

# Restriction Screening & ESG Policy

---

GLOBAL FIXED INCOME TEAM | NOVEMBER 2021

## Overview

### SFDR Classification

The Restriction Screening and ESG Policy (“the Policy”) described below refers specifically to the fixed income Morgan Stanley Investment Funds (MS INVF) listed in footnote 1 (“the Funds”).<sup>1</sup>

The Funds promote environmental and social characteristics within the meaning of **Article 8** of Regulation (EU) 2019/2088 of 27 November 2019 on sustainability-related disclosures in the financial sector (“**SDFR**”).

The MSIM Fixed Income Sustainable Investing team in collaboration with the Credit Analysts and Portfolio Managers (“the Investment Team”), are responsible for establishing the screening and Environmental, Social and Governance (ESG) criteria of this Policy, which will be reviewed and updated on at least an annual basis to ensure that it remains consistent with our view on best practice in the context of the goals of the Funds.

### Restriction Screening Rationale

Restriction screening refers to intentionally avoiding investments in certain countries, sectors or issuers. In designing the restriction screening policy as part of our investment strategies, we consider the following aspects:

- **Reducing exposure to risks related to ESG factors.** *These risks may be reputational, regulatory or financial, stemming from the business activities or practices of the issuer. We aim to remove some of the most material of these risks through restriction screening at the country level for sovereign issuers, or sector level for corporate issuers.*
- **Values alignment.** *We may decide to exclude certain countries where inadequate institutions or governance result in social violations, or certain sectors from the portfolio based on our assessment that they have an overall negative impact on society or the environment which is not aligned to the objectives of the fund.*
- **Consideration as to whether there is an opportunity for engagement on ESG issues** *and whether an issuer may be able to transition its business activities or practices to a more sustainable model. We therefore may apply thresholds or carve-outs as part of the sector-level exclusions for corporates or state-owned enterprises with an aim to engage with certain issuers to help drive positive change and long-term value.*
- **Adherence to core basic standards, minimum safeguards and ethical norms.** *We expect issuers to adhere to minimum standards as defined by international ESG norms.*
- **Implications for portfolio construction.** *We aim to consider whether restrictions may have an effect on the risk/return profile of the fund, or narrow the investable universe to an extent which may be detrimental to that profile.*

Our current list of restrictions applicable to the Funds is presented below.

<sup>1</sup> This Policy applies to the following funds:

MS INVF Emerging Markets Debt Fund

MS INVF Emerging Markets Domestic Debt Fund

## I. Social Violations

MSIM Fixed Income promotes good governance and social practices among sovereign debt issuers to ensure that fundamental social rights are enjoyed by the citizens of those countries.

Consequently, we will not make **any new investments** in countries where there is evidence of significant social violations, defined as those countries ranked in the **bottom-10% in terms of their Social Violations Indicator**. Details on the construction of the Social Violations Indicator are provided in the ESG Integration Methodology section below. However, any existing investments in such countries shall not necessarily need to be sold, and any countries exhibiting positive momentum with respect to such violations shall not be subject to the purchase restriction.

In addition, the following restrictions apply to the Funds' investments in corporate securities:

## II. Controversial Weapons

MSIM Fixed Income views controversial weapons as indiscriminate and excessively injurious, often resulting in civilian casualties and causing a disproportionate level of pain and suffering. These weapons may also pose a long-term risk to civilian populations from unexploded ordnance which can detonate long after their initial use.

We shall not knowingly invest in securities of issuers that generate **any revenue** from the manufacturing or production of controversial weapons or intended use components, or are a **majority owner of, or majority owned by,** controversial weapons companies. Controversial weapons are defined as including anti-personnel landmines, cluster munitions, biological/chemical weapons and nuclear weapons.

Our approach to controversial weapons is consistent with the Ottawa Convention 1999, the Oslo Convention 2010, the Biological Weapons Convention 1975, and the Chemical Weapons Convention 1997.

## III. Civilian Firearms

We take the view that although firearms can in some cases support rightful and peacekeeping activities, their use by civilians, particularly in the case of automatic and semi-automatic firearms, poses a threat to society as there is a high risk that they might end up being used illegally or indiscriminately against other people, causing mass wounding or death.

We shall not knowingly invest in securities of issuers that generate **any revenue** from the manufacturing or production of civilian firearm systems.

## IV. Tobacco

We believe tobacco has significant negative social and economic impacts and is considered the single greatest preventable cause of death. As a result, tobacco companies are exposed to significant ongoing financial and reputational risk from increased regulation. Moreover, in our view, there is no reasonable level of tobacco consumption and we believe engagement with the tobacco industry will not lead to significant change.

We shall not knowingly invest in securities of issuers that generate **any revenue** from the manufacturing or production of tobacco products.

## V. Thermal Coal

We estimate that coal is the most carbon-intensive of the fossil fuels and it is exposed to significant stranded asset risk from climate-related policy, and we therefore look to exclude it from the Funds to mitigate our climate-related financial risks.

We shall not knowingly invest in securities of issuers that generate **5 percent or more of their revenue** from the mining and extraction of thermal coal.

The exception to this is that the Fund may invest in labelled bonds such as Green, Sustainability, Transition, Sustainability-Linked Bonds, as defined further below in this Policy, or other debt securities that are issued to raise capital specifically for climate-related or environmental projects, which are issued by issuers that would otherwise be subject to the coal exclusion above, so long as we have determined that the objectives of such instruments are consistent with a reduction by the issuer in its carbon emissions. Investment in such instruments will be subject to diligence by the Sustainable Investing team, with the support of our MSIM Credit Analysts.

We may also engage issuers' management more broadly around the topics of decarbonisation and climate risk (as well as corporate governance practices and what it deems to be materially important other environmental and/or social issues facing an issuer) including those issuers involved in coal-fired power generation and those that generate less than 5 percent of their revenue from the mining and extraction of thermal coal. As part of such engagements, we will endeavor to encourage issuers to develop decarbonisation strategies and specify science-based targets to transition their business models to more sustainable ones.

## VI. Monitoring of ESG Controversies and International Norms

We expect any corporate or state-owned enterprise issuers we invest in to comply with minimum standards and safeguards around human rights, labour rights, environment, business ethics and corruption as defined by international norms such as the United Nations Global Compact, the International Labour Organization's (ILO) fundamental principles and the Organisation for Economic Co-operation and Development's (OECD) Guidelines for Multinational Enterprises. We monitor business practices on an ongoing basis, through data on ESG controversies and standards screening that we source from third-party providers. Although failure to comply with such standards will **not automatically result in exclusion from the Funds**, it may cause us to pursue a more cautious stance to the company, conduct further research and due diligence, and engage with company management to try to ensure that our understanding of the issue is as comprehensive as possible, and that any action we take is fully informed.

## ESG Methodology

### Environmental & Social Characteristics

The Investment Team integrates the consideration of sustainability issues in its investment decision-making based on bespoke methodologies developed by MSIM Fixed Income to evaluate the ESG characteristics of issuers and transactions across sub-asset classes including corporates, sovereigns, securitised and sustainable bonds (as defined below). Details of the methodologies are available on the web links below:

- [ESG Credit model](#)
- [ESG Sovereign model](#)
- [ESG Securitised model](#)
- [Sustainable Bond evaluation](#)

We may **engage issuers** around specific ESG themes, including carbon emissions, climate vulnerability, forestry conservation, life expectancy & health, education, living standards, voice & accountability, political stability, effective government, regulatory quality, rule of law, corruption, violence/terrorism.

The Funds may also invest in Sustainable Bonds, defined as labelled bonds where the issuer has committed to financing or attaining specific environmental and/or social objectives, including but not limited to the below based on the main labels of bonds issued to date, including those recognised by the International Capital Market Association (ICMA):

- Green Bonds
- Social Bonds
- Sustainability Bonds
- Transition Bonds
- Sustainability-linked Bonds

### Sustainability Indicators

The Investment Team measures and monitors the relevant environmental and social characteristics for the Funds with the use of certain sustainability indicators. The table below specifies some sustainability indicators used in the security selection process and data sources.

Sustainability indicator	Metric	Methodology	Data sources
Social Violations Indicator	<p>Custom indicator applicable to sovereign issuers, built by equally weighting two Worldwide Governance Indicators:</p> <ul style="list-style-type: none"> <li>• “Voice &amp; Accountability” represents the extent to which a country’s citizens are able to participate in selecting their government, their political rights and civil liberties such as freedom of expression, freedom of association, and a free media;</li> <li>• “Rule of Law” reflects the quality of a country’s contract enforcement and property rights, citizens’ confidence in the police force and judicial system, the degree of security as well as the likelihood of crime and violence, including trafficking of people.</li> </ul>	<p>The Social Violations Indicator sets the exclusion threshold at the bottom-10% rank across the list of all countries for which data is available.</p> <p>A list including the bottom-10% countries (“social violation country list”) is coded into our portfolio surveillance system to inform the restriction screening process. In cases where the proprietary MSIM Sovereign Sustainability model and/or Analysts’ research indicates positive momentum in the relevant underlying factors, the Investment Team may conclude that the custom Social Violations Indicator does not reflect a country’s current sustainability trajectory. In such cases, the Investment Team would be permitted to invest in these countries, provided the sustainability rationale is justified and documented. The social violations country list will be updated at least annually, to reflect the frequency of publication of new Worldwide Governance Indicators, and will be approved by the Investment Team following an internal review meeting.</p>	World Bank’s Worldwide Governance Indicators
Issuer’s ESG score	ESG scores at issuer-level developed by MSIM, with data inputs from third-party providers.	Information regarding an issuer’s ESG score is incorporated in the investment process.	MSIM proprietary methodologies, with third-party inputs, where relevant, from MSCI, World Bank, United Nations, Emission Database for Global Atmospheric Research (EDGAR), University of Notre Dame

## ESG Data

In undertaking the above ESG assessment and restriction screening, the Investment Team supplements its own analysis with data from third parties such as the World Bank, the United Nations, the Emission Database for Global Atmospheric Research (EDGAR), and the University of Notre Dame for sovereign issuers. For corporate screening, MSCI, Sustainalytics, S&P Trucost, ISS ESG and other providers may be used. The Investment Team will bear the costs in relation to the use of third-party data. Third-party data is subject to change, which can result in delays in reflecting such changes in the portfolios. Where this is the case, we will resolve such instances as soon as possible.

## Policy Compliance

This Policy applies to the physical investments held directly in the Funds. Any sale of existing investments held in the Funds by the Investment Team will take into account the best interests of the Investors in the Funds.

Representatives from several areas of MSIM are responsible for monitoring the portfolio for compliance as outlined below:

*Portfolio Managers and the Fixed Income Sustainable Investing team* are primarily responsible for ensuring compliance with the Policy.

*Traders* are responsible for executing trades that are consistent with Policy and subject to best execution. They also must enter trades into the portfolio trading system, which enables traders to monitor individual portfolios for guideline conformity.

The *Portfolio Surveillance team* is responsible for coding ESG-related rules into our trade compliance system, which uses an automated process to monitor the Policy and ensure adequate surveillance of the portfolio.

Issued by MSIM Fund Management (Ireland) Limited. MSIM Fund Management (Ireland) Limited is regulated by the Central Bank of Ireland. MSIM Fund Management (Ireland) Limited is incorporated in Ireland as a private company limited by shares with company registration number 616661 and has its registered address at The Observatory, 7-11 Sir John Rogerson's Quay, Dublin 2, D02 VC42, Ireland.

This document supplements the information provided in the Prospectus. Investors should read the Key Investor Information Document and Prospectus before investing. T

There is no assurance that a Fund will achieve its investment objective. Funds are subject to market risk, which is the possibility that the market values of securities owned by the Fund will decline. Accordingly, you can lose money investing in this Fund.