

# Sustainability Policy

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## Purpose

The Fourth Swedish National Pension Fund's (AP4's) Sustainability Policy lays out overarching guidelines and strategies for the asset management organisation's work on integrating sustainability aspects in the investment operations.

AP4 works according to the 1987 Brundtland commission's definition of sustainable development, as societal development that meets the needs of people today without jeopardising future generations' opportunities to meet their needs, and that this is a precondition for maintaining favourable and balanced economic development over time.

It is thus an investment belief for AP4 that taking sustainability issues into account in the asset management is a precondition for being able to conduct long-term successful asset management, as it contributes to a better risk-adjusted return over time. In such way AP4 helps safeguard current and future pensions at the same time that sustainable development and growth are promoted.

## Background

AP4's operations are grounded in the National Pension Funds Act (*Lagen (2000:192) om allmänna pensionsfonder*), which stipulates that the overarching mission of the First, Second, Third and Fourth AP Funds (the AP Funds) is to manage the fund assets in such way that they will be of the greatest possible benefit for insuring income-based retirement pensions, that is, generate the highest possible long-term return for the benefit of the insureds in the income pension system.

In addition, the AP Funds Act stipulates that the AP Funds shall manage the fund capital in an exemplary way through responsible investments and responsible ownership. In the asset management activities, special emphasis must be given to how sustainable development can be promoted without compromising on the objective of achieving the highest possible long-term return.

The AP Funds Act also stipulates that the AP Funds shall collaborate on achieving the goal of exemplary asset management, at a minimum by establishing a shared set of core values for management of the fund capital, uniform guidelines for reporting on how this goal has been achieved, and guidelines for which assets the fund capital should not be invested in. Each of the AP Funds shall also adopt guidelines for exercising their voting rights.

Since the AP Funds manage the public pension system's assets, the AP Funds' core values and actions on sustainability issues are based on the Swedish State's core values, which are concretised in, among other things:

- Sweden's Instrument of Governance (corresponds most closely to the constitution of other countries), which is based on democracy, fundamental freedoms and rights, the equal value of all people and the individual's freedom and dignity,
- the UN's international conventions that Sweden has signed, concerning among other things the environment, human rights, labour rights, corruption and inhumane weapons,
- the ILO's core conventions,
- international frameworks that Sweden supports, such as the UN Global Compact, the OECD Guidelines for Multinational Enterprises, the UN Guiding Principles on Business and Human Rights (UNGP), and

- Sweden's positions on matters pertaining to international public law.

It is important in sustainability work to have a starting point in international and generally accepted frameworks, as this strengthens the opportunities to conduct a successful dialogue with companies regardless of their national domicile. This also applies to the opportunities to cooperate with other investors and actors, which is deemed significant for achieving positive change.

In cases where Sweden is in support of a new convention or modification of an existing convention, but where such has not yet been formally ratified in Sweden, the AP Funds will act as if ratification has already taken place. The AP Funds will regularly monitor how the ratification process of the new or modified convention is proceeding. If Sweden has not ratified a convention within a three-year period from the time Sweden has announced its support of such, the AP Funds may reconsider the starting point for their guidelines on the issues that the new or modified convention pertains to.

Based on the aforementioned laws and international frameworks, the AP Funds have together drawn up an overarching description of the AP Funds' approach with respect to exemplary management of the fund assets in the income pension system and a shared set of core values. In addition, the AP Funds have drawn up uniform guidelines for reporting on how this goal has been achieved, which describe among other things the sustainability standards that the AP Funds report in accordance with as well as guidelines for which assets the fund capital should not be invested in. AP4 has concretised guidelines for exercising its voting rights in a separate Ownership Policy. These documents are available at AP4's website.

## Responsibility

The Board of Directors adopts this Sustainability Policy. The Policy is reviewed every year and is revised if needed. The Board of Directors adopts and follows up AP4's long-term strategy and yearly plan, in which concrete sustainability activities are included as a significant part.

The CEO administers sustainability matters in the operations on a continuous basis or delegates this duty to another employee of AP4. The CEO reports to the Board of Directors on a regular basis on the progress and development of sustainability work.

The Sustainability Policy is applied for the entire investment operations, both for investments in Sweden and internationally, and both for its own internal asset management and for external asset management mandates.

## Strategies for AP4's sustainability work

AP4 addresses a breadth of sustainability areas within the investment operations:

- climate and environment, such as climate change, resource efficiency, biodiversity, hazardous emissions,
- social aspects, such as human rights and workers' rights, and
- corporate governance aspects, such as shareholders' rights, board compositions, remuneration issues, transparency, and business ethics aspects such as corruption.

AP4 has five main strategies for conducting sustainability work in the investment portfolio:

## 1. Measure and report on sustainability

AP4 measures and reports on its internal sustainability work. Transparent reporting is something that AP4 also expects from the companies and businesses that AP4 has invested in. AP4 advocates for the development and production of qualitative sustainability data, and for transparent and suitable reporting on such from all pertinent parties.

## 2. Integrate sustainability factors in investment processes

AP4 integrates sustainability factors in investment decisions in a structured manner, adapted to the respective asset classes and investment process. Sustainability shall be an integrated part of all internal investment processes in order to, over time, ensure well-balanced and controlled risk and to be able to achieve a high return. When using external asset management services, sustainability is an important evaluation criterion.

## 3. Influence as an owner, investor and community actor

AP4 takes responsibility as an owner and investor by influencing companies, other investors and political decision-makers in a dialogue on sustainability issues. AP4 collaborates with other investors in order to achieve greater influence in dialogues and other advocacy work. For AP4, active corporate governance is an effective tool for, over time, creating and safeguarding asset values – also in relation to sustainability aspects.

## 4. Reduce sustainability risks in the portfolio

AP4 strives to reduce exposure to assets that are associated with elevated sustainability risks in an effort to reduce the level of risk in the portfolio. AP4 may also choose to not invest in companies whose operations are judged to be not aligned with an exemplary interpretation of the international conventions that Sweden has signed or international guidelines that Sweden supports. AP4 does invest in securities issued by companies or countries that are the subject of sanctions by the EU or UN.

## 5. Invest in strong sustainability trends

AP4 makes thematic investments that contribute to and benefit from the sustainability transition. Having an understanding of and analysing various sustainability aspects can contribute to returns through identification of investment opportunities for AP4, for example in specific sectors or companies that can be expected to contribute to and draw benefit from the transition to a more sustainable society.

## Broad handling of sustainability aspects

AP4's starting point is to maintain a broad perspective of sustainability aspects in the investment operations, where material sustainability aspects in climate and the environment, social responsibility and corporate governance are taken into consideration and handled.

## AP4's expectations on companies with respect to sustainability

AP4 believes that companies have a responsibility to work in accordance with laws, conventions and international guidelines, regardless of whether these are directed at states, individual companies or organisations. This responsibility applies regardless of whether the countries in which the companies operate have signed the conventions or have weaker protection of rights under law. AP4 expects companies to work actively to identify and manage risks, opportunities and consequences from economic, environmental, social responsibility and corporate governance perspectives. Further, AP4 expects companies to ensure the implementation of relevant policies, strategies and processes. This expectation also includes that companies follow up the effectiveness of their governance of sustainability aspects and risks coupled to the climate and environment, social responsibility and corporate governance, and that they transparently report on such to the public.

All of AP4's investments coupled to listed companies are subject to regular scrutiny with respect to violations of international conventions. If a company is identified in this process, a more in-depth analysis is initiated, followed by a dialogue, which is AP4's main tool for influencing companies. AP4 engages in dialogue with companies through its own asset management activities as well as through the Council on Ethics of the AP Funds (the Council on Ethics), which is a collaborative body between the AP Funds. A dialogue with respect to a violation that has been verified shall be conducted for a maximum of four years if the dialogue is not constructive. In the event a dialogue is not constructive, or the goal of the dialogue is not expected to be achieved, the Council on Ethics of the AP Funds recommends that the AP Funds exclude the company. Decisions to exclude a company are made by each AP Fund individually. An exclusion decision entails that AP4's holdings of securities issued by the company in question are to be divested. Every year the Council on Ethics monitors to see if the situation for excluded companies has changed. If a company resumes conducting operations in line with international conventions, a decision on re-inclusion may be made.

For AP4's unlisted investments, expectations regarding sustainability are regulated in investment agreements, including side letters. In the event of any violations, AP4's counterparties shall inform AP4, whereby a dialogue is initiated, and suitable follow-up is decided on.

## Identification of material sustainability aspects

AP4 conducts a stakeholder dialogue and materiality analysis on a regular basis together with other AP Funds to inform stakeholders about the AP Funds' work and to assess stakeholders' views of the AP Funds' handling of their respective assignments and operations in relation to returns and sustainability aspects. This dialogue and analysis contributes to prioritisations of the focus of sustainability work as well as consideration of material sustainability risks and reporting. Based on the stakeholder dialogue and own analysis, AP4 has identified three areas as being the Fund's most material with respect to sustainability risks:

### Climate risks

Climate change, which includes changes to the environment, biodiversity, ecosystems and ecosystem services, and the climate transition are systemic risks with global impacts on society, economies and expected returns. Climate risks include physical risks, such as extreme weather, flooding and rising sea levels, and transition risks,

for example changes in regulations, industry requirements and demand. Climate risks can thereby have a significant impact on the companies and assets that AP4 invests in.

## Human rights

Human rights entails that all people are born free and have equal value and rights. Human rights are universal, mutually collaborative and indivisible. There are various types of rights, including citizenship and political rights, economic, social and cultural rights, and special protections for individuals who belong to specific groups.

Human rights are part of international public law and are codified in various types of international agreements and conventions. Governments therefore bear ultimate responsibility for protecting human rights in their respective countries.

All companies have a responsibility to respect human rights, and this is part of sound and sustainable business activities and risk management. Respecting human rights entails that companies shall avoid having negative impacts on human rights and that companies shall act to prevent such negative impacts from arising.

Companies can have an impact on human rights through their operations, supply chains, interaction with communities and stakeholders, and through use of their products and services. Human rights violations can lead to, in addition to substantial individual and collective suffering, damaged reputation, fines, etc., which in turn can have a significantly negative impact on AP4's investments in companies and assets.

## Corruption

Corruption and shortcomings in business ethics are a global problem that exists in many companies and sectors. It is harmful and costly for society, it skews sound competition and undermines asset values as well as people's trust in society governed by law as well as political and economic systems. Various forms of corruption present commonly occurring sustainability risks for companies. With broad, global asset exposure, corruption poses a risk to the portfolio's long-term return.

## Focus areas in AP4's asset management and sustainability work

There are sustainability areas with systemic impacts on an investment portfolio and that are particularly suitable for an investor to address. These are areas that are financially significant and moreover that offer investment opportunities and thereby an opportunity to wield significant influence on a portfolio's long-term return and risk characteristics. AP4 has set two such focus areas: Climate & Environment and Corporate Governance.

### Climate & Environment as focus area

Climate change is one of the greatest challenges of our time, with a major expected impact on the environment, biodiversity, ecosystems and ecosystem services, and thus also on countries, sectors, companies and individual people. Climate change is considered to be a serious systemic risk that will have a growing impact on asset values and opportunities to generate long-term returns. Slowing climate change is therefore a

prerequisite for stable economic growth and thereby for AP4's opportunities to successfully perform its mission over time.

AP4 has chosen Climate & Environment as a prioritised sustainability area in its asset management operations. The area is considered to be financially material and represents a systemic risk that affects the ecological, social and financial stability of all the world's economies and countries. Sectors and companies with couplings to climate change are

exposed to significant risks – physical, regulatory, technological and social – that could bear a substantial impact on asset values and opportunities to generate long-term returns.

## Corporate Governance as focus area

A responsible owner and investor conducts active corporate governance work, which encompasses dialogues with companies and other stakeholders in order to bring about positive change, exercise voting rights at general meetings and investor forums, take an active role in companies' nomination committees, boards and investor bodies, and cooperate with other shareholders and investors.

AP4 has chosen Corporate Governance as a prioritised sustainability area in its asset management operations. Corporate governance is one of AP4's most important tools for integrating sustainability aspects in its asset management, and it is considered to be important from a financial perspective for AP4 to make demands and wield influence as a long-term and engaged owner in an effort to contribute to the portfolio companies' businesses and enable them to develop, improve and be conducted responsibly and transparently. Through its corporate governance work, AP4 has an effective tool to mitigate the sustainability risks that have been identified as being significant, that is, climate risks, human rights violations and corruption. Corporate governance is also an integral part of AP4's asset management strategy and is believed to contribute to long-term favourable returns.

As a long-term and engaged owner, AP4 shall work in the best interests of all shareholders and individual companies. AP4 shall also advocate for development of quality and practice in corporate governance and promote a well-working securities market.

## Sustainability goals

### Overarching goal for sustainable business

AP4's goal and expectation is that all companies that AP4 has invested in will operate in accordance with laws, conventions and international guidelines for the climate and environment, social responsibility and corporate governance. Additionally, AP4 has set specific goals for the Climate & Environment and Corporate Governance focus areas:

## Metrics and goals for Climate & Environment focus area

AP4 has set the following, specific goals for the Climate & Environment focus area. AP4 shall:

- contribute to the transition to a sustainable society. AP4's portfolio shall have net zero greenhouse gas emissions by 2040 at the latest, with an intermediate goal to cut greenhouse gas emissions in half by 2030 at the latest compared to 2020;
- make investments that reduce climate risk in the portfolio;
- make proactive investments based on strong sustainability trends that contribute to and benefit from the climate transition;
- based on identified indicators, evaluate possible asset management strategies, i.e., develop the way in which AP4 makes investments in the Climate & Environment focus area; and
- use its influence as a shareholder to contribute to a climate transition in line with the Paris Agreement.

## Metrics and goals for Corporate Governance focus area

AP4 has set the following, specific goals for the Corporate Governance focus area. AP4 shall:

- base its corporate governance work on the individual company's preconditions and strive to strengthen value creation in the company for the company's best interests and also to safeguard the interests of all shareholders. AP4's long-term goal is that the companies' businesses will develop and be conducted responsibly, sustainably and transparently, and thereby contribute to the companies' long-term value creation;
- use its influence and take responsibility as an owner and investor by working on nomination committees by virtue of its ownership stakes, actively participate in investor forums, and so on. In its work on nomination committees AP4 shall strive to ensure that the companies have the best possible boards based on the companies' needs of expertise and experience. In this regard, AP4 shall work systematically and advocate for adherence to the recommendation of the Swedish Code of Corporate Governance (the Code) on the share of women on company boards;
- vote at general meetings of shareholders. Particular emphasis shall be put on companies in which AP4 has a large holding or is a major shareholder; and
- advocate for development of quality and best practice in corporate governance, and promote a well-working securities market. AP4 supports well-grounded initiatives that support shareholders' rights and companies' work with sustainability.

## Follow-up and reporting

AP4's sustainability reporting shall be characterised by openness and provide factual and transparent information so that its operations can be reviewed and evaluated externally.

AP4's sustainability work, like its other work, is followed up and evaluated on a regular basis to ensure high quality and continuous development. This applies for AP4 as well as for the companies and assets that AP4 has invested in.

AP4 reports on its activities and goal achievement continually and in annual reporting.