed account.

We utilise three sets of exclusions based on product involvement and prescriptive regulatory screens and updated on a quarterly basis:

Figure 3 **Exclusionary Screening Criteria**

Climate Related Exclusions	**Carbon Intensity**
	Fossil Fuel Reserves
	Brown Revenues
ESG Risks and Reputation Risk Related	**Violations of UN Global Compact Principles** Screens companies for violations of commonly accepted international norms related to human rights, labor rights, the environment and business ethics.
	Controversial Weapons/Armaments Screen companies involved in production and distribution of weapons that have disproportionate and indiscriminate impact on civilians
	Severe ESG Controversies
	R-Factor Laggards Avoids companies with poor industry-specific ESG risks and opportunities.
Based on Prescriptive Regulatory Screen	**Swedish Ethical Council** Focused on influencing companies to operate in a more sustainable way by acting to bring about positive change in companies associated with violations of international conventions on environment and human rights
Controversial Product Involvement	**Arctic Oil & Gas** **Oil Sands** **Controversial Weapons** **Thermal Coal** **Tobacco**

Our product involvement framework has two core criteria — drivers of product involvement and scope of resulting restricted list:

Figure 4 **Drivers of Product Involvement**

Three Drivers of Product Involvement	Description	Focused Involvement	Broad Involvement
1. Revenue	*What percent of a company's total revenue is derived from this industry, product, or topic?*	Higher revenue threshold	Lower revenue threshold
2. Activities	*What part of the value chain is the company involved in?*	Direct involvement inthe product	Direct and/ or indirect involvement in the product
3. Significant Ownership	*Is the company an owner of, or owned by, another company with involvement in this issue?*	Companies whose primary business activity is the product in question, or who own a significant portion of a company with involvement	Companies with any ownership relationship to the product in question are screened

← **Scope** →

Fewer names screened — More names screened

The metrics used in a particular screen depend on the availability from our data providers. For example, some weapons only have revenue metrics, others only activity metrics.

We follow a well-defined methodology that leverages best-in-class available data from multiple data providers where accessible to us.

2 Source the Best Data

All investment strategies rely on relevant and high-quality data and climate strategies are no different. At State Street Global Advisors, we employ an open architecture to source the best-available data. We have selected the following data providers for the Sustainable Climate Bond Strategy:

- **Trucost** for carbon emission intensity, fossil fuel reserves and brown revenues
- **Climate Bonds Initiative** for green bonds & climate-aligned issuers
- **ISS ESG** for adaptation score

- **Sustainalytics and MSCI** for product and controversy involvement
- **R-Factor™** for ESG rating based on the SASB ESG risk materiality framework

3 Design for Optimal Outcomes and Balance for Risk-Adjusted Return

We utilise a mitigation and adaptation framework to rebalance the portfolio towards companies that will aim to achieve our stated objectives:

Figure 5 **Designed for Maximum Impact**

↓	**Reduce Exposure** to companies with worse climate profiles. Eliminate highly polluting sectors.
↑	**Increase Exposure** to green bonds which fund projects that have positive environmental and/or climate benefits.
↑	**Increase Resiliency** by targeting companies that are positioned to benefit from the transition to the coming low-carbon economy.

We then balance the portfolio to target the highest expected risk-adjusted return, given the desired constraints.

We model the portfolio based on the following specifications:

- 70% or greater reduction in GHG emissions
- 95% or greater reduction in companies involved in brown sectors or that have fossil fuel reserves
- 100% exclusion of companies that violate ethical principles relating to corruption, human rights, labour standards, serious controversies, controversial weapons and tobacco
- 0.167 "Adaptation Score", below which a company will be ineligible for inclusion in a portfolio[5]
- 2.5x or greater increase in green bonds (recognised as green according to the green bond standards and taxonomy defined by the Climate Bonds Initiative)

4 Maximize Value with Indexed Offer

The portfolio is implemented using an indexed approach to deliver a consistent, cost-efficient and diversified investment exposure. This approach is built around stratified sampling which State Street Global Advisors pioneered. With about ten thousand issues in the broad corporate bond market, buying every bond is not a cost-effective approach for replication.

Skilled sampling can replicate the broad risk profile of the relevant corporate index efficiently and effectively, with a fewer but still highly diversified set of holdings.

In addition, we employ sophisticated indexing techniques focussed on minimising costs and tightly controlling systematic risks, while also adding value. Our value-add indexing approach is underpinned by minimising fund turnover relative to that of the index, effective trading and execution, harnessing the 'new issue premium' and a relative value (RV) security selection process.

Figure 6 **Euro Corporate Bond Strategy Performance**

	Euro Corporate Bond Strategy Performance (Gross of Fees)	Euro Corporate Bond Strategy Performance (Net of Fees)	Benchmark
1 Month (%)	-3.36	-3.38	-3.32
3 Month (%)	-3.11	-3.18	-3.06
6 Month (%)	-10.33	-10.46	-10.12
YTD	-14.77	-14.96	-14.58
1 Year (%)	-15.22	-15.47	-15.14
Since Inception*	-14.51	-14.87	-14.47

*Inception Date: May 2021.
Source: State Street Global Advisors, as of September 30, 2022. Used with permission. All other portfolio data provided by State Street Global Advisors. The performance shown is of a composite consisting of all discretionary accounts using this investment strategy. The above information is considered supplemental to the GIPS presentation for this Composite, which can be found in the Appendix or was previously presented. A GIPS presentation is also available upon request.
Past performance is not a reliable indicator of future performance. Performance returns for periods of less than one year are not annualized. The performance figures contained herein are provided on a gross and net of fees basis. Gross of fees do not reflect and net of fees reflect the deduction of advisory or other fees which could reduce the return. Some members of this composite may accrue administration fees. The performance includes the reinvestment of dividends and other corporate earnings and is calculated in EUR. Index returns are unmanaged and do not reflect the deduction of any fees or expenses. Index returns reflect all items of income, gain and loss and the reinvestment of dividends and other income as applicable. The calculation method for value added returns may show rounding differences. The performance shown is of a composite consisting of all discretionary accounts using this investment strategy. The above information is considered supplemental to the GIPS presentation for this Composite.
Benchmark: Bloomberg-Euro Aggregate Corporates Index.

Figure 7 **US Corporate Bond Strategy Performance**

	US Corporate Bond Strategy Performance (Gross of Fees)	US Corporate Bond Strategy Performance (Net of Fees)	Benchmark
1 Month (%)	-5.25	-5.28	-5.26
3 Month (%)	-5.11	-5.19	-5.06
6 Month (%)	-11.85	-11.98	-11.95
YTD	-18.42	-18.60	-18.72
1 Year (%)	-18.16	-18.41	-18.53
Since Inception*	-15.96	-16.31	-16.27

*Inception Date: May 2021.
Source: State Street Global Advisors, as of September 30, 2022. Used with permission. All other portfolio data provided by State Street Global Advisors. The performance shown is of a composite consisting of all discretionary accounts using this investment strategy. The above information is considered supplemental to the GIPS presentation for this Composite, which can be found in the Appendix or was previously presented. A GIPS presentation is also available upon request. Past performance is not a reliable indicator of future performance. Performance returns for periods of less than one year are not annualized. The performance figures contained herein are provided on a gross and net of fees basis. Gross of fees do not reflect and net of fees reflect the deduction of advisory or other fees which could reduce the return. Some members of this composite may accrue administration fees. The performance includes the reinvestment of dividends and other corporate earnings and is calculated in US dollars. Index returns are unmanaged and do not reflect the deduction of any fees or expenses. Index returns reflect all items of income, gain and loss and the reinvestment of dividends and other income as applicable. The calculation method for value added returns may show rounding differences. The performance shown is of a composite consisting of all discretionary accounts using this investment strategy. The above information is considered supplemental to the GIPS presentation for this Composite.
Benchmark: Bloomberg US Credit Corporate Index

As an example, on average for a Euro Corporate Bond strategy, we are able to achieve a carbon intensity reduction of more than 300% versus the Bloomberg Euro Corporate Bond Index.[6] We are also able to reduce the portfolio's fossil fuel reserves and brown revenues[7] by 95–100%, and we bring the green and climate-aligned bond concentration up from 7.49% (Bloomberg Euro Corporate Bond Index) to 21.34% (Strategy).[8]

Paris Alignment

The Paris Agreement is an international accord that aims to limit the rise in global average temperatures to below 2°C above pre-industrial levels by the end of this century, and to pursue efforts to limit it to 1.5°C. While there is no 'one-dimension-fits-all' portfolio solution "Paris-aligned" investment means implementing an investment strategy that is consistent with the global goal of net zero emissions by 2050. Global net zero emissions by 2050 represents a no-or low-overshoot scenario associated with a >66% probability of limiting temperature increase to 1.5°C and is therefore recommended as the appropriate precautionary approach to achieving the 1.5°C goal of the Paris Agreement (IPCC, 2018).

The objective for the Sustainable Climate Bond Strategy is to maximise efforts that achieve decarbonisation in the real economy and increase investments in the solutions needed to achieve net zero. When applying this to investments, this requires the implementation of a comprehensive framework with concrete targets set at the portfolio level, as shown on the previous page.

These top-down and bottom-up reference targets are an important means to set direction and appropriate ambition for an investment strategy and serve as an ongoing reference point to monitor whether that strategy is achieving the expected outcomes. Issuers that do not meet the criteria are typically excluded from the eligible investment universe rather than underweighted. Our Sustainable Climate Bond Strategy are also reinforced through our company engagements to influence issuers and their policies in order to bring companies and their supply chains towards greater alignment with the Paris Agreement goals.

Target: Net Zero

As a proud signatory of the Net Zero Asset Managers initiative, we believe that there is an urgent need to accelerate the transition towards global net zero emissions. State Street Global Advisors has established net zero targets, both in interim for 2030 and ultimately by 2050. In setting these targets we are playing our part in helping to deliver the goals of the Paris Agreement and ensuring a just transition to the low-carbon economy.

Who We Are

State Street Global Advisors' ESG experience covers portfolio management, investment research, proxy voting and engagement, as well as valuable relationships with third-party research providers. While most clients' custom ESG criteria require a separate account, State Street Global Advisors has created pooled funds that address many of the more common client approaches. Pooled vehicles may offer advantages such as economies of scale, lower fees and lower administrative costs.

We apply a multi-dimensional approach to our ESG investing solutions. Through our extensive ESG data and research, we can help develop and implement solutions for our clients that align policy, principles and values, yet seek maximum performance or minimum tracking error within the constraints.

1 Operationalising positive tipping points towards global sustainability', Lenton et al (2022).

2 'COVID-19 and Energy in the New World', State Street Global Advisors and Carbon Tracker Initiative (2020).

3 UN Principles for Responsible Investment.

4 UN PRI Quarterly Signatory Update as of June 2022, located at https://unpri.org/signatories/signatory-resources/quarterly-signatory-update. This is latest available at time of publication.

5 0.167 is the 'Adaptation Score' below which a company will be ineligible for inclusion. The Adaptation Score scale is 0 (lowest) to 1 (highest). The above targets are estimates based on certain assumptions and analysis made by State Street Global Advisors. There is no guarantee that the estimates will be achieved.

6 Data is measuring the weighted average carbon intensity (WACI), specifically, weighted average carbon emissions per $1 million in revenue.

7 Fossil fuel reserves are measured by the weighted average of embedded carbon, millions of tons. Brown revenues are measured by the percent of revenue at the corporation.

8 Green and climate aligned bond concentration is measured by weighted average market value (%). **Green Bonds & Climate Aligned Issuers:** State Street Global Advisors (SSGA) seeks to identify qualifying securities according to the Climate Bonds Initiative Taxonom y (CBI). For historical back testing, Green bonds are identified using Thomson Reuters Data and switched to CBI data when available. The Green Bond market aims to enable and develop the key role that debt market can play in funding projects that contribute to environmental sustainability. Even though some data providers propose a Green Bond label, there is no market consensus regarding the definition of Green bond. The International Capital Market Association proposed a set of guidelines with four components: 1. Use of proceeds, 2. Process for project evaluation and Selection, 3. Management of Proceeds 4. Reporting. On 17th June 2020, SSGA partnered with CBI and joined CBI's partners network. The use of a 3rd party to assess the suitability of the Green-labelled bond label give us more confident in the use of proceeds. Due to the fairly concentrated nature of the Green bond market, the Climate strategy includes also bonds that are labelled as "Climate-Aligned" Bonds. Climate-aligned bonds are bonds which CBI identify as financing assets and activities for climate change solutions. The climate-aligned bond universe is composed of: a) Unlabelled bonds from issuers that derive >95% of revenues from "green" business lines. Such issuers are defined as "fully aligned" issuers b) unlabelled bonds from issuers that derive 75–95% of revenues from "green" business lines. Such issuers are defined as "strongly-aligned" issuers c) labelled green bonds issued by green bond issuers. For more information on the CBI Taxonomy please visit: https://climatebonds.net/standard/taxonomy. The Sustainable Climate Corporate Bond Strategy identifies qualifying green bonds and climate aligned securities as financing projects needed to deliver a low carbon economy and gives GHG emissions screening criteria consistent with the 2-degree global warming target set by the COP 21 Paris Agreement. As such they are excluded all together from any filtering (with exception to the SSGA UNGC, Controversial Weapons and Swedish Ethical Council Screen which all securities must comply with) and are treated as a "stand-alone" allocation. Additionally, and following consultation with S&P Trucost, State Street Global Advisors replaces green bonds with "zeros" for carbon intensity, brown revenue and fossil fuel reserves metrics and this may cause an underestimate in the final weighted average volumes.

About State Street Global Advisors

For four decades, State Street Global Advisors has served the world's governments, institutions and financial advisors. With a rigorous, risk-aware approach built on research, analysis and market-tested experience, we build from a breadth of index and active strategies to create cost-effective solutions. As stewards, we help portfolio companies see that what is fair for people and sustainable for the planet can deliver long-term performance. And, as pioneers in index, ETF, and ESG investing, we are always inventing new ways to invest. As a result, we have become the world's fourth-largest asset manager* with US $3.26 trillion† under our care.

* Pensions & Investments Research Center, as of December 31, 2021.
† This figure is presented as of September 30, 2022 and includes approximately $55.12 billion USD of assets with respect to SPDR products for which State Street Global Advisors Funds Distributors, LLC (SSGA FD) acts solely as the marketing agent. SSGA FD and State Street Global Advisors are affiliated. Please note all AUM is unaudited.

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This document provides summary information regarding the Strategy. This document should be read in conjunction with the Strategy's Disclosure Document, which is available from SSGA. The Strategy Disclosure Document contains important information about the Strategy, including a description of a number of risks.

Not all products are available to all investors, please contact SSGA for further information regarding this strategy.

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