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PUTTING PRINCIPLES INTO PRACTICE

2018 RESPONSIBLE INVESTMENT REPORT

Part of BNY MELLON

ABOUT INSIGHT INVESTMENT

OUR CREDENTIALS[1]

Asset manager owned by BNY Mellon:

- Based in London, New York, Sydney and Tokyo
- 221 investment professionals, 757 total staff

Key areas of specialisation:

- Risk management solutions
- Fixed income
- Absolute return

Responsible investment credentials:

- Pioneer of new approaches to support responsible investment, such as the investment industry's first climate risk model for corporate fixed income
- Offering a wide array of ESG or responsible investment implementation options, such as exclusions and norms screens, 'best-in-class' and positive impact approaches
- Founding signatory to Principles for Responsible Investment (PRI) in 2006
- A+ in 2017 PRI reporting assessment for ESG integration in corporate fixed income[2]
- Tier 1 ranking from the UK's Financial Reporting Council, signifying "a good quality and transparent description of [our] approach to stewardship"

Total assets under management:
£585bn/€659bn/$791bn/AUD1,012bn

By investment area

By client type

For more information, contact us at:
ri@insightinvestment.com

[1] As at 31 December 2017. Assets under management (AUM) are represented by the value of cash securities and other economic exposure managed for clients. FX rates as per WM Reuters 4pm spot rates. Reflects the AUM of Insight, the corporate brand for certain companies operated by Insight Investment Management Limited (IIML). Insight includes, among others, Insight Investment Management (Global) Limited (IIMG), Insight Investment International Limited (IIIL), Cutwater Asset Management Corp. (CAMC), Cutwater Investor Services Corp. (CISC) and Insight North America LLC (INA), each of which provides asset management services.
[2] The PRI reporting assessment generates a rating based on a range of metrics provided by signatories to the United Nations-supported PRI. More information about the PRI and relevant reports are available on the PRI web site at www.unpri.org

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Responsible investment lies at the heart of our business

ABDALLAH NAUPHAL

FOREWORD

Abdallah Nauphal
Chief Executive Officer

Responsible investment is not an optional extra.

At Insight, we believe that delivering superior investment solutions depends on the effective management of the risks and opportunities presented by environmental, social and governance (ESG) issues, as well as other long-term value drivers. We have integrated the analysis of ESG risks across our investment practices and processes, and we strive to continuously improve our approach.

These issues have an impact on every asset class and explain why we continually work to improve and strengthen our approach to responsible investment.

To focus on our fixed income capability, we have developed what we believe to be the investment industry's first climate risk model focusing on corporate debt, to help our portfolio managers and analysts by ranking issuers across our credit investment universe according to climate change risks. We hope this model will be of use to our clients and other investors and foster deeper engagement and thought on the risks presented by climate change. Another first has been our decision to distil our many years of experience and expertise managing segregated portfolios reflecting ESG criteria to develop a new sustainable euro corporate bond strategy that aims to have a positive environmental and/or social impact.

We have also continued to actively support initiatives that help to build the long-term sustainability and resilience of financial markets. As we discuss in this report, we have constructively engaged with stakeholders and regulators on the long-term replacement for Libor, sought to develop alternative sources of repo liquidity to ensure our clients are able to continue to hedge their exposures efficiently and effectively and urged regulators to consider the impact of encouraging cash-only variation margin on derivatives markets.

We believe that responsible investment means considering the long-term impact on our clients, rather than simply focusing on the short term for our business. I am proud to say that Insight has invested heavily in engaging on these and other issues, as this report reveals.

I hope the information we provide will help our clients and our peers to appreciate the value of Insight's approach and build confidence that responsible investment lies at the heart of our business.

A+

Rating from the PRI for strategy, governance and the integration of responsible investment-related issues across corporate bond portfolios

2006

Founding signatory to the UN-supported Principles for Responsible Investment (PRI)

Tier 1

Top ranking from the UK's Financial Reporting Council, signifying "a good quality and transparent description of [our] approach to stewardship"

© Image: *'Ghost World'* by Mikkel Beiter (Denmark)
Insight Astronomy Photographer of the Year competition 2017

The right way to invest for the long term is to invest responsibly...

Companies need finance, and in that context, bondholders' engagement with issuers is important.

ADRIAN GREY,
CHIEF INVESTMENT OFFICER
– ACTIVE MANAGEMENT

Q&A: WHAT IS RESPONSIBLE INVESTMENT – AND WHY IS INTEREST GROWING?

Q: HOW DO YOU DEFINE RESPONSIBLE INVESTMENT?

The meaning of responsible investment has evolved over time. Originally, responsible investment meant excluding some companies from your investment universe, according to pre-set criteria, but this has changed.

At the highest level, I find it helpful to ask: what does it mean to invest irresponsibly? If you invest without careful analysis; if you invest without taking all material risks into account; if you invest without considering the wider implications; if you invest without focusing on achieving your, or your client's, stated objectives – then you are investing irresponsibly.

This clarifies for me what responsible investment is. It's about investing in a way which takes all risks into account, for both the short and long term.

This means that we can understand what responsible investment is not. It does not mean simply avoiding certain investments, or divesting from particular sectors or issuers, though it may involve doing so. Nor does responsible investment mean sacrificing performance. In fact, we believe investing responsibly over the long term has the potential to increase the likelihood of achieving your objectives.

When you look at responsible investment in this way, it is clear that it is not a niche approach relevant to only a few investors or just part of your portfolio. Nor does it clash with investors' fiduciary duty. The right way to invest for the long term is to invest responsibly.

Q: INTEREST IN RESPONSIBLE INVESTMENT SEEMS TO BE GROWING. WHAT'S DRIVING THE CHANGE?

Since Insight was formed in 2002, we have committed to responsible investment across our business and in recent years we have seen a marked increase in client demand. This is encouraging us to keep pioneering new approaches, and it's also encouraging the wider investment management industry to demonstrate that they follow a responsible approach.

Regulatory change is also encouraging a shift towards demonstrable progress on relevant issues. A notable example is the French Energy Transition Law, which came into force in 2016 – it requires institutional investors to report on how they take ESG risks into account, and more specifically, climate risks. More broadly, there is a growing recognition that taking a responsible approach leads to better long-term outcomes for investors.

ESG issues are clearly material: we need to identify, assess and manage them, and this is not just about investment analysis but about engagement. Our clients expect us to be active owners. In many ways, equity investors are ahead of fixed income investors – the ability of equity investors to vote means they bear a specific responsibility with regard to how companies operate, and they can have a direct say in matters that affect long-term performance. But fixed income investors have become increasingly aware of the influence they can have. Companies need finance, and in that context, bondholders' engagement with issuers is important. They can play an important role in encouraging companies to better manage their ESG-related risks and opportunities, as our experience demonstrates.

THEMES FOR 2018

WE SET OUT THE KEY TRENDS FOR THE RESPONSIBLE INVESTMENT LANDSCAPE OVER THE YEAR AHEAD, AND EXPLAIN WHAT WE ARE FOCUSING ON IN THESE AREAS.

KEY TRENDS

Renewable financing

- Global investments in renewable energy and energy-smart technology totalled $333.5bn in 2017 (Source: Bloomberg New Energy Finance)
- **Insight expects to provide debt financing to support further renewables energy generation**

Green bond growth

- Green bond issuance reached over $140bn in 2017 (Source: Bloomberg), and more issuance is expected from new companies
- **Insight will apply its sustainable bond framework to new bonds issued (see page 20)**

Coal retirements

- More coal power plants were retired in 2017 across developed markets (Source: Bloomberg). In 2018 we expect large utilities in the US and Europe to continue retiring legacy coal plants and investing in renewables and natural gas
- **Insight will continue to monitor these trends and explicitly consider the financial implications of asset retirement and asset stranding**

Technology

- Technology impacts became more widespread and more companies developing digital strategies
- **Insight will be engaging with companies in 2018 on their cybersecurity activities (see page 57)**

Other sustainability bonds

- Insight anticipates more diversity of sustainable bond issuance in 2018
- **In 2017 Insight invested in its first social and sustainability bonds, including the first gender bond issued by a financial institution. In 2018 we will continue to apply our framework to evaluate new sustainable issues**

Corporate malfeasance

- Several high-profile scandals engulfed the corporate world in 2017 in developed and emerging markets
- **Insight will continue to focus on the fundamentals and getting to know management before investing in order to avoid these corporate shocks**

Regulation

- In Europe, regulators will likely issue stronger guidelines for investors on incorporating ESG factors into decision-making and improving stewardship
- **Insight will continue to support the work of the Institutional Investors Group on Climate Change, which encourages policymakers to develop robust frameworks for investors to incorporate climate risks into decision-making**

INSIGHT'S RESPONSIBLE INVESTMENT FOCUS FOR 2018

Stewardship

- Insight will undertake more ESG engagements and collaborate more with other investors to drive change and improvements at companies to encourage best practice

Client reporting

- Insight will enhance its clients reporting to provide more analysis of their portfolios' carbon exposures and ESG performance relative to their benchmarks

Increase access to our ESG capabilities

- Insight is considering developing vehicles that offer broader access to our responsible investment capabilities

© Image: *'Wanderer in Patagonia'* by Yuri Zvezdny (Russia)
Insight Astronomy Photographer of the Year competition 2017

INNOVATIONS IN 2017

Insight has pioneered responsible investment in corporate fixed income, and we continued to develop our approach in 2017:

- We developed what we believe to be the investment industry's first comprehensive ranking of how corporate fixed income issuers manage their climate change-related risks and opportunities (see page 12)
- We built on our wide-ranging expertise and experience of responsible investment to develop a new sustainable euro corporate bond strategy
- We created a framework to help our credit analysts assess sustainable bonds (see page 20)

A NEW CLIMATE RISK MODEL

INSIGHT HAS A LONG-STANDING COMMITMENT TO RESPONSIBLE INVESTMENT AND HAS EXPLICITLY TAKEN ESG ISSUES INTO ACCOUNT IN ITS FIXED INCOME RESEARCH PROCESS FOR WELL OVER A DECADE. CLIMATE CHANGE-RELATED RISKS – LITIGATION, PHYSICAL RISKS, TAXATION AND REGULATION – HAVE BEEN A KEY AREA OF OUR FOCUS OVER THIS TIME. WE HAVE DEVELOPED A NEW CLIMATE RISK MODEL TO HELP INVESTORS BETTER UNDERSTAND THE RISKS AND OPPORTUNITIES THAT CLIMATE CHANGE INTRODUCES TO THEIR PORTFOLIOS.

While our clients have been interested in our approach, there has been a dramatic upswing in their focus on climate change in the last two or three years. The reasons are obvious: the ratification of the Paris Agreement has signalled a step change in policy action and the Financial Stability Board's Taskforce on Climate-related Financial Disclosures (TCFD) has explicitly called on asset owners to report on how they are managing climate change-related risks and opportunities.

Our clients now ask us detailed and in-depth questions about the issuers we hold, how these issuers manage climate-related risks and opportunities, and the actions we are taking to manage climate-related risks in our portfolios.

With this level of attention, we concluded that we needed to put our analysis of issuers on a much more systematic and structured footing, allowing us to present a full cross-portfolio analysis and make meaningful assessments of how we are managing climate-related risks and opportunities.

INSIGHT'S CLIMATE RISK MODEL: A SUMMARY

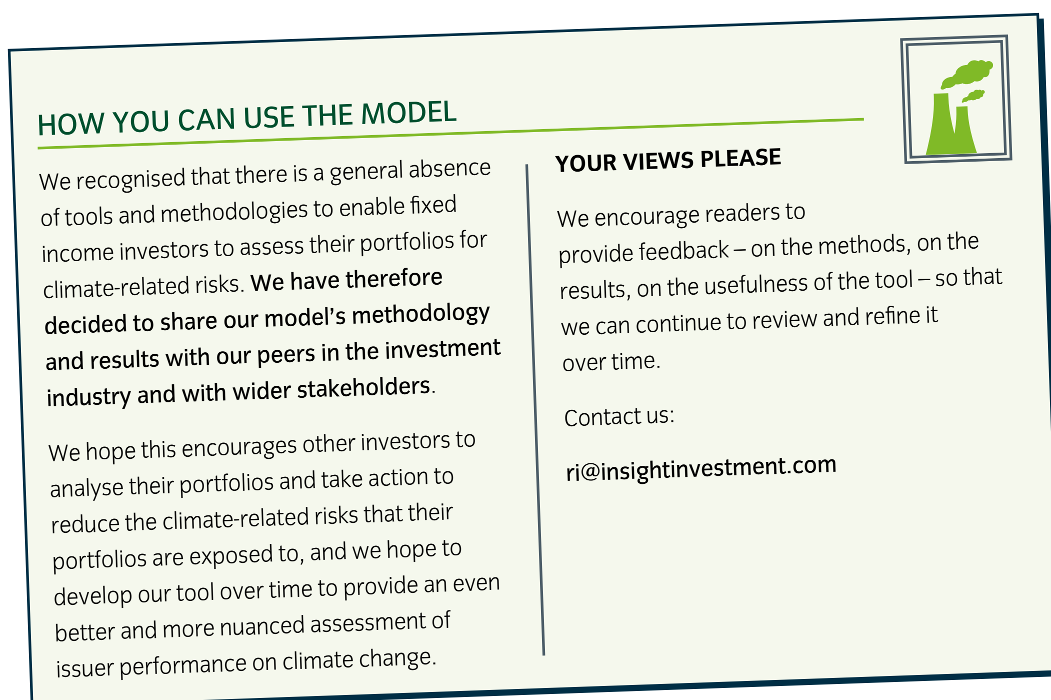
Our climate risk model is what we believe to be the investment industry's first comprehensive ranking of how fixed income corporate credit issuers manage their climate change-related risks and opportunities, and how are they are positioning themselves for the transition to a low-carbon economy. The model is designed to be used by institutional investors looking to assess risks and opportunities in their investment portfolios related to climate change.

- **It provides a wide-ranging assessment** of how nearly 1,900 corporate fixed income issuers – investment grade and high yield – are managing the risks and opportunities presented by climate change
- **It aims to help manage risk**, accounting for the risk characteristics of specific sectors and for the carbon impact of individual issuers. It aims to help investors identify the issuers most at risk from a transition to a low-carbon world. It also allows investors to identify issuers that are managing these risks effectively and those that are not
- **It helps users monitor risks in line with TCFD guidelines**. The model's framework and methodology are aligned with the requirements of the TCFD, with companies assessed against objectively assessable indicators across the four TCFD themes: governance, strategy, risk management, and metrics and targets
- **It is based on independent data** sourced from the Carbon Disclosure Project (CDP), MSCI and Bloomberg

HOW INSIGHT USES THE MODEL

At Insight, we use the model in a number of different ways, making it an integral part of our investment practices and processes:

- **To highlight companies to consider for engagement**: Engagement or active ownership is an integral part of our investment process, and we use the model to prioritise companies for engagement on environmental factors. We focus on the issuers in which we have, or intend to have, credit exposure. Among these issuers, we focus on those where we have strong relationships or in situations where we can work in collaboration with other investors or stakeholders – as we believe we are most likely to instigate change through such engagement. This helps to ensure that our engagement is more likely to have a significant impact.
- **To inform our credit analysis**: Insight's credit analysts have incorporated environmental risks into credit analysis for over a decade. Our process involves using third-party analysis, including research and ratings, to identify companies potentially showing elevated risk levels

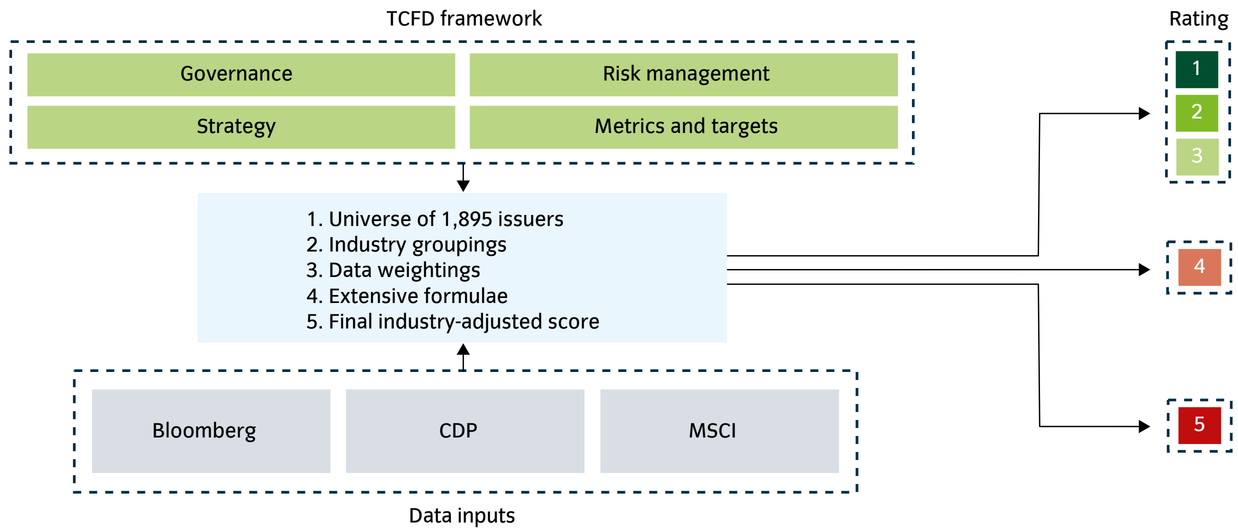


METHODOLOGY OVERVIEW

Our climate risk model (see Figure 1, overleaf) has a number of important features:

- The model's universe is a list of corporate bonds, based on the consolidated list of issuers from the three largest corporate bond indices (the Bloomberg Barclays Pan-European Aggregate Index, Bloomberg Barclays Global Aggregate Index and Bloomberg Barclays Global High-Yield Index). In total, we assessed 1,895 issuers in the 2017 iteration of the model
- Sectors (and issuers within sectors) are divided into one of three risk groups according to whether we deem them to be exposed to high, moderate or low climate-related risk
- The model is based on information provided by Bloomberg, MSCI and CDP
- The model is aligned with TCFD and a total of 35 indicators are used to assess performance against the four dimensions recommended by TCFD (governance, strategy, risk management, and targets and metrics)
- Issuer rating is graded from 1 (best) to 5 (worst). The grading process accounts for issuer ranking based on individual indicators, with the results weighted to reflect sector-specific characteristics, and the carbon ranking of issuers relative to their sector peers

Figure 1: Insight's climate risk model



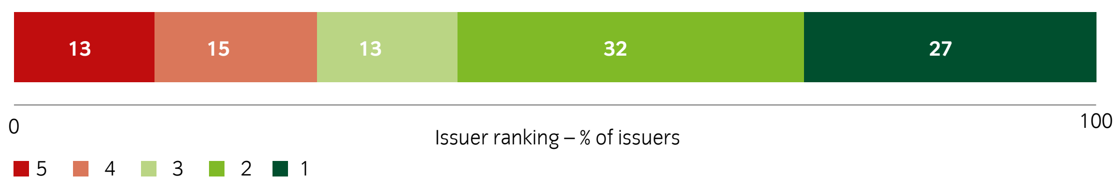
TWO KEY FINDINGS FROM THE 2017 RESULTS

We intend to publish the results on our website later in 2018. Here we outline two key findings from the first iteration of the model, and offer some wider observations.

1 Key finding: There are wide variations in ranking between issuers – suggesting significant variance in approach to climate change-related issues

The results reveal wide variation in rankings, reflecting the management practices, processes and performance of leading companies relative to their peers (see Figure 2).

Figure 2: Issuer ranking in Insight's climate risk model[3]



The leading companies generally have the following characteristics:

- Better governance processes (e.g. they have board oversight of climate change issues; they provide incentives for the management of climate change issues)
- Superior risk management processes (e.g. they explicitly identify climate-related risks and opportunities; they have reduced their exposure to high risk geographies)
- More developed carbon-management strategies (e.g. they have long-term emission reduction targets; they engage constructively with policymakers; they use significant amounts of clean or renewable energy)
- Better data and more robust targets

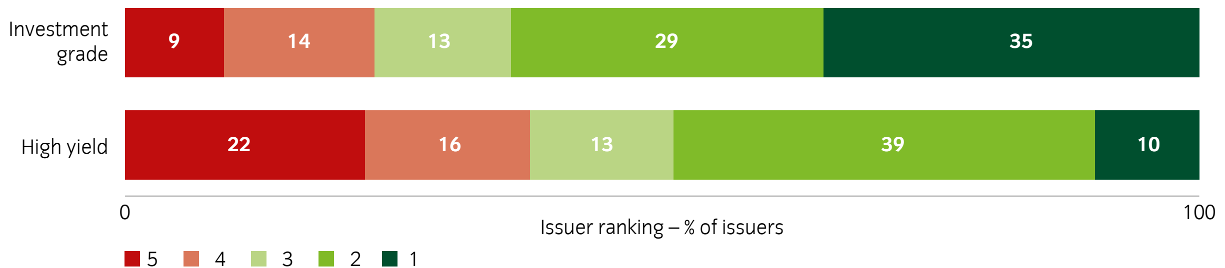
Implication: Detailed issuer analysis will pay dividends in identifying climate-change related risks

[3] Source: Insight Investment. As at 31 December 2017.

2 Key finding: Investment grade issuers appear to manage climate risks better than their high yield peers

There is a notable divergence in the performance of investment grade and high yield issuers (see Figure 3). Within investment grade credit, 35% of issuers are given our top rating, compared to 10% of high yield issuers. High yield issuers are also more likely to receive our lowest rating, at 22%, versus 9% for investment grade credit.

Figure 3: Ratings distribution for the two major universes in the model[3]



Investment grade companies are more likely to have better disclosures, as many of these bonds are issued by listed companies. The model rewards and acknowledges companies with more transparent disclosures.

By contrast, many high yield issuers are smaller companies, which typically have fewer management resources to devote to climate-change-related matters (whether management systems, processes or reporting). Furthermore, the energy sector – which, as discussed above, is one of the sectors most exposed to climate change – is disproportionally represented in high yield universes.

Implication: Detailed analysis is even more important for high yield issuers relative to their investment grade peers as there are wide variations in ranking between issuers – suggesting significant variance in approach to climate change-related issues

WIDER OBSERVATIONS

Fixed income disclosures on climate change remain very poor.

While there are pockets of excellence, most companies simply do not provide enough information for investors to properly assess the risks and opportunities associated with the impact of climate risk. These issues are particularly prevalent for issuers that are not publicly listed, for smaller companies and for companies that are classed as high yield.

It is our hope that this situation will improve as the TCFD recommendations are adopted, as governments move to introduce formal climate change disclosure requirements for companies and as investors start to increase the pressure on companies to improve their climate change-related disclosures.

There appears to be a gap between management practices and carbon performance.

Our perception is that many companies do a reasonably good job in terms of, for example, disclosing that they have a board and executives responsible for climate change, identifying climate-related risks and opportunities and providing basic disclosures.

However, it is not clear that these translate into better performance in areas that arguably matter the most, such as carbon emissions.

We will continue to develop our data to test this comprehensively.

[3] Source: Insight Investment. As at 31 December 2017.

SUSTAINABLE EURO CORPORATE BOND STRATEGY

IN 2017, WE ADAPTED AN EXISTING EUROPEAN CREDIT STRATEGY TO CREATE A NEW SUSTAINABLE EURO CORPORATE BOND STRATEGY.

The strategy has three distinguishing features:

1. It will only invest where minimum standards for environmental, social and governance (ESG) factors are met,
2. It seeks to make a positive impact by favouring issuers with superior sustainability profiles, and
3. We will actively engage with companies held to encourage better management of social and environmental issues.

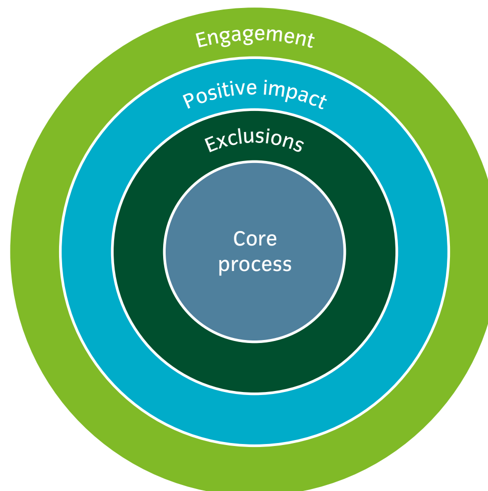
BENEFITS

- **Unique approach combining core alpha-seeking investment expertise and sustainability criteria**: the strategy seeks to outperform a conventional corporate benchmark (the Barclays Euro Aggregate Corporate Index) while also taking ESG and sustainability criteria into account
- **Sophisticated management of ESG factors focusing on impact as well as exclusions**: the strategy seeks to positively allocate to companies which have superior ESG profiles or are deemed to have a positive impact
- **Commitment to engagement**: we commit to engage with companies with deteriorating ESG profiles with a view to actively influencing their future behaviour
- **In-depth reporting**: Insight intends to offer detailed annual reports on ESG and sustainability characteristics resulting from the strategy (see page 18 for examples of the data we offer)
- **Established strategy and attractive track record**: the underlying euro corporate bond strategy, on which the sustainable strategy is based, has been managed since 2005

IMPLEMENTING A SUSTAINABLE APPROACH

The strategy invests on the basis of our long-established investment philosophy and process, and incorporates quantitative and qualitative inputs. Our sustainable approach builds on this investment process to augment the ESG focus of the strategy.

Figure 4: Insight's sustainable euro corporate bond strategy – a sustainable approach



EXCLUSIONS

In the strategy, Insight applies exclusions and screens focused on various ESG and sustainability factors that aim to avoid worst-in-class industry players and unsuitable sectors. Typically 10% to 15% of the benchmark (by value) is excluded. The exclusions leave the strategy with an ESG-optimised universe from which to build a portfolio.

POSITIVE IMPACT

While exclusions are an important part of ESG investing, we believe that investors should also focus on the impact of the investments they are making. In this regard, there are two main pillars to our unique impact strategy. First, using the ESG-optimised universe, we aim to tilt a portfolio in favour of companies with higher ESG ratings while balancing this goal with alpha-generating targets. Secondly, we look to positively allocate to issuers deemed to have a positive social impact. Using a proprietary impact policy, we seek to take an overweight position in 'positive impact' bonds. These are bonds issued by companies with material revenue derived from sources aligned with the UN Sustainable Development Goals (SDGs), as well as green bonds that pass our internal assessment framework. (Green bonds are issues where proceeds are used for projects or activities that reduce climate impact.)

ENGAGEMENT

Company engagement is an integral part of our credit process. All our analysts regularly meet with issuers to discuss a range of factors, including ESG factors. When the strategy identifies deteriorating ESG performance in one of its holdings, our analysts will engage with the company to establish the reasons and enquire about remedial actions. If relevant problems are not resolved within 12 months, the strategy will sell the bonds.

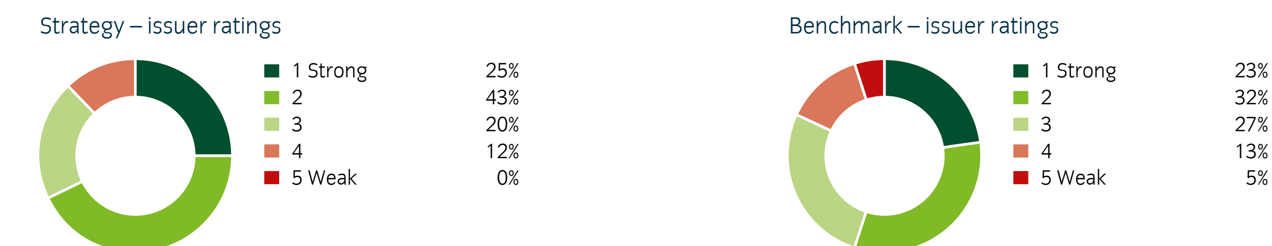
CARBON

We believe that focusing on carbon emissions is an important factor for any portfolio aiming to focus on ESG and sustainability-related factors. As part of this focus, the strategy will aim to have a carbon intensity that is significantly lower than benchmark levels.

© Image: *'The Cable Route of Half Dome at Night'* by Kurt Lawson (USA)
Insight Astronomy Photographer of the Year competition 2017

TRANSPARENCY IN ESG REPORTING

Figure 5: The strategy's ESG profile compares favourably with its benchmark (Barclays Euro Aggregate Corporate Index)[4]



	Theme	Strategy	Benchmark
Environment		2.0	2.2
	Carbon emissions	1.3	1.3
	Climate vulnerability	2.4	2.3
	Biodiversity	2.8	2.8
	Toxic emissions	1.6	1.9
	Water risk	1.8	1.8
	Product footprint	1.8	2.2
Social		2.9	3.1
	Labour management	3.1	3.2
	Health & safety	1.5	1.6
Governance		2.9	3.0
	Corporate governance	2.6	2.6
	Business ethics/Fraud	3.4	3.4
	Anti-competitive practices	3.1	3.2
	Corruption and instability	3.2	3.2
	Financial system stability	4.1	4.0
	Tax transparency	2.8	2.7

Figure 6: The strategy's weighted carbon intensity compares favourably with its benchmark[5]

Carbon intensity measures the efficiency of a portfolio in managing carbon emissions. The figure is calculated using Scope 1 and Scope 2 carbon figures.[6] The combined figure is then normalised by revenue for each issuer. Insight then weights the carbon intensity according to strategy holdings to derive an overall carbon intensity figure for both the strategy and the benchmark.

Carbon intensity is the most commonly-used metric for assessing the carbon footprint of a portfolio. The figure allows for a more accurate measure of a portfolio's efficiency because is takes into account a company's size rather than absolute carbon output.

[4] Source: Insight Investment. As at 31 December 2017. The ESG themes above provide a quick summary of the portfolio's most important ESG impacts. These themes are identified by Insight as the largest risk and performance drivers. Every ESG theme has a different weighting that contributes towards a pillar score. The ratings use data from a third-party provider. [5] Source: Insight Investment. As at 31 December 2017. [6] Scope 1 emissions refer to direct emissions from sources owned or controlled by the issuer. Scope 2 emissions refer to indirect emissions as a result of energy purchased by the issuer.

MEASURING THE STRATEGY AGAINST THE UN SUSTAINABLE DEVELOPMENT GOALS (SDGs)

We measure our strategy against the UN SDGs by estimating the proportion of company revenues of each issuer relative to each of the 17 themes (see Figure 7). For example, pharmaceuticals are assessed for revenues linked to treating major diseases, which is denoted as being a positive social impact under goal three of the SDGs ('good health and well-being').

We identify issuers that we deem to have a significant revenue link to an SDG, and aim to allocate at least 5% of the strategy to these high-impact issuers. As at 31 December 2017, more than 10% of the strategy was classified as high impact.

Figure 7: The proportion of the strategy assets linked to the UN SDGs[7]

[7] Source: Insight Investment. As at 31 December 2017.

SUSTAINABLE BOND ANALYSIS FRAMEWORK

WE HAVE DEVELOPED A FRAMEWORK TO ASSESS COMPANIES' SUSTAINABLE BOND ISSUANCE. THE TRAFFIC-LIGHT OUTPUT FROM THE FRAMEWORK IS USED BY OUR CREDIT ANALYSTS AND IS AN ADDITIONAL INPUT INTO OUR PROCESS WHEN CONSIDERING BONDS FOR ALL INSIGHT'S INVESTMENT PORTFOLIOS.

Joshua Kendall
ESG Analyst

"With green bond issuance reaching over $140bn in 2017 (see page 51), Insight felt a process to evaluate sustainable bonds was required to help guide our decisions to buy or avoid some credits. We saw, for example, some controversial green bond issuance in some sectors and we considered these bonds inappropriate for portfolios, even though they were deemed appropriate by third parties. The need for an internal process is important as more impact-themed bonds come to market. We subject sustainable bonds to greater analysis in three key areas to inform our overall assessment on the strengths of their sustainability. We believe this approach is different to the sustainable bond rating agencies because we are judging the ESG credentials of both the issuer and the issue. Every new sustainable bond that we add to client portfolios on primary issuance will have been viewed by a credit analyst."

Our credit analysts, accustomed to viewing ESG and rating agency reports, rate issuers on the following categories from our framework:

ESG RANKING

Analysts consider the ESG performance of the issuer, including corporate governance quality, its history of environmental and social activity and breaches of global norms. Analysts pay close attention to companies with:

- High-profile negative events
- Weak history of ESG activities
- Performance versus peers

STRUCTURE OF BOND IMPACT

Analysts consider the strengths of the framework outlining the impact of the bond. The framework provides guidance for how the company will use bond proceeds. Analysts will consider:

- Breadth of eligible projects for investment (is the framework clear on how money can be spent)
- Quality of the bond investment framework (is there a good internal governance process for monitoring spending/approval)
- Whether there is an independent third-party assessment of the bond's structure
- Commitment to annual reporting and type of disclosure

BOND IMPACT PERFORMANCE

Analysts focus on the tangible impact of the bond. This is a qualitative and quantitative assessment. Individual credit analysts have the flexibility to define the impact performance of the bond. A qualitative assessment may consider:

- Tangible change in strategy and the ambitions of the issuer
- Links to new projects targeting organic growth versus business-as-usual

A quantitative assessment may consider:

- Positive sustainability activity, including efficiencies and individual metrics. This may include new renewable energy produced
- Negative sustainability activity, including individual metrics. This may include a review of overall net carbon emissions following capital expenditure investments

Analysts consider the three framework areas and allocate a yes/no score. Credit analysts will then use their judgement to allocate a traffic light score.

- Red score indicates the sustainability bond does not meet Insight's minimum sustainability requirements
- Amber score indicates there are weaknesses in the bond with regard to sustainability
- Green score indicates a company's sustainability bond meets Insight's minimum sustainability requirements

Analysts are expected to give a brief summary of the bond and their reasons for assigning the traffic light score. A 'red' score does not automatically exclude the bond from Insight's portfolios. The rating will be used as an input into the overall fundamental review of a credit and its suitability for all credit portfolios.

Figure 8: Insight's framework for assessing sustainable bonds[8]

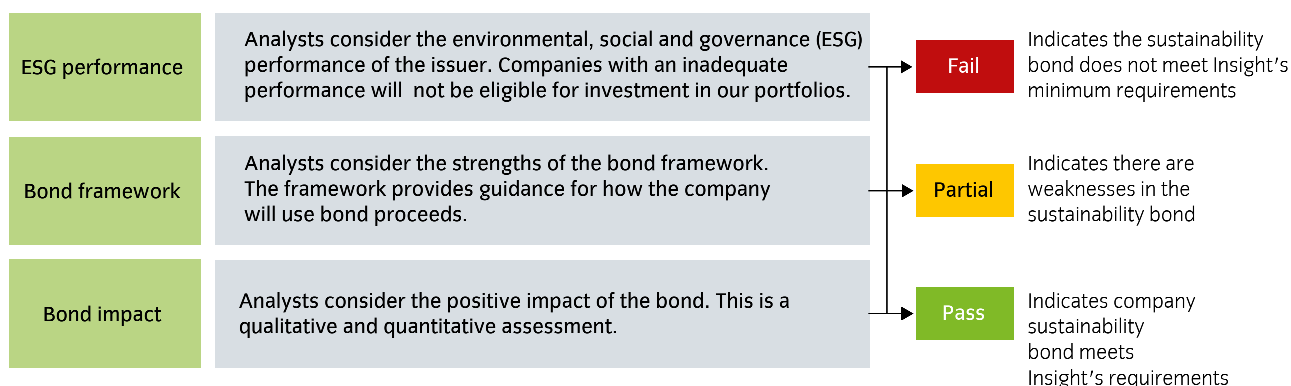


Figure 9: Examples of sustainable bond assessments in 2017[9]

Issuer sector	Bond type	ESG performance criteria met?	Bond structure criteria met?	Impact criteria met?	Framework score	Analyst assessment
Utilities	Green	Yes	Yes	Yes	Pass	The green hybrid proceeds will be used to finance and/or refinance renewable energy projects in the UK and Germany: onshore and offshore wind projects. The company has a best-in-class ESG rating and will report on the annual GHG emissions avoided (in tCO2e) in its Annual Sustainability Report.
Autos	Green	No	No	No	Fail	The bond proceeds are to be used to fund retail lease and financing sales of the company's petrol-electric hybrid vehicle models. This will not change the usual operations of the issuer and the green credentials of these hybrid vehicles is questionable. The company also fails on the ESG front with 'worst-in-class' governance practices and weak labour management practices.
Financials	Green	Yes	Yes	Yes	Pass	Proceeds will be used to fund existing assets, split roughly equally between renewable power and low carbon commercial property. The latter must meet the Climate Bonds Initiative's Climate Bonds Standards for low carbon and have high ratings in relevant national environmental building scores. The company has a high environmental score from MSCI.
Utilities	Green	Yes	Yes	No	Fail	Mixed impact from eligible projects. While offshore wind projects have a beneficial impact on carbon reduction, the use of proceeds for the conversion of central power stations to biomass is more questionable. Burning wood pellets releases a material amount of CO2 and could accelerate deforestation if the technology is adopted on a large scale.

[8, 9] Source: Insight Investment.

© Image: *'Mr Big Dipper'* by Nicholas Roemmelt (Germany)
Insight Astronomy Photographer of the Year competition 2017

RESPONSIBLE INVESTMENT IN PRACTICE

Insight has applied a responsible investment approach since our launch in 2002. We have long-established processes that fully integrate ESG factors into our credit research process, and have continued to enhance our approach across our business. For example, we have created a process to generate ESG ratings where we cannot source independent ESG analysis from our market data providers. This is often needed for smaller issuers, especially emerging market and high yield companies.

Examples of how our ESG risk analysis has influenced our investment decisions or the industry in 2017 include:

- Our engagement with a major listed company, along with other investors, which led the company to provide more detailed information in its financial reports (see page 30)
- A decision to invest in a new consumer non-discretionary issue in our active bond portfolios but sell it earlier than would have if we did not have the analysis (see page 31)
- A decision to not invest in a new investment-grade retail issue due to overriding ESG risks (see page 31)

INSIGHT'S RESPONSIBLE INVESTMENT POLICY

WE BELIEVE STRONG GOVERNANCE PRACTICES AND MANAGEMENT OF ENVIRONMENTAL AND SOCIAL RISKS ARE IMPORTANT DRIVERS OF INVESTMENT VALUE OVER THE SHORT AND THE LONG TERM. WE ALSO BELIEVE THAT DELIVERING SUSTAINABLE INVESTMENT RETURNS IS DEPENDENT ON EFFICIENT AND WELL-MANAGED FINANCIAL MARKETS, AND STABLE AND TRANSPARENT SOCIAL, ENVIRONMENTAL AND ECONOMIC SYSTEMS.

Our objective is to achieve superior investment returns over clients' expected time horizons. We consider responsible investment to contribute towards this goal through providing investment solutions that deliver quality and excellence; managing financial and non-financial risks for our clients; and operating to high ethical and professional standards.

We consider responsible investment as central to our investment activities, to our culture, to our relationship with clients and to our interaction with stakeholders.

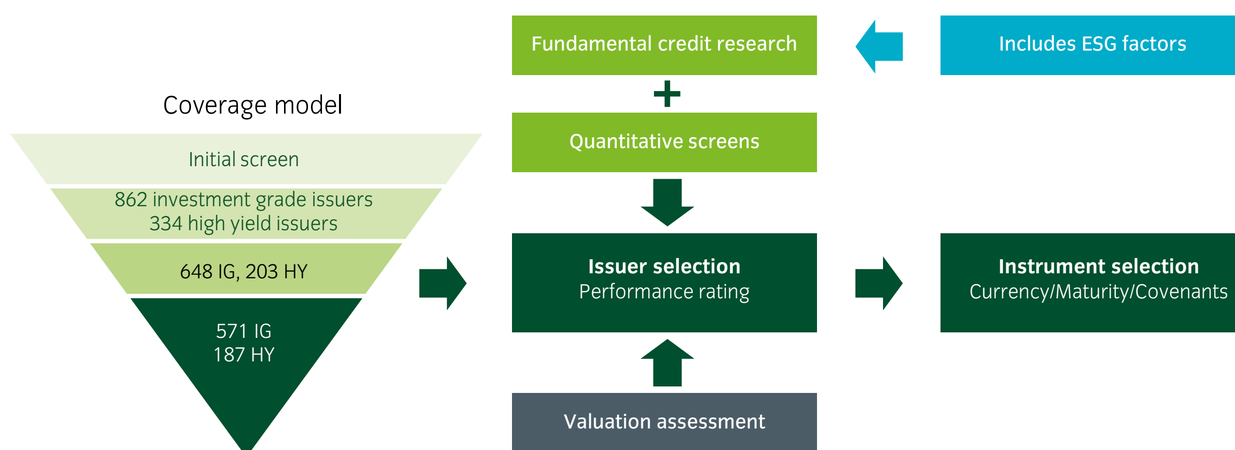
To deliver on our objectives, we:

1. **Take account of financially material short and long-term risk factors in our investment research and decision-making processes**. These risk factors may include environmental, social and governance (ESG) issues.
2. **Exercise our stewardship role in the companies and other entities in which we invest**. We believe that good stewardship can create investment opportunities and reduce investment risk. We therefore engage with management to discuss issues such as strategy, deployment of capital, performance, remuneration, risk management and ESG factors. We also vote our shareholdings.
3. **Support efforts that seek to improve the operation, resilience and stability of financial markets**. This includes sustainable economic development and health of the natural environment.

RESPONSIBLE INVESTMENT PROCESS IN FIXED INCOME

IN DISCUSSION WITH PORTFOLIO MANAGERS, WE APPLY FILTERS TO OUR CREDIT UNIVERSE TO ARRIVE AT A SMALLER GROUP OF INVESTABLE ISSUERS. THIS SHORTER LIST IS THEN SUBJECT TO RIGOROUS FUNDAMENTAL ANALYSIS BY OUR CREDIT ANALYSIS TEAMS IN LONDON AND NEW YORK. WE TEND TO SCREEN OUT INVESTMENTS IN ISSUERS THAT OFFER INSUFFICIENT ACCESS TO FINANCIAL DATA AND COMPANY MANAGEMENT, AND ISSUES WHICH ARE INSUFFICIENTLY LIQUID (SEE FIGURE 10).

Figure 10: ESG risks are integrated within Insight's credit analysis[10]

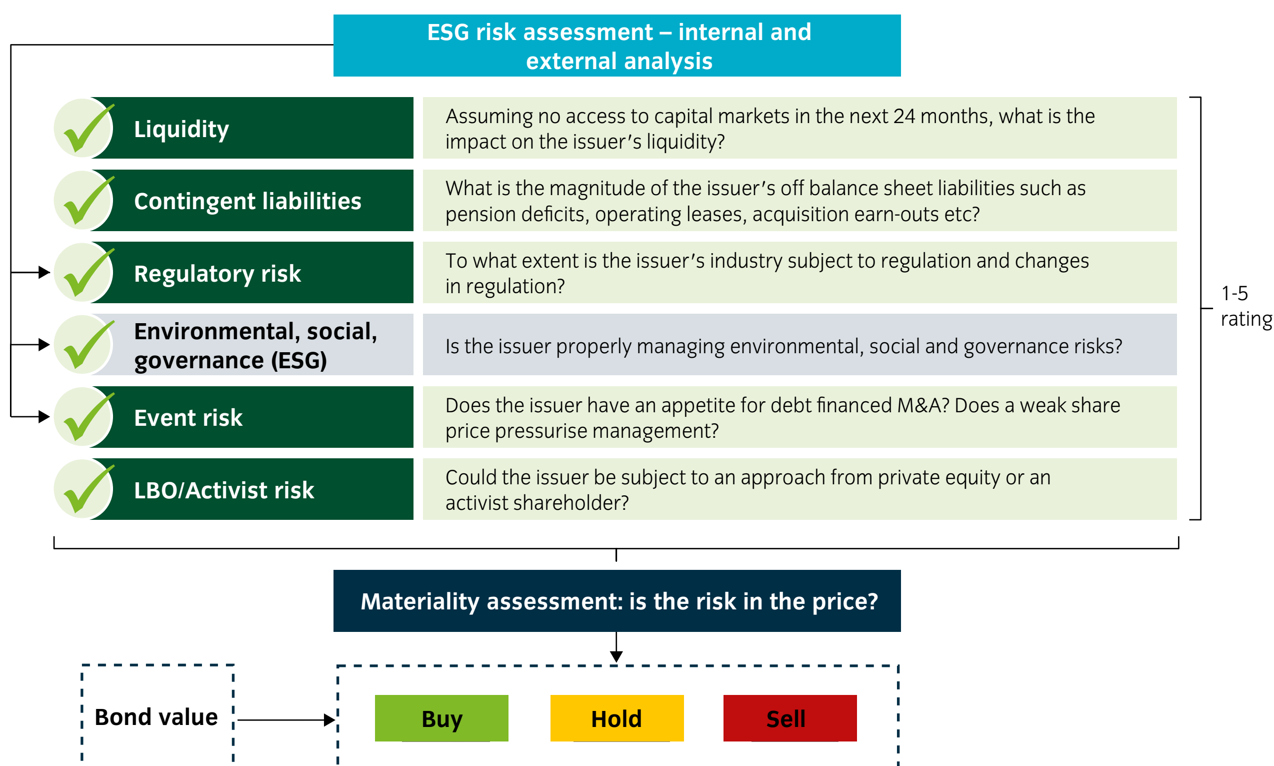


Our analysts conduct a fundamental review of a company's financial risk, in particular its cash flow, revenue and profitability. We pay particular attention to the scoring of key business risks using a checklist that identifies important sources of risk that can lead to a sudden deterioration in credit quality and that identifies sources of risk that may not be readily apparent from an examination of a company's financial performance (see Figure 11, overleaf).

© Image: *'The Rho Ophiuchi Clouds'* by Artem Mironov (Russia)
Insight Astronomy Photographer of the Year competition 2017

[10] Source: Insight Investment. For illustrative purposes only.

Figure 11: Insight's risk checklist[11]



Default risk is the prism through which our analysts consider every issue. A full investment analysis is required to inform an investment decision and ESG risk scores are a necessary element in assigning a credit rating that indicates the relative risk of default loss. Insight's credit analyst team is charged with determining the materiality of issues on the checklist, defined as the contribution these make to the default likelihood of a potential investment.

It is through the combination of ESG risk screening and financial analysis that Insight's extended credit risk appraisal process brings together an assessment of the financial risks associated with a company's performance with a clearly defined set of key business risks, including ESG considerations, as a part of the mainstream investment process. Insight believes that its approach exemplifies Principle 1 of the UN-supported PRI.

EXAMPLES OF ANALYST RECOMMENDATIONS

Below, we give two examples of how our analysts' views on ESG have affected their investment recommendations. Note that low ESG scores do not automatically result in an exclusion or sell decision.

Example LONG – European autos company

- Worst-in-class ESG rating
- Improving governance outlook
- Committed to improving ESG rating

Analyst recommendation:
Suitable for active and buy-and-maintain portfolios

Example SHORT – US telecoms company

- Low ESG ratings, especially for governance
- Uncertain fundamentals due to high-risk M&A and increased leverage
- Risk of credit rating agency downgrade

Analyst recommendation:
Sell via credit default swap, buy protection; not suitable for buy-and-maintain

[11] Source: Insight Investment.

IDENTIFYING ESG RISKS

We transpose third-party ESG ratings into the five-point risk scale that we use to assess the significance of non-financial risk factors. Our ESG assessment focuses on the material risks in each sector or business. For example, we consider health and safety, and carbon emissions, as important risks for companies operating in the mining sector, but we see these as generally of lower importance for financial services companies. The exception is with corporate governance, where we consider the risks an important part of our evaluation for every type of issuer and credit quality. The range of ESG risk issues and the scores used are illustrated in the graphic below.

Figure 12: ESG ratings framework[12]

ESG Overall Score Normalised industry-adjusted score 1-5							
Environment Pillar Absolute score 1-5			Social Pillar Absolute score 1-5			Governance Pillar Absolute score 1	
Carbon	Natural Capital	Pollution	People	Products	Place	Corporate Governance	Behaviour
Carbon Emissions	Water Stress	Toxic Emissions	Labour Management	Product Safety and Quality	Controversial Sourcing	Board	Business Ethics
Carbon Vulnerability	Biodiversity and Land Use	Waste	Health & Safety	Chemical Safety		Pay	Anti-Competitive Practices
Product Footprint	Raw Material Sourcing		Human Capital Development	Financial Product Safety		Ownership	Corruption and Instability
Financing			Supply Chain	Privacy and Data Security		Accounting	Financial System Instability
			Health and Demographic Risk	Responsible Investment			Tax Transparency

Ratings used in Risk Checklist (ESG Overall Score and pillar scores)

ESG key issues (issue rows)

Assessed category for all issuers (Board, Pay, Ownership, Accounting)

FILLING THE GAP

Data from third-party providers is important, but not enough. For many smaller issuers, especially emerging market and high yield companies, the availability of relevant non-financial data often lags behind that available for larger issuers. For issuers in our investment portfolios it is important that, wherever possible, we have data that enables us to make a robust assessment of companies' risk exposure and risk management. We are particularly aware that assuming that a lack of disclosure means that a company is not effectively managing the issue in question could lead to us significantly mispricing the risks associated with these issues.

Insight follows a process to generate ESG ratings where we cannot source independent ESG analysis from our market data providers:

1. Credit analysts identify companies with no ESG ratings but where the company is, or may be, issuing bonds that may be suitable for Insight's credit portfolios
2. Credit analysts work with the ESG Analyst to develop a custom ESG self-assessment tool that reflects the sector-specific risk issues relevant to the issuer
3. Company management is contacted to complete the self-assessment
4. Insight generates an ESG scorecard based on the self-assessment response
5. Insight credit analysts follow up with any risk issues identified

IF ESG, STRATEGIC AND FINANCIAL RISKS ARE IDENTIFIED THROUGH A DUE DILIGENCE PROCESS, OUR

[12] Source: Insight Investment and MSCI. For illustrative purposes only. Based on MSCI ESG ratings framework.

ENGAGEMENT IN FIXED INCOME

ANALYSTS ARE EXPECTED TO ENGAGE IN A DIALOGUE WITH COMPANY MANAGEMENT. AS A LARGE INSTITUTIONAL INVESTOR, INSIGHT HAS GOOD ACCESS TO AND REGULARLY MEETS WITH MANAGEMENT TO DISCUSS MATTERS RELATING TO STRATEGY, PERFORMANCE, AND FINANCIAL POLICY.

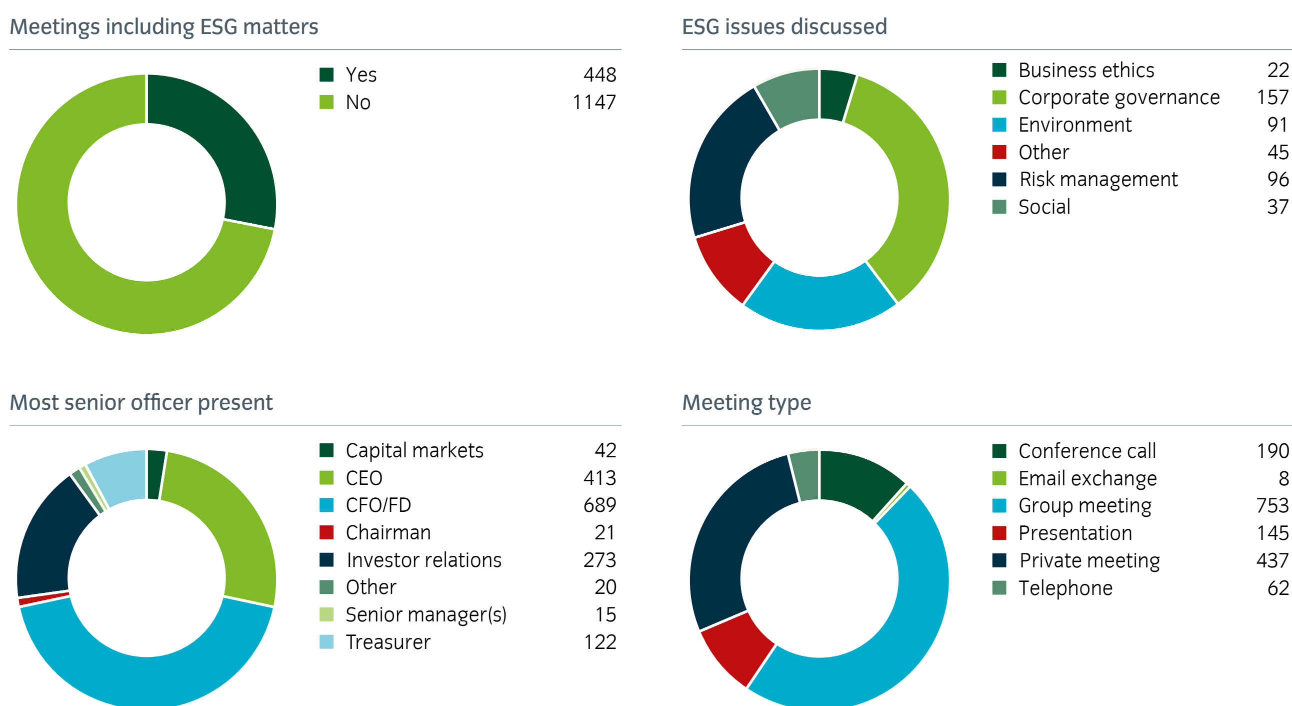
Material governance issues are regularly discussed and material environmental and social issues are covered when relevant. This is because we consider ESG risks alongside other factors when assessing a company's financial strength, strategic direction, overall quality of management, and the market valuation of its securities. We also monitor changes, particularly downgrades, to key risk scores each quarter.

Insight's credit analysts meet all companies before investing in any bonds or loans they have issued or are about to issue. We have regular contact with companies through a variety of methods, including face-to-face meetings, investor conferences, conference calls, emails and letters. The frequency of our communication with issuers depends on the risks identified during our research process. Company meetings are undertaken by our in-house analysts because we consider engagement to have material financial implications and that it is best understood within the context of the wider investment process.

Escalating engagement activities will occur on a case-by-case basis. From a risk perspective, if we are not satisfied with a company's management of risk (including ESG-related risks), we are prepared to sell holdings or move to an underweight position. In some portfolios that will not be possible because of mandate restrictions. In such situations, we discuss potential investment actions with clients (which may include take-no-action, sell holdings, or continue monitoring).

For 2017, our ESG engagement activities are shown in Figure 13.

Figure 13: Dialogue with issuer management in 2017[13]



[13] Source: Insight.

LIVE EXAMPLES: CREDIT ANALYST COMMENTS IN 2017

ENERGY

"[Company] scores very poorly on ESG due to weak governance (mainly on concerns over corruption risk) and weak safety and security as operations are not certified to international third-party standards. This is also combined with a number of severe controversies. I believe that ESG risks do currently have a negative effect on the company, mainly through the effects of unexpected stoppages in the company's operations. Making improvements to reliability would likely require more capital investments into its upstream and downstream facilities and put further pressure on the financials."

HEALTHCARE

"Corporate governance concerns include overloaded directors and compensation practices. The concerns are not material to [Company's] overall creditworthiness but the company's increased leverage and more aggressive financial policy makes the company a 'no' for buy-and-maintain accounts."

CONSUMER DISCRETIONARY

"It has become increasingly clear over the years that [management's] only objective is to maximise equity value, hence the re-levering strategy…and the hefty pay despite poor business performance. The board is entrenched and scores below-par in terms of independence. These weak corporate governance standards should be a key consideration if one considers an investment in [Company]."

FINANCIALS

"[Company] has corrected most of their previously flagged corporate governance issues. Mostly from fixing the audit committee, its corporate governance score went from 5 to 4 (now better than peers). We had it on Hold specifically because it had one of the worst corporate governance scores in our coverage universe; this takes it to mid-table. Agreed to add this to next buy-and-maintain meeting agenda to consider taking it off Hold."

MATERIALS

"Significant governance risk in the following areas: a board that does not include a majority of independent directors, the Chairman is an executive, the presence of certain related-party transactions and possible board entrenchment, poor disclosure in relation to executive pay and evidence of material internal control weaknesses. Given these issues, I am recommending that [Company] remains a 'no' for high yield buy-and-maintain."

ENERGY

"I asked management about their relative low ranking versus peers on the investor call yesterday and management was extremely candid and open about their environmental policies and stewardship. Management noted several initiatives taken that proactively addressed issues raised by environmental groups. Management noted that they are required to make standard greenhouse gas emission reports to the regulator, but they also highlighted the fact that they are the only company in the sector to take this a step further by tracking nearly every molecule of methane emissions (one of the components of greenhouse gas) emissions. I don't think the 5 score for environmental factors should preclude us from owning bonds."

FINANCIALS

"The action [to remove the CEO] also gives rise to corporate governance questions. There was clearly no external search for the most suitable candidate if the decision to remove the current (highly regarded) CEO was a strategic one. Additionally, given the unanimous nature of the board's decision, it is not clear if board representatives have taken part in the vote. If they did, it may have led to a potential conflict of interest."

Note: These quotes have been taken from internal credit analysts' notes, but have been edited for clarity.

CASE STUDIES IN RESPONSIBLE INVESTING

CASE STUDY: RESPONSIBLE INVESTING THROUGH ENGAGEMENT

A credit analyst at Insight engaged directly with a major listed company in 2017 to discuss a lack of transparency in its financial statements. The engagement led the company to provide more information. We provide the analyst's report below.

Summary: I engaged with the company during the year to gain clarification on some very large 'other' items in the financial statements that lacked disclosure. I persisted on the topic until I received a full explanation of the accounting mechanics across the financial statements.

1. **Risk identified**

   Very large 'other' items in the financial statements that lacked disclosure – these figures are in excess of the company's annual cash generation and relate to the financing of new vehicles.

2. **Action undertaken**

   I persisted on the topic until I received a full explanation of the accounting mechanics across the financial statements. Both the investor relations and treasury teams were unable to provide a correct explanation and I escalated until they provided a specialist from the finance team.

   To highlight the need to provide better disclosure I contacted leading sell-side analysts and challenged them to explain the accounting. When they couldn't they called the company.

3. **Reception from issuer**

   The investor relations team was very helpful and put in hours of work trying to understand/learn the accounting quirks that were taking place and ultimately arranged a conference call with members of the finance team who are responsible for the reported financial statements.

4. **Response from issuer**

   I was assured disclosure would improve.

   They admitted that as the company's financial service business has grown, disclosure in the financial statements to explain the interaction with the industrial operations has somewhat lagged. Market concerns over risks in the leasing book has brought reporting here into focus.

5. **Impact on your work**

   Understanding the mechanics of these large 'other' items allowed me to calculate estimates for potential impact under various scenarios; this got me comfortable with the risks to the company's cash flow and I followed by moving the company to an overweight rating.

CASE STUDY: ESG FACTORS INFORMING OUR ANALYSIS

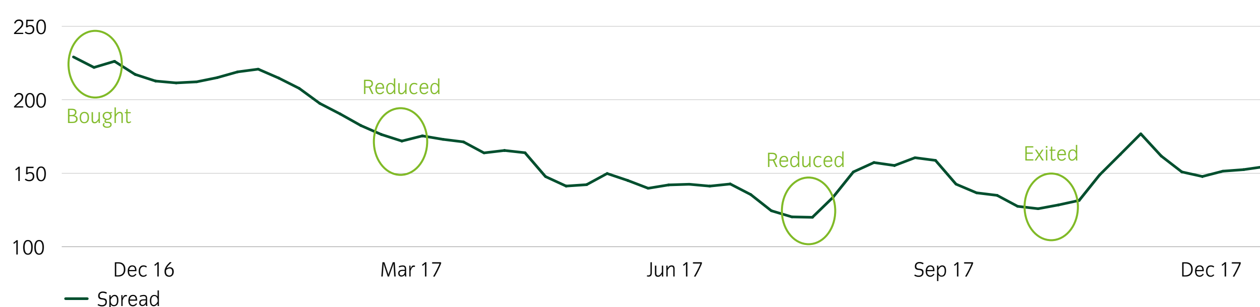
Consumer non-discretionary issuer (investment grade)

A company in the consumer non-discretionary sector brought a new issue to the market in November 2016. Our credit analyst highlighted ESG issues, scoring a 5 (the worst possible ESG rating), with particular concerns around corruption and product quality breaches. Partly as a result of this score, the issue was not deemed suitable for our long-term buy-and-maintain portfolios.

However, for our active portfolios, because the bonds had an investment grade rating but were priced as a high yield BB-rated issue, we believed the potential upside in terms of short-term investment return potential outweighed the likely material impact of a weaker ESG profile. After our investment, the bonds rallied. This meant that financial and non-financial risks – including ESG risks – were no longer priced into spread levels, and we sold down the bonds.

Spreads subsequently widened, driven both by weakness in the generic pricing environment and the issuer becoming embroiled in price fixing allegations, which could lead to material fines.

Figure 14: Spread of the company's bonds over government bonds[14]



CASE STUDY: ESG FACTORS DRIVING AN INVESTMENT DECISION

Retail issuer (investment grade)

An investment-grade global retailer came to the market with a new issue in 2017. There was strong demand for the bond, but during the due diligence process our analyst identified several credit and business risks:

- The issuer had a very complex corporate structure
- The bond was issued from a regional entity, while the financial statements were for the group as a whole
- The regional issuing entity did not have access to the cash flow or assets of other entities
- The issuer was listed in an arguably unstable emerging market

These risk factors showed the prevalence of accounting and governance risks with the new bond. The analyst therefore recommended avoiding buying the new issue.

In late 2017, significant accounting irregularities were reported, but not detailed. Credit ratings agencies materially downgraded the company from investment grade to high yield, and the issue from 2017 has lost around almost half its value.

[14] Source: Bloomberg, Insight Investment. As at 2 December 2017.

OTHER EXAMPLES

In 2017, several issues were either sold from, or placed on hold for, our buy-and-maintain portfolios largely as a result of ESG factors. A selection of these is provided in the table below (1 = best possible score; 5 = worst possible score).

Figure 15: Selection of changes to Insight's buy-and-maintain portfolios due to ESG factors[15]

Company	Date	Overall ESG	E	S	G	Comment
Industrials	11/08/2017	4	1	5	3	Long-standing weaknesses in governance (founder-control, entrenched board, related party transactions) and on social issues (labour rights and supply chain controversies). These practices have not been addressed and could have a material financial impact. The company has decided not to insure against cyber-attacks despite falling victim this year. Engagement with management regarding our ESG concerns has been difficult.
Consumer discretionary	28/06/2017	3	2	4	3	Poor disclosure – no audited breakdown of financial statements, poor governance, high recall costs, with product safety and quality in the bottom quartile for the sector. It also has one of the highest exposures to leasing in its sector.
Utilities	28/06/2017	2	2	2	2	Elevated leverage, poor international investment track record and looming regulatory risk – a large portion of their regulated revenue is not regulatory-asset-based and could be scrapped at the next review (though not before 2020)
Consumer staples	28/06/2017	2	3	3	1	Rising sector-focused regulation expected to hit [Company] first and hardest
Healthcare	02/05/2017	3	2	3	3	With the CFO and CEO leaving the company, asset disposals now seem further away, none of which is supportive with the imminent launch of the expected approval and production of new products
Materials	29/03/2017	3	3	4	5	Rated bottom-quartile on corporate governance due to executive pay issues and significant votes against directors. Safety is also rated poorly. Added to the uncertainty around the merger and resulting capital structure, placed on Hold subject to review post-completion
Utilities	29/03/2017	5	4	4	3	More than half of the business is reliant on coal-based generation, leading it to be bottom-quartile for carbon emissions score. Of the 31 US utilities covered, the company scores second lowest on environmental issues.
Communications	29/03/2017	5	1	5	5	Bottom-quartile on corporate governance and human capital development. Concerns are that there is a clear pattern of behaviour by senior executives of the key operating companies that rules do not apply to them (sexual harassment issues), that financial settlements and other payments may have been hidden from investors, and that oversight by executives at the group level and by the board is weak (with the behaviour of execs at the operating company level being tolerated in the pursuit of profits).

[15] Source: Insight Investment.

FLEXIBILITY TO APPLY ESG OVERLAYS TO CORPORATE BOND PORTFOLIOS

INSIGHT CAN APPLY A WIDE VARIETY OF ESG OVERLAYS TO CORPORATE BOND PORTFOLIOS.

Typical overlays include:

1. **Exclusion screens:** Using criteria provided by clients to prevent investments in certain business activities, such as tobacco, weapons and alcohol.
2. **Norms screens**: Managing (reducing or eliminating) exposure to companies with past high-profile events that suggest they do not meet globally respected standards such as the UN Global Compact and those set out by the International Labour Organisation.
3. **'Best in class'**: Using ESG ratings to rank companies on their ESG performance, which can be used to identify leaders and tilt portfolios away from companies with the worst ESG performance and/or the highest ESG risks, and towards companies with the best ESG performance/the lowest ESG risks.
4. **Low carbon**: Identifying companies with poor carbon emissions performance or those demonstrating greater environmental risk, and using this information to reduce the carbon footprint of portfolios.
5. **Positive impact**: Tilting portfolios in favour of either individual bonds or corporate issuers that have a sustainability element. This includes green bonds and the UN SDGs. See page 51 for more information on our investments in green bonds.

© Image: *'Venus Phase Evolution'* by Roger Hutchinson (UK)
Insight Astronomy Photographer of the Year competition 2017

RESPONSIBLE INVESTMENT IN LDI

PENSION SCHEMES' LIABILITIES TYPICALLY STRETCH OVER MANY DECADES AND THEIR PRESENT VALUE IS DIRECTLY LINKED TO INFLATION, INTEREST RATES AND THE LONGEVITY OF THEIR MEMBERS. AN LDI SOLUTION INVESTS SOME OF THE PENSION SCHEME'S ASSETS TO HELP MANAGE THESE LIABILITY RISKS. PARTIALLY-FUNDED INSTRUMENTS, SUCH AS SWAPS AND REPO, ARE OFTEN USED TO PROVIDE INVESTMENT EXPOSURES WITHOUT A SUBSTANTIAL COMMITMENT OF INITIAL CAPITAL. HOWEVER, THEY INTRODUCE BANK COUNTERPARTY RISK.

As part of our stewardship responsibilities, Insight manages the risks associated with swaps and repo through counterparty selection and daily collateralisation, among other processes.

- **Counterparty selection**: Insight's Counterparty Credit Committee (CCC), chaired by Insight's Chief Risk Officer, oversees this process. The CCC was established to ensure that Insight exercises due care and diligence in the selection and monitoring of counterparties with whom Insight will deal as agent on behalf of its clients. A key facet of this is to monitor closely the creditworthiness and business strategies of such counterparties, which involves regular face-to-face meetings between the bank management teams and Insight's credit analysts, Insight's senior legal staff and members of Insight's executive management team
- **Daily collateralisation**: Insight is highly experienced at managing the risks associated with swaps and repo through counterparty risk management and collateralisation. Insight was one of the pioneers of LDI and from the outset, recognising its importance to clients, introduced the daily collateralisation of swap and repo positions. Previously, industry best practice had been for weekly or even monthly collateralisation which, in light of Lehman Brothers' failure, could have led to significant losses for pension schemes. As the credit quality of many banks has deteriorated following the global financial crisis, Insight has increasingly sought to protect its clients by further strengthening its daily collateral requirements and providing additional protections to clients

Insight has been vocal in lobbying for users of derivatives, including our clients with LDI mandates, in a world where regulators are pushing hard for clearing houses as a solution to help mitigate bank counterparty risk. While the use of clearing houses is supported by Insight, if the collateral deposited as margin is limited to cash, it is highly inefficient for pension schemes which typically operate with little cash, but tend to hold high quality assets such as government bonds.

Moreover, if interest rates were to rise sharply, to meet margin calls pension schemes could be forced to sell assets to raise cash, at a time when many other pension schemes and other investors were doing the same. This would have the effect of exacerbating downward movements in asset prices and, potentially, forcing pension schemes to liquidate assets in a falling market. We continued to actively lobby on this issue in 2017.

For more information on our efforts in this area, and other areas relevant to LDI, please see our section focusing on supporting sustainable financial markets (see pages 43 to 57).

RESPONSIBLE INVESTMENT IN EQUITIES/ MULTI-ASSET

MOST OF OUR EQUITIES EXPOSURE IS THROUGH DERIVATIVES, WHICH MEANS WE HAVE LESS ABILITY TO DIRECT AND CONTROL COMPANIES THROUGH VOTING. WE REVIEW A RANGE OF FINANCIAL AND NON-FINANCIAL FACTORS AS PART OF OUR INVESTMENT STRATEGY, AND THE EQUITIES TEAM ENGAGES DIRECTLY WITH COMPANIES WHERE THEY DEEM IT NECESSARY.

EQUITY INCOME PORTFOLIOS

Our voting activity relates to our equity income portfolios, and we consider relevant ESG issues in our voting decisions. Equity portfolios focus on UK issuers, where we believe there to be comparable and typically strong governance standards with sufficient regulatory oversight.

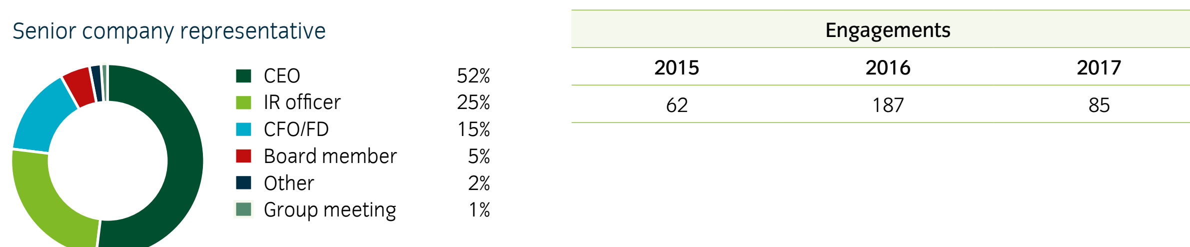
SPECIALIST EQUITIES PORTFOLIOS

For our specialist equities funds, where we hold ownership positions, we meet with companies to discuss investment risks and opportunities. (Over 90% of our holdings are via derivatives rather than shares.) These meetings involve a review of all salient business investment issues, including strategy, financial performance, and ESG factors where relevant.

Our investment focus is UK and European-listed entities and meetings are organised directly with companies or via their advisers.

For 2017, our Specialist Equities Team's engagement activities are shown in Figure 16.

Figure 16: Dialogue between Specialist Equities Team and company management in 2017[16]



Engagements		
2015	2016	2017
62	187	85

[16] Source: Insight Investment. As at 31 December 2017.

Figure 17: Specialist equities funds – voting on management resolutions in 2017

	Insight's vote			
Category	**For**	**Against**	**Abstain**	**Grand Total**
Auditor – Election	73			73
Auditor – Remuneration	66			66
Capital Structure	7			7
Change of Name	1			1
Directors – Discharge	2			2
Directors – Elect	656			656
Dividends	52		2	54
Environmental Practices	1			1
General Meeting Procedures	56			56
Issue of Shares & Pre-emption Rights	210		1	211
Meeting Formalities	2			2
Other A&R related	2			2
Other Articles of Association	11		2	13
Political Activity	48			48
Remuneration – Amount (Component, Individual)		1		1
Remuneration – Non-executive	8			8
Remuneration – Other	2		2	4
Remuneration – Policy (All-employee Share Plans)	4			4
Remuneration – Policy (Long-term Incentives)	5		11	16
Remuneration – Policy (Overall)	2		44	46
Remuneration – Report	6		63	69
Report & Accounts	73		1	74
Share Buybacks & Return of Capital	79			79
Transactions – Other	1			1
Transactions – Related Party	1			1
Transactions – Significant	4			4
Treasury Shares	1			1
Grand Total	**1373**	**1**	**126**	**1500**

MULTI-ASSET PORTFOLIOS

Insight's flagship multi-asset approach, the Insight broad opportunities strategy, dynamically invests across a wide range of asset classes.

The strategy seeks to generate long-term capital growth through a dynamic asset allocation strategy involving several asset classes (including equities, fixed income securities as well as commodities and property), primarily through investments in financial derivative instruments, in direct holdings and in collective investment schemes.

- **Fixed income**: ESG considerations arise indirectly through actively managed fixed income pooled funds managed by Insight that the strategy may have exposure to. ESG considerations are a key element of the research process underlying fundamental corporate bond evaluation processes, as described elsewhere in this report (see pages 25 to 27)
- **Derivatives**: Financial derivatives employed in the strategy provide indirect exposure to broad market indices within equities, fixed income, commodity and currency, resulting in no direct ESG considerations for the majority of the portfolio
- **Real assets**: As part of its real assets exposure, the strategy invests in listed closed-end investment companies with a focus on cash generative investments in social infrastructure, renewable energy and asset-backed aviation finance. We maintain regular contact with the companies as part of our ongoing monitoring and portfolio management. We also vote on our shareholdings which typically cover routine matters such as adoption of reports and accounts, appointment of auditors, election of members of the board and changes to capital base

Figure 18: Multi-asset holdings – voting on management resolutions in 2017

	Insight's vote			
Category	**For**	**Against**	**Abstain**	**Grand Total**
Auditor – Election	10			10
Auditor – Remuneration	8			8
Authorised Share Capital	1			1
Directors – Elect	49			49
Dividends	12			12
Issue of Shares & Pre-emption Rights	15			15
Other Articles of Association	2			2
Other Corporate Action	1			1
Remuneration – Non-executive	2			2
Remuneration – Policy (Overall)	1			1
Remuneration – Report	7			7
Report & Accounts	10			10
Share Buybacks & Return of Capital	8			8
Transactions – Other	1			1
Treasury Shares	1			1
Grand Total	**128**			**128**

KEY FOCUS: CLOSER LOOK AT REMUNERATION

Insight believes executive remuneration must balance long and short-term performance considerations. An effective and clear policy, along with an independent remuneration committee, is essential to ensure remuneration is aligned with and commensurate with performance.

Figure 19: Voting on remuneration in 2017

	Actual vote			
Res Cat	**For**	**Against**	**Abstain**	**Grand Total**
Remuneration – Amount (Component, Individual)	0	1	0	1
Remuneration – Non-executive	10	0	0	10
Remuneration – Other	2	0	2	4
Remuneration – Policy (All-employee Share Plans)	4	0	0	4
Remuneration – Policy (Long-term Incentives)	5	0	11	16
Remuneration – Policy (Overall)	3	0	44	47
Remuneration – Report	13	0	63	76
Total	**37**	**1**	**120**	**158**

RESPONSIBLE INVESTMENT IN FARMLAND

SINCE 2011, INSIGHT INVESTMENT HAS ADVISED ON INVESTMENTS IN FARMLAND. ASSETS IN THESE STRATEGIES ARE DIVERSIFIED BY REGION AND COMMODITY, AND THE MAIN LINES OF PRODUCTION CONSIST OF CASH CROPS (ROMANIA AND POLAND), BEEF CATTLE (AUSTRALIA) AND PASTURE-BASED DAIRY FARMS (NEW ZEALAND AND CHILE).

Since initial investment, the Farmland team has integrated ESG and sustainable and responsible investment (SRI) frameworks as a core part of the operating and development activities of the underlying assets. In this section we focus on three specific elements of this integration:

- Our approach to due diligence
- Examples of notable developments in 2017
- How our team sets management guidelines, supported by the SRI Committee

Also, we are in the process of ensuring the underlying entities are aligned with the UN SDGs and will evaluate relevant reporting against the SDGs in the future.

INSIGHT'S DUE DILIGENCE PROCESS

The ability of our farmland investments to farm sustainably in diverse geographies and product segments was the foundation for portfolio construction. This process includes a comprehensive assessment of unique comparative advantages of each product/ geography mix to design sustainable production systems entailing tailored best-in-class agricultural practices.

The due diligence process for farmland investments incorporates both desktop research and intensive on-site visits. The process assesses each potential investment against a variety of indicators – such as the quality of assets and infrastructure, the potential for productivity enhancement and/or development and industry viability – and includes environmental and other SRI considerations.

Focusing on environmental considerations, Insight is committed to undertake environmental due diligence on all the farming opportunities that we assess. This aspect of the due diligence process aims to identify relevant environmental issues and factors such as chemical storage; waste management; land use; water management; the implications for flora, fauna and their habitats of infrastructure development; the use or replacement of building materials such as asbestos; environmental incident analysis; and features on surrounding sites that may negatively impact the land investment being considered.

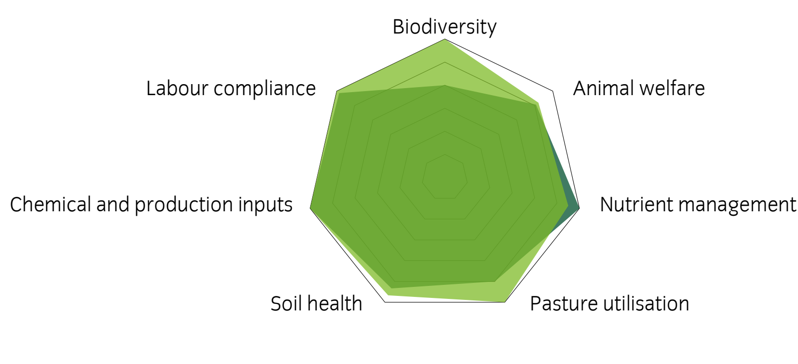
EXAMPLES OF NOTABLE DEVELOPMENTS IN 2017

Insight's existing farmland investments are diversified across commodities and geographies, with countries selected for sustainable comparative advantage in the production of target commodities. The core of Insight's approach has been based on Integrated Farm Management, a dynamic framework developed by Linking Environment and Farming, which aims to provide guidelines for effectively balancing the objectives of productivity and profitability with environmental considerations.

The guidelines provide desired practices across a range of activities that are intrinsic to farming. These include approaches to soil management, animal welfare, waste disposal, community and labour relations, and energy efficiency.

The most significant changes in 2017 are highlighted in Figure 20.

Figure 20 – RI improvements in 2017[17]



Notable achievements include:

- **Cropping** – an increase in biodiversity by introducing and increasing the numbers of crops grown, including cover crops for soil health management; investments in seeding and tillage machinery to increase the effectiveness of cultivation; reduce soil disturbance; and increase efficiency of fuel and energy use
- **Livestock** – an annual pasture management and monitoring report for the Tanumbirini station in the Northern Territory of Australia highlights continuing improvements in plant, animal and bird biodiversity, and pasture condition across the properties. A noteworthy development was the sighting and photographing of rare and endangered species of birds never recorded previously on these properties, including the Gouldian finch and the purple-crowned fairy-wren among the 111 recorded bird species

The examples above demonstrate Insight's considered approach to adopting suitable and conservationist systems relevant to a wide-range of farmland types and ecosystems. Insight achieves this by continually seeking to identify best practice on a global basis, taking input from local management and working with independent specialists.

Some other examples include:

- **Biodiversity** – improvements in farming systems in Romania, improved pasture and livestock management in Australia
- **Animal welfare** – continues to be a focus, with improvements in Chile and New Zealand in the dairy herds, but weaning percentage continues to be a challenge in Australia
- **Nutrient management** – overall good steady state soil nutrient status in most locations, however an updated effluent management regulatory requirement has necessitated a change in the license approval in New Zealand
- **Pasture utilisation** – increasing management skills in Chile continue to give better utilisation results
- **Soil health** – overall good steady state soil nutrient status as shown in soil testing across all locations where samples are taken;
- **Chemicals and other production inputs** – continued adoption of farming systems techniques and rotations in Romania drive consistent good outcomes
- **Labour compliance** – no labour issues noted with continued compliance with regulatory frameworks in all jurisdictions

Figure 21 – Example indicators used[17]

Categories	Example indicators			
Biodiversity	Pasture monitoring report	Crops grown		
Animal welfare	Body condition score	Calving percentage	Mortality rate	Animal condition
Nutrient management	Effluent management	Units N deployed	Soil testing	Licence regulatory review
Pasture utilisation	Grass consumed	Feed budget		
Soil health	Soil sampling	Tillage passes		
Chemical and production inputs	Inputs applied	Yield		
Labour compliance	Anti bribery and corruption	Health and safety	Labour relations review	

[17] Source: Insight Investment. Scores range from 1 to 3 with 0.5 scale on graph – values are weighted averages for each category.

MANAGEMENT GUIDELINES AND THE SRI COMMITTEE

Insight's farmland management team comprises experienced members with an industry track record of performance and involvement in global best practice. The team is supported by an external SRI Committee.

The SRI Committee was established to provide the investment team with an external source of information and research on best practice in sustainable farming techniques. It comprises individuals with expert knowledge of the issues highlighted above to seek their advice and guidance on relevant issues where necessary.

Through understanding the variety of industries and environments in which the underlying businesses are operating, a range of policies have been established/adopted to clearly state the fund's management strategy. Examples of key management policies that local operating entities will have in place are:

- The use of hormonal growth promotants (HGPs)
- The use of recombinant bovine somatotropin (rBST)
- The treatment of bobby calves
- Policy on controlled burning and fire

We work with local management to conduct regular training courses to ensure the key tenets of this responsible investment approach are adhered to.

In addition to operational policies and practices, we also consider higher-level ESG factors, such as:

- Operational health and safety
- Anti-bribery and corruption
- Business ethics and code of conduct

As a recurring matter and to ensure highest industry standards are reflected, we conduct internal audits across all policies and procedures of the investments to ensure corporate compliance requirements and local regulations are met. Insight continues to engage with external agencies and local/global consultancies to redirect and support an approach which aligns with both the SDG and the needs of the stakeholders.

© Image: *'Hustle and Peaceful'* by Prisca Law (China)
Insight Astronomy Photographer of the Year competition 2017

SUPPORTING SUSTAINABLE FINANCIAL MARKETS

As a global asset manager, we have an important role in financial markets. We believe that we must take a proactive role in ensuring the long-term sustainability of the markets – this is in our clients' long-term interests, as well as that of wider society.

Long-term initiatives include:

- Active engagement with other industry members to ensure our clients' rights and considerations are fully represented, including joining the Working Group on Sterling Risk-Free Rates (see page 45)
- Development of new sources of repo liquidity – a key issue for pension funds seeking to manage risk efficiently and effectively (see page 47)
- Challenging the pressure on derivatives users, including pension funds, to post only cash as variation margin on their derivatives transactions – a key issue for pension funds seeking to manage risk effectively over the long term (see page 48)
- Supported the transition to a low carbon economy by investing in 43 green bonds, and encouraging banks to consider green bond issuance (see page 51)
- Collaboration with peers on a range of issues, such as a new engagement on cybersecurity initiated by the PRI (see page 57)

ENGAGEMENT ON RISK-FREE RATES

ON 27 JULY 2017, ANDREW BAILEY, CEO OF THE FINANCIAL CONDUCT AUTHORITY (FCA), GAVE A SPEECH ON THE FUTURE OF THE LONDON INTERBANK OFFERED RATE (LIBOR). HIS SPEECH WAS INTERPRETED AS IMPLYING THAT LIBOR, IN ALL CURRENCIES AND TENORS, WILL BE PHASED OUT BY THE END OF 2021. THE MAIN CONCERN OF THE FCA IS THAT THE UNSECURED LENDING MARKET ON WHICH LIBOR IS BASED IS NO LONGER SUFFICIENTLY ACTIVE. THE FCA THEREFORE BELIEVES THAT IT NEEDS TO ENCOURAGE MARKET PARTICIPANTS TO UNDERTAKE THE WORK REQUIRED TO MOVE TO ALTERNATIVE INTEREST RATE BENCHMARKS.

There is much ongoing work in relation to the future of lending rates – reviews of (and changes to) overnight rates, as well as term rates, are occurring in most major markets. While it is too early to assume knowledge of the outcome, we are reviewing the potential impacts on our clients' portfolios so we can plan how best to adapt to any change and help clients with any decisions they need to take.

We have identified the following four key areas in which benchmark interest rates have a bearing on our clients' mandates:

- **Derivative instruments** with a floating-rate leg (e.g. swaps with Libor or Sterling Overnight Index Average (Sonia) obligations)
- **Floating rate physical debt assets** (e.g. loans and asset-backed securities with Libor-linked coupons)
- **Benchmarks** for money market, absolute return and other 'cash-plus' strategies
- **Discount rates** for the benchmarks of liability hedging mandates

Insight is engaging with other industry members to ensure that our clients' rights and considerations are fully represented as the market evolves. **This includes joining the Working Group on Sterling Risk-Free Rates**, following the announcement by the Bank of England and the Financial Conduct Authority that they were extending the membership of the group to include investment management firms.

© Image: *'The Blue Hour'* by © Tommy Eliassen (Norway)
Insight Astronomy Photographer of the Year competition 2017

ALTERNATIVE SOURCES OF REPO LIQUIDITY

LIQUIDITY IN THE GILT REPO MARKET – TRADITIONALLY SUPPLIED BY BANKS – HAD SHRUNK IN RECENT TIMES LEADING TO INCREASED COSTS. THIS HAD FUELLED CONCERNS AMONG SOME INVESTORS WHO USE GILT REPO TO MANAGE RISK AS PART OF AN LDI STRATEGY. INSIGHT HAS DEVELOPED SEVERAL APPROACHES TO TACKLE THIS ISSUE, HELPING IMPROVE GILT REPO LIQUIDITY IN 2017.
THESE INITIATIVES INCLUDED:

- **New sources of liquidity:** We reached agreement with major clearing houses, including LCH.Clearnet, to provide liquidity for repo for a number of major clients. In addition, in 2017 we pioneered access to LCH RepoClear for pension fund clients. RepoClear matches some €13trn of gross notional repo and cash bond trades per month.[18] We expect our clients will have access to substantially greater repo liquidity and benefit from cheaper trading costs when they gain access to the platform.
- **New repo facility:** We built on our innovative approach to sourcing liquidity for gilt repo by introducing a new government liquidity vehicle. Drawing on our experience and expertise in the fixed income, LDI and derivatives markets, this new approach provides sterling corporate cash investors with a cash vehicle offering security, daily liquidity and a yield comparable to a prime money market fund.

  The security is achieved by the gilt collateral which is provided by UK defined benefit pension schemes who trade repo with the vehicle. It also provides cash investors an alternative to investing in banks and money market funds, both of which are under pressure in light of new European Union money market fund regulations finalised in 2017.

  The new approach provides an alternative source of repo liquidity for UK pension funds, reducing the cost of repo funding. At the time of writing, over 40 UK pension scheme clients trade gilt repo using this structure. The assets managed grew materially over the year under review: since launch the structure has grown to over £2.5bn in size.

© Image: *'In Autumn Dance'* by © Kamil Nureev (Russia)
Insight Astronomy Photographer of the Year competition 2017

[18] For more information, please see: https://www.lch.com/services/repoclear/repoclear-ltd

ENGAGEMENT WITH EUROPEAN UNION ON CASH-ONLY VARIATION MARGIN

THERE IS AN EMERGING CONSENSUS THAT USERS OF DERIVATIVES, INCLUDING PENSION FUNDS SEEKING TO PRUDENTLY MANAGE THEIR RISKS, SHOULD USE ONLY CASH TO COVER MARGIN CALLS. THIS PRESENTS SIGNIFICANT ISSUES FOR INVESTORS, INCLUDING OUR CLIENTS WITH LDI MANDATES, LEADING US TO CHALLENGE THIS CONSENSUS.

In our opinion, the significant push by banks to improve their capital position by rejecting the efficiencies of cash and gilt-collateralised bilateral trading, and the acceptance of this stance by some asset managers, introduces additional risks into pension portfolios. We believe there is significant potential value for pension funds in keeping their options open, especially when regulation is still under review.

THE EVOLUTION OF DERIVATIVES MARKETS

In the early days of LDI, derivative dealing was relatively straightforward, characterised by liquid markets, keen banks and a high degree of consistency in the approaches adopted across the industry. Those days are long gone.

Whereas cash and gilt-collateralised bilateral derivatives were overwhelmingly the norm across the LDI industry, more recently, banks have sought to incentivise cash-only collateralisation and cleared derivatives as a way to improve the efficiency of their own balance sheets. Pension funds are not subject to the same rules and have a choice to make amongst a variety of trading venues, including:

- Cash and gilt-collateralised bilateral derivatives
- Cash-collateralised bilateral derivatives
- Cash-collateralised cleared derivatives

No single trading venue is capable of simultaneously meeting all requirements for all pension funds. For example, cash collateralisation is preferred by banks, but cash-only collateralisation and clearing can introduce significant additional costs and tail risks into pension portfolios (see Figure 22). Therefore, any blanket decision in favour of any one trading venue is unlikely to be the right decision for all trades, especially whilst some key regulatory matters (such as the extension of the exemption from mandatory clearing for European pension funds) are still under review. In our view, one size does not fit all.

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Insight Astronomy Photographer of the Year competition 2017

WHAT IS THE ALTERNATIVE?

Insight can help pension funds adopt what we believe to be a better approach:

- Maintain access to all viable trading venues; don't be forced down a single path
- Assess the cost and risk implications of clearing and cash collateralisation, and put in place the necessary safeguards
- Use a suitable blend of trading approaches to manage cost, risk and collateral considerations

In order to provide pension funds access to trading efficiency, liquidity, collateral adequacy benefits and avoid significant potential pitfalls and risks, we believe pension funds should adhere to the following guidelines:

- Preserve the credit and collateral terms applicable to existing positions (i.e. on positions in place before the European Market Infrastructure Regulation rule change on 1 March 2017)
- Negotiate the ongoing ability to post gilts and cash as collateral with as many counterparties as possible (if this is not possible, a transitional arrangement to post gilts is more favourable than a move to cash-only collateralisation immediately)
- Maintain access to cash-collateralised bilateral agreements with remaining counterparties as well as to cleared derivatives in order to maximise flexibility and access to liquidity
- Put in place measures to monitor any additional risks arising from cash collateralisation and clearing member dependency, and address as many of these as possible ahead of time (e.g. by seeking contractual protections around porting of positions to another clearing member if the need arises)

INSIGHT'S ONGOING ACTIVITY

We continue to engage with policymakers to address the root causes behind the increased capital burden and costs banks face as they trade with pension funds. Quite simply, we believe the systemic stability being pursued by the policymakers can be achieved without adversely impacting pension funds. Policymakers are increasingly aware of the disadvantages associated with requiring pension funds to post cash collateral, for example, and Insight is actively engaged with the relevant bodies to argue the case on the behalf of pension funds.

We believe there is significant potential value for pension funds in retaining the ability to collateralise with gilts. This is particularly relevant when regulation is still under review and moving to cash collateralisation may not be enforced in the future.

Figure 22: Pros and cons of different derivative trading venues

Venue	Pros	Cons
Cash and gilt-collateralised bilateral	Best long-term hedging approach due to the collateral flexibility it affords and the compatibility with pension fund investment strategies which typically have high allocations to gilts	Bank regulations and capital rules are making this route less capital-efficient from the perspective of banks
Cash-collateralised bilateral	Lower initial trading costs	Introduces the requirement to hold a large cash balance or risk needing to source cash collateral at times of market stress
Clearing	Lower initial trading costs (counterbalanced by the fact that inflation hedge pricing might be more expensive in clearing due to the one-way nature of this market)	Least efficient from a collateral perspective. Introduces the requirement to hold a large cash balance or risk needing to source cash collateral at times of market stress Clearing member related costs and risks: • Exposure to the risk of clearing member exercising their right to terminate • Clearing member credit exposure • Collateral segregation • Inferior protections for pension funds in the event of clearing member default • Higher ongoing costs

SUPPORTING THE TRANSITION TO A LOW-CARBON ECONOMY

WE HAVE IMPLEMENTED OR PARTICIPATED IN A NUMBER OF INITIATIVES THAT REFLECT THE LONG-TERM TRANSITION TOWARDS A LOW-CARBON ECONOMY.

CLIMATE ACTION 100+

Insight signed the Climate Action 100+ initiative, an investor initiative encouraging corporate environment disclosure in line with the TCFD recommendations.

The initiative involves about 225 global investors, with a combined $26trn under management, who have come together in the short time since the invitation was issued in September 2017. Entities backing the project include the Swedish AP buffer funds, many of the UK's local authority schemes, and some of the most influential Australian, Canadian and US public pension funds. Coordinators include the Institutional Investors Group on Climate Change (IIGCC), the Investor Group on Climate Change (IGCC), and the Principles for Responsible Investment (PRI).

To participate, investors must commit to pursuing at least one engagement each year with at least one company on the focus list. Insight will work with other investors targeting three of the focus companies.

What are investors asking companies to do?

Investors supporting the initiative will be requesting the boards and senior management of companies to:

1. **Implement a strong governance framework** which clearly articulates the board's accountability and oversight of climate change risks and opportunities
2. **Take action to reduce greenhouse gas emissions across the value chain**, consistent with the Paris Agreement's goal of limiting global average temperature increase to well below two degrees Celsius above pre-industrial levels
3. **Provide enhanced corporate disclosure** in line with the final recommendations of TCFD and, when applicable, sector-specific Global Investor Coalition on Climate Change Investor Expectations on Climate Change. These disclosures should provide sufficient information to enable investors to assess the robustness of companies' business plans against a range of climate scenarios, including well below two degrees Celsius, and to improve investment decision-making

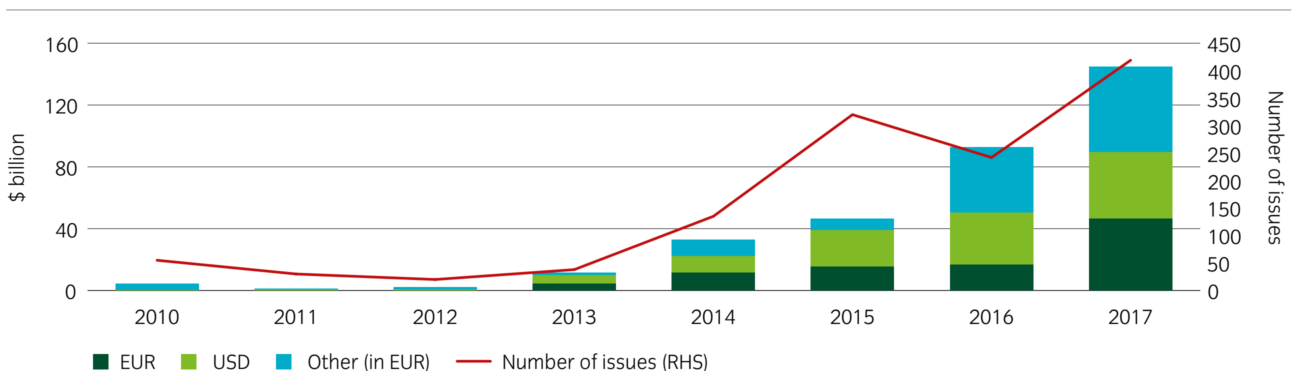
In 2017, Insight added more green bonds to portfolios than in any previous year

INVESTMENT IN GREEN BONDS

In 2017, Insight added more green bonds to client portfolios than in any previous year – 43 in total (see Figure 24 overleaf). This was helped in part by increased issuance of green bonds. This included government issuance for the first time: green French government bonds were issued – marking the largest green-bond issuance ever at nearly €10bn.

In line with the overall green bond market, most green bonds added to Insight's portfolios were from utilities and financials. Utility issuance is often used to for financing the development of renewable energy projects such as wind and solar. Financials have generated significant growth in issuance, and the proceeds are used for supporting the development of loans to eligible businesses that meet green bond framework requirements.

Figure 23: Growth of the global green bond market[19]



© Image: *'Auroral Crown'* by Yulia Zhulikova (Russia)
Insight Astronomy Photographer of the Year competition 2017

[19] Source: Bloomberg. As at 31 December 2017.

Figure 24: Green bonds held and/or added to Insight portfolios in 2017[20]

Issuer	Currency	Country	Sector	Use of proceeds
Banco Nacional de Costa Rica	USD	Costa Rica	Financials	Environment projects
BNP Paribas SA	EUR	France	Financials	Environment projects
BPCE SA	EUR	France	Financials	Environment projects
BRF SA	EUR	Brazil	Consumer Staples	Energy efficiency projects
Covanta Holding Corp	USD	United States	Industrials	Waste-to-energy development projects
Electricite de France SA	EUR	France	Utilities	Renewable energy projects
Electricite de France SA	USD	France	Utilities	Renewable energy projects
Enel Finance International NV	EUR	Netherlands	Utilities	Renewable energy projects
Engie SA	EUR	France	Utilities	Renewable energy projects
Fonciere Des Regions	EUR	France	Financials	Sustainable real estate development
French Republic Government Bond OAT	EUR	France	Government	Six broad sectors
Gas Natural Fenosa Finance BV	EUR	Netherlands	Utilities	New renewable energy generation
Iberdrola Finanzas SA	EUR	Spain	Utilities	Renewable energy projects
Iberdrola International BV	EUR	Netherlands	Utilities	Renewable energy projects
ICADE	EUR	France	Financials	Renewable property development
ING Bank NV	EUR	Netherlands	Financials	Renewable energy projects
innogy Finance BV	EUR	Netherlands	Utilities	Renewable energy projects
Intesa Sanpaolo SpA	EUR	Italy	Financials	Environment projects
Kaiser Foundation Hospitals	USD	United States	Health Care	Building efficiency
Kreditanstalt fuer Wiederaufbau	USD	Germany	Government	Sustainable energy
MidAmerican Energy Co	USD	United States	Utilities	Wind energy
National Australia Bank Ltd	EUR	Australia	Financials	Energy and transport projects
Orsted A/S	EUR	Denmark	Utilities	Renewable energy
Paprec Holding SA	EUR	France	Industrials	Recycling
Skandinaviska Enskilda Banken AB	EUR	Sweden	Financials	Low-carbon projects
Societe Generale SA	EUR	France	Financials	Renewable energy projects
Southern Power Co	EUR	United States	Utilities	Renewable energy generation
SSE PLC	EUR	Britain	Utilities	Onshore wind farms
Swedbank AB	EUR	Sweden	Financials	Property and renewable energy
TenneT Holding BV	EUR	Netherlands	Utilities	Wind energy
Unibail-Rodamco SE	EUR	France	Financials	Sustainable real estate development
Vornado Realty LP	USD	United States	Financials	Sustainable real estate development
Westpac Banking Corp	EUR	Australia	Financials	Energy, property and transport projects

[20] Source: Insight Investment. As at 31 December 2017. This is not a comprehensive list.

GREEN BONDS: ISSUES TO CONSIDER

We remain cautious of the risks inherent within the green bond market. We believe there are three important matters for investors to consider.

- **Unclear definition:** Despite more than 150 corporate bond issues, we still do not have a universally agreed definition of 'green'. The transition to a low-carbon economy is happening quickly and energy companies need to be part of that change. However, when balancing the positive (carbon reduction) and negative (continued carbon output) factors, investors can find it difficult to assess the merits of any green bond.

  Most hold that it is positive for energy companies to reduce their carbon externalities, and any attempt to reduce emissions validates a green bond issuance. Other arguments posit that companies issuing green bonds must make an overall environment commitment with stretched targets and clear decarbonising strategy to reduce emissions. Insight holds the latter view
- **No global standard:** We believe we have reached a tipping point where the lack of an enforced global standard for green bonds may limit the market. If a company's overall economic and business model remains largely unchanged, as is widely accepted is the current case with most energy companies, and investors cannot identify commonly-agreed green bonds from others, they may discount them all, thereby limiting the flow of capital into these areas. There is also concern from Insight that bonds are being labelled as green simply to meet demand from institutional investors, even if the activities being financed cannot really be considered as green. For example, green bond proceeds have been used to build airports and car-parks
- **Mixed suitability for green portfolios:** Carbon-intensive energy companies need to improve their carbon performance, but issuing green bonds (for carbon efficiency) does not necessarily make them suitable for green bond funds and strategies. Energy companies, especially those operating in Europe, face significant regulatory and technological challenges, with limited alternative power businesses, and probably do not meet the 'impact' needs of most green investors. Additionally, clients' portfolios may still have significant exposure to carbon-emitting activities and are also subject to credit risks from factors including climate regulation and 'stranded assets'

Investors want to put money to good use and green (and increasingly social) labels are an easy way to build sustainable goals into portfolios. But Insight encourages caution. Green bonds cannot replace fundamental, including environmental, analysis for mainstream investors.

ENGAGING WITH BANKS ON GREEN BONDS

In 2017, we wrote a letter to 28 banks across developed and emerging markets, including fixed income issuers to which we have long-standing material exposure, through to newer issuers or those to which we have less exposure. The letter aimed to encourage banks to consider green bond issuance.

The banks' replies revealed that some have made some progress towards issuing green bonds, while others are only beginning to consider such issuance – or have not done so at all.

BANK ENGAGEMENT LETTER – GREEN BOND FRAMEWORKS

Dear [XXXXX],

The finance needs for a successful transition to a low-carbon economy are estimated at $5-7trn*. Commercial banks, like asset managers, are critical intermediaries and face increasing scrutiny from regulators, clients and the public on how they contribute towards this transition.

Insight Investment is a UK-based investment manager investing on behalf of pension funds, governments, insurers and corporations responsible for more than $700bn in assets.**

As investors in XX's bonds, we would like to encourage you to develop a strategy for issuing green bonds and implement a framework for using the proceeds of green bonds. The mobilisation of more environment-focused debt and loans will help shift the global economy to a more sustainable path.

Insight currently owns green bonds in a number of credit portfolios. Insight would in principle be interested in adding XX green bonds to its investment portfolios.

What are green bonds?

In 2013, Bank of America became the first corporation to issue a green bond. Since then, a number of large financial institutions have followed, including ABN AMRO, BNP Paribas, Morgan Stanley and Nordea Bank.

The proceeds of green bonds are used to finance eligible businesses and projects that promote a sustainable economy, including:

- Renewable energy
- Energy efficiency
- Efficient buildings
- Waste management
- Efficient land use
- Clean transportation
- Water management
- Climate and weather adaptation
- Pollution prevention and control

Why are banks important?

The evidence for a warming climate system is unequivocal and that anthropogenic drivers are likely the main cause. Banks will have a critical role promoting and supporting a wholescale financing of businesses and industries that will be key to meeting the low-carbon economy challenge.

* Based on meeting the global sustainability challenge presented by the UN Sustainable Development Goals (UNEPFI).
** As at 30 June 2017. Assets under management (AUM) are represented by the value of cash securities and other economic exposure managed for clients. Reflects the AUM of Insight, the corporate brand for certain companies operated by Insight Investment Management Limited (IIML). Insight includes, among others, Insight Investment Management (Global) Limited (IIMG), Insight Investment International Limited (IIIL), Cutwater Asset Management Corp (CAMC), Cutwater Investor Services Corp (CISC) and Insight North America LLC (INA), each of which provides asset management services. FX rates as per WM Reuters 4pm Spot Rates.

There are two primary risks to banks from climate change: physical risk and transition risk. Physical risks, such as climate and weather-related events, may potentially result in large financial losses, reduce the value of assets and increase credit risks. Transition risks are the costs borne from rapid changes in policy, technology or market sentiment from the process towards a low-carbon economy. The scale of transformation is significant, and is estimated at $90trn by 2030.[***]

Regulators and oversight bodies, including the FSB, the EU and Bank of England, are taking steps or discussing how to ensure banks meet their low-carbon responsibilities. Governments are working on national climate impact reduction plans, which will likely be supported by primary legislation. The transition away from fossil fuels will create many new businesses opportunities. Likewise, there are real financial risks, including declining corporate activity and aggressive policy action.

What are the benefits to issuing a green bond?

XX's sustainable programme shows the bank is committed to following best practice economic, social and environment policies.

While a relatively new market solution, green bonds are effective in directing finance towards industries in a low-carbon economy. Green bonds can affirm XX's commitment to support a low-carbon future; meet your social responsibility to help nascent or established businesses build a strong market position; and align with your public-good mandate.

A green bond framework will help XX build and grow internal expertise that will place the bank in a strong position to meet unknown regulatory challenges associated with climate change. Banks' exposure to climate risks is well-known and a green bond framework will enable the bank to measure and monitor risk and realise commercial opportunities. This is vital to managing long-term risks associated with climate change.

We are seeing significant market demand for green bonds, especially from institutional investors. Insight is managing large investment strategies that stipulate increasing exposure to green bond issuance. Your decision to issue green bonds has the potential to be positive for our clients, the fledgling green bond market, and your brand as prudent risk managers and industry leaders.

Next steps

Insight encourages XX to start planning for its first green bond issuance.

We encourage building specialist units or using existing teams to:

- Develop a green bond framework
- Identify opportunities with existing clients
- Develop risk frameworks around climate change
- Monitor for global regulatory changes
- Report on green bond use of proceeds

A green bond evaluation and reporting process will ensure that investors can measure the impact of green bonds and the effectiveness of your green bond framework. We encourage you to be fully transparent with your green bond activities, in keeping with best practice.

Insight would be happy to discuss developing a green bond process in more detail. We would like to learn more about your plans and encourage you to meet the leadership standards already pursued by some of your peers.

We look forward to hearing from you on how you expect to start issuing green bonds.

Yours sincerely,

[XXXXXX]

[***] Global Commission on the Economy and Climate.

SAMPLE RESPONSE FROM AN EMERGING MARKET BANK

Dear [XXXXX],

Many thanks for your letter and for detailed explanation of the green bonds importance to your business. We have taken a firm notice on Insight Investment interest to expand its green bonds portfolio and would like to update you on the situation within [our company] in this respect.

Frankly speaking we have not yet started to think about a potential green bond issuance. The main reason for that is not at all related to any underestimation of the problems of climate change, environmental protection, energy saving, etc. The answer relates more to the absence of needs for long USD liquidity. As you may recall from our meeting in London at JPM conference, in 2017 we've faced rather limited demand for long term loans in USD. As such there was no obvious need for us to issue plain vanilla USD denominated senior eurobonds on behalf of the bank. Since for quite some time there were no plans for any senior bond offerings, there were no plans for green bonds as well.

However we will revise the existing loan portfolio and look whether we've financed any companies \ projects in the areas you've indicated as eligible for green bonds - renewable energy, etc, we'd analyse whether it could make sense to refinance them out of bond proceeds. Needless to say that we'll keep in mind that should we consider a new project in one of the eligible areas, we may also contemplate this kind of financing. Having said that I can summarize that we may be close to a debut green bond issuance in 2018 or even later…

With best regards,

[XXXXX]

INDUSTRY ENGAGEMENT ON RELEVANT ISSUES

WE PARTICIPATED IN A RANGE OF COMMITTEES AND OTHER PROJECTS RUN BY THE UN-SUPPORTED PRI OVER THE YEAR.

CYBERSECURITY

In 2017, Equifax announced a cybersecurity breach. Criminals had accessed over 145 million US consumers' personal data, including their full names, Social Security numbers, credit card information, birth dates, addresses and, in some cases, driver license numbers.

There were dozens of cyber-attacks in 2017 affecting a range of businesses, from technology to consumer firms of all sizes and with various degrees of sophistication. The impact for companies often remains unknown – sometimes for years – until they are uncovered and reported to authorities. The breaches have the potential to be material for companies' reputations and costly in terms of remediation activity and upgrading systems.

Following this emerging threat, Insight joined a new collaborative initiative on cybersecurity initiated by the PRI.

Cybersecurity is an emerging risk for all businesses, particularly those that manage sensitive data. High profile data breaches in recent times have put the spotlight on companies' preparedness and readiness to respond to an attack. The engagement aims to:

- Build investors' understanding on how companies are positioned in terms of their policies and governance structures to demonstrate cyber resilience
- Seek improvements on the level of company disclosure on cyber risks and their management

Insight will take the lead in engaging with an international pharmaceutical company as part of this initiative.

Separately, in 2018, Insight will commence discussions with select financial institutions on their preparedness on cyber risks. This is independent of the PRI initiative described above, and is aimed at enabling us to inform ourselves of the risks and to compare the companies we invest in to generate a sense of 'best practice'.

CREDIT RATINGS

The PRI's ESG in Credit Ratings Initiative aims to enhance the transparent and systematic integration of ESG factors in credit risk analysis. As global bonds outstanding have hit US$104.8bn[21], and fixed income instruments are by far the largest asset class globally, it is important to understand how ESG factors can affect the default risk of a bond issue or its issuer.

Insight is a member of the Advisory Committee on Credit Ratings (PRI working group).

The first report produced by the Committee, Shifting perceptions: ESG, credit risk and ratings – part 1: the state of play, outlines how investors and credit rating agencies are paying heed to ESG factors in credit risk analysis. The report concludes that investors and credit rating agencies are ramping up efforts to consider ESG factors in credit risk analysis (available at www.unpri.org).

To address some of the disconnects between investors and credit rating agencies that have emerged so far, the PRI is organising roundtables around the world aimed at credit risk analysts, fixed income portfolio managers and strategists. Credit rating agencies' representatives will participate to explain how they incorporate ESG factors in their credit ratings and to answer any questions attendees may have. The season began with a panel session in September 2017 at the PRI in Person event in Berlin focused on ESG factors in sovereign credit risk, with speakers from Beyond Ratings, Global Evolution, the French Treasury and Moody's Investors Service. Insight hosted the London forum in November, the conclusions of which will be reflected in a report set to be published later in 2018.

[21] Source: Bloomberg. As at 31 December 2017.

APPENDIX I. VOTING COMMITMENT

WITH RESPECT TO SHARE OWNERSHIP, IN THE MAJORITY OF THE CURRENT EQUITY INVESTMENT STRATEGIES INSIGHT DOES NOT HAVE MATERIAL INVESTMENTS IN PHYSICAL HOLDINGS. WHERE INSIGHT DOES HOLD PHYSICAL EQUITY POSITIONS WE ROUTINELY VOTE ON BEHALF OF OUR CLIENTS WITH REGARD TO THE UK COMPANIES IN WHICH THEY HAVE A SHAREHOLDING.

Insight retains the services of a third party for proxy voting services and votes at all meetings where it is deemed appropriate and responsible to do so. The third party provider offers research expertise and voting tools through sophisticated proprietary IT systems allowing Insight to take and demonstrate responsibility for voting decisions. Independent governance analysis is drawn from thousands of market, national, and international legal and best practice provisions from jurisdictions around the world.

Independent and impartial research provides advance notice of voting events and rules based analysis to ensure contentious issues are identified. The third party provider analyses any resolution against Insight -specific voting policy templates which will determine the direction of the vote. Where contentious issues are identified these are escalated to Insight for further review and direction. Insight will undertake a review of the voting policy templates on an annual basis.

APPENDIX II. WEAPONS POLICY

INSIGHT DOES NOT INVEST IN COMPANIES INVOLVED WITH THE PRODUCTION, SALE OR MAINTENANCE OF CLUSTER MUNITIONS OR LANDMINES.

There are two major international conventions that address cluster munitions and landmines specifically:

- The Convention on Cluster Munitions (2008): This Convention restricts the manufacture, use, and stockpiling of cluster munitions and the components of these weapons
- The Convention on the Prohibition of the Use, Stockpiling, Production and Transfer of Anti-Personnel Mines and on Their Destruction (1997): This Convention, often referred to as the Anti-Personnel Landmines Convention, aims to eliminate anti-personnel landmines around the world

In line with these international conventions and following their ratification into domestic law by a number of countries, Insight has adopted a global policy which commits it to avoiding direct investments in companies that:

- Design, produce, sell or maintain cluster munitions and/or landmines
- Undertake research and development to develop cluster munitions and/or landmines
- Breach the requirements of the Convention on Cluster Munitions or the Anti-Personnel Landmines Convention

This policy:

- Applies across all asset classes
- Excludes affiliated companies: that is, companies with affiliations or commercial relationships with screened companies will not be excluded from investments
- Does not apply to passive holdings in index-tracking instruments

APPENDIX III. LEADING OUR RESPONSIBLE INVESTMENT PROGRAMME

OUR RESPONSIBLE INVESTMENT ACTIVITIES ARE OVERSEEN BY THE ESG WORKING GROUP, WHICH CONSISTS OF SENIOR MANAGERS FROM ACROSS THE BUSINESS, REPRESENTING INVESTMENT MANAGEMENT, RISK, HUMAN RESOURCES AND COMMUNICATIONS DEPARTMENTS.

The ESG Working Group sets, reviews and monitors the implementation of responsible investment. It focuses particularly on the following:

- Identifying new/emerging ESG issues
- Prioritising issues that require further action
- Ensuring that agreed actions are implemented

The ESG Working Group, which met five times in 2017, now reports periodically to the Executive Management Committee and to the Business Management Forum, a senior management group of Insight executives and employees chaired by Insight's Chief Executive Officer.

Over the year, the ESG Working Group's efforts included:

- A review of the TCFD recommendations and its impact on Insight's clients and business
- A response to a UK government consultation on corporate governance reforms

ESG Working Group members include:

- David Averre, Head of Credit Analysis
- Joshua Kendall, ESG Analyst
- David Chellew, Head of Marketing
- Victoria May, Head of Client Management, North America
- Lynne Dalgarno, Head of Human Resources
- Bonnie Smith, Product Director
- Jonathan Eliot, Chief Risk Officer
- Rory Sullivan, Responsible Investment Advisor
- Adrian Grey, Chief Investment Officer – Active Management

Insight's ESG Analyst, Joshua Kendall, supported by our Responsible Investment Advisor, leads the responsible investment strategy and ensures that our investment processes remain consistent with Insight's Responsible Investment Policy.

IMPORTANT INFORMATION

RISK DISCLOSURES

Past performance is not indicative of future results. Investment in any strategy involves a risk of loss which may partly be due to exchange rate fluctuations.

The performance results shown, whether net or gross of investment management fees, reflect the reinvestment of dividends and/or income and other earnings. Any gross of fees performance does not include fees and charges and these can have a material detrimental effect on the performance of an investment.

Any target performance aims are not a guarantee, may not be achieved and a capital loss may occur. Strategies which have a higher performance aim generally take more risk to achieve this and so have a greater potential for the returns to be significantly different than expected.

Portfolio holdings are subject to change, for information only and are not investment recommendations.

ASSOCIATED INVESTMENT RISKS

Fixed income, liability-driven investment and multi-asset

Where the portfolio holds over 35% of its net asset value in securities of one governmental issuer, the value of the portfolio may be profoundly affected if one or more of these issuers fails to meet its obligations or suffers a ratings downgrade.

A credit default swap (CDS) provides a measure of protection against defaults of debt issuers but there is no assurance their use will be effective or will have the desired result.

The issuer of a debt security may not pay income or repay capital to the bondholder when due.

Derivatives may be used to generate returns as well as to reduce costs and/or the overall risk of the portfolio. Using derivatives can involve a higher level of risk. A small movement in the price of an underlying investment may result in a disproportionately large movement in the price of the derivative investment.

Investments in emerging markets can be less liquid and riskier than more developed markets and difficulties in accounting, dealing, settlement and custody may arise.

Investments in bonds are affected by interest rates and inflation trends which may affect the value of the portfolio.

Where high yield instruments are held, their low credit rating indicates a greater risk of default, which would affect the value of the portfolio.

The investment manager may invest in instruments which can be difficult to sell when markets are stressed.

Farmland

Investments in emerging markets can be less liquid and riskier than more developed markets and difficulties in accounting, dealing, settlement and custody may arise.

Farmland is exposed to the impact of government policy. Subsidies, renewable fuels, trade agreements and attitudes to ownership rights can vary between markets, and may change over time. Farmland is an inherently illiquid asset subject to the range of risks associated with primary production. Land values, like commodities, will experience large deviations from the equilibrium as a result of a range of market forces such as returns across other assets, level of interest rates, and investor sentiment.

The investment manager may invest in instruments which can be difficult to sell when markets are stressed.

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Insight does not provide tax or legal advice to its clients and all investors are strongly urged to seek professional advice regarding any potential strategy or investment.

For a full list of applicable risks, and before investing, investors should refer to the Prospectus or other offering documents. Please go to www.insightinvestment.com.

Unless otherwise stated, the source of information and any views and opinions are those of Insight Investment.

Telephone calls may be recorded.

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13778-03-18

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Insight Astronomy Photographer of the Year competition 2017