

## Global Sustain Strategy

# Restriction Screening Policy

INTERNATIONAL EQUITY TEAM | SEPTEMBER 2021

### RESTRICTION SCREENING

This restriction screening policy relates to Morgan Stanley Investment Management's Global Sustain Strategy (the "Strategy") which is managed by the International Equity team (the "Investment Team"). It applies to a number of Global Sustain vehicles that the Investment Team manages, including the Morgan Stanley Investment Fund ("MS INVF"), the Morgan Stanley Funds (UK) ("MS Funds UK") and separate accounts, as agreed on a client by client basis. The Investment Team applies restriction screening to the Strategy which incorporates a Greenhouse Gas ("GHG") Emissions<sup>1</sup> Intensity filter and Sector / Industry level exclusions, as further detailed below.

Restriction screening refers to intentionally avoiding investments in certain sectors or issuers. When assessing the investment universe for the Strategy, the below restrictions are applied pre-investment and are binding.

#### 1. GHG Emissions Intensity Criteria Exclusions:

The Strategy will firstly exclude investments in any company that the Investment Team determines has any tie to fossil fuels as classified by the MSCI ESG Business Involvement Screening Research ("MSCI ESG BISR") database<sup>2</sup>, or any company that has been assigned the following sectors or industries under the MSCI Global Industry Classification Standards ("MSCI GICS")<sup>3</sup>:

- *Construction Materials*
- *Energy*
- *Metals & Mining*
- *Utilities (excluding renewable electricity and water utilities)*<sup>4</sup>

The remaining issuers will then be ranked according to their GHG emissions intensity estimates. Issuers with the highest emissions intensity are excluded. For further details, see the GHG Emissions Intensity section.

<sup>1</sup> The GHG Protocol establishes comprehensive global standardized frameworks to measure and manage GHG emissions from private and public sector operations, value chains and mitigation actions. GHG emissions, as defined by the GHG protocol include carbon dioxide (CO<sub>2</sub>), methane (CH<sub>4</sub>), nitrous oxide (N<sub>2</sub>O), hydrofluorocarbons (HFCs), perfluorocarbons (PFCs) and sulphur hexafluoride (SF<sub>6</sub>) in metric tonnes of CO<sub>2</sub> and CO<sub>2</sub> equivalent. Third party ESG data providers typically use the GHG protocol when measuring company GHG emissions intensity. For more information about the Greenhouse Gas Protocol please visit <https://www.ghgprotocol.org>.

<sup>2</sup> Companies with a tie to fossil fuels (thermal coal, oil and gas), in particular reserve ownership, related revenues and power generation.

<sup>3</sup> GICS, is a four-tiered, hierarchical industry classification system. Companies are classified quantitatively and qualitatively. Each company is assigned a single GICS classification at the Sub-Industry level according to its principal business activity. MSCI and S&P Dow Jones Indices use revenues as a key factor in determining a firm's principal business activity. Earnings and market perception, however, are also recognized as important and relevant information for classification purposes, and are taken into account during the annual review process.

<sup>4</sup> Utilities (excluding renewable electricity and water utilities), including any company whose core business activity involves nuclear power generation and/or nuclear power trading.

## 2. Sector / Industry Exclusions:

In addition to the above GHG-related exclusions, the Investment Team immediately screens out any company that has been assigned any of the following MSCI GICS sectors or industries:

- *Brewers*
- *Casinos & Gaming*
- *Distillers & Vintners*
- *Tobacco*

Further to this, the Investment Team screens out any company that generates more than 10% of its revenue from any of the following areas according to the MSCI ESG BISR database:

- *Adult entertainment*
- *Alcohol*
- *Civilian firearms*
- *Gambling*
- *Tobacco*
- *Weapons*

## 3. Controversial Weapons Exclusions:

The Strategy will not invest in any company which, according to the Investment Team's methodology, is involved in controversial weapons, including in particular any company excluded from the MSCI World ex Controversial Weapons Index due to its involvement with controversial weapons, as defined by that Index.<sup>5</sup> In addition, the Investment Team prohibits investment in companies that are 50% or more owned by a company with depleted uranium weapons involvement and companies that own 20% to 49.9% of a company with depleted uranium weapons involvement.

## GHG Emissions Intensity

The Strategy seeks to achieve a GHG emissions intensity that is significantly lower than that of the reference universe (which is defined, only for the purposes of comparing GHG emissions intensity, as the MSCI AC World Index). The GHG emissions intensity reduction target of the Strategy is to seek to be at least 50% lower than that of the reference universe on the basis of Scope 1 and Scope 2 emissions. To help achieve this objective, the Strategy uses a binding GHG emissions intensity of company sales exclusionary screen. The screen is designed to capture and exclude companies with relatively high GHG emissions intensity that are not already captured by the binding exclusions set out above, or for which GHG emissions intensity estimates are not available and/or cannot be estimated (at the Investment Team's discretion). The Investment Team uses third-party data providers to ascertain the GHG emissions intensity of company sales data of issuers, based on Scope 1 and Scope 2 emissions.

In some cases, data on specific issuers may not be available, may be estimated by an alternative third-party data provider, or may be estimated by the Investment Team using internal methodologies or reasonable estimates. The methodologies used by different data providers may vary and if the preferred data provider changes its methodology, the GHG emissions intensity estimates for one or more issuers may also change significantly. The Investment Team will also use its best efforts to exclude any company determined to have a tie to fossil fuels (e.g. reserve ownership, related revenues and power generation) but in some cases data may not be available or fully representative of the activities of the issuer.

The GHG-based emissions intensity criteria should collectively result in a reduction of the reference universe in a significantly engaging manner. In combination, these screens seek to achieve at least a 20% reduction in the reference universe. For the MS INV F only, the Investment Team will ensure that at least 90% of the issuers in the portfolio are assessed against these criteria.

<sup>5</sup> To apply this screen, the Investment Team prohibits investment in any company that is defined by the MSCI ESG BISR database to have any tie to controversial weapons in addition to any company that has been excluded from the MSCI World ex Controversial Weapons Index due to its involvement with controversial weapons, as defined by that index. The Index has been developed for use by investors who wish to avoid investments in cluster bombs, landmines, depleted uranium, chemical and biological weapons, blinding laser weapons, non-detectable fragments and incendiary weapons (white phosphorus).

## Restriction Policy Compliance

This restriction screening policy applies to the investments held directly in the Strategy. Investments that are held by the Strategy but become restricted after they are acquired for the Strategy, will be sold. Such sales will take place over a time period to be determined by the Investment Team, taking into account the best interests of the shareholders of the Strategy. The Investment Team reviews this policy periodically and any changes will be reflected in this document. In addition to ongoing monitoring by the portfolio managers, Morgan Stanley Investment Management's Portfolio Surveillance team codes the restricted criteria into the firm's surveillance system, and uses an automated process to monitor adherence to investment guidelines, including pre- and post-trade guideline monitoring and exception-based screening, and informs the Investment Team of possible guideline violations for this policy.

## Compliance with Minimum Standards and Safeguards

Given our focus on high quality companies with high quality management, the Investment Team expects the issuers it invests in to comply with minimum standards and safeguards around human rights, labour rights, environment, business ethics and corruption as defined by international norms. The Investment Team monitors business practices on an ongoing basis, through data on ESG controversies and standards screening that the Investment Team sources from third-party providers, including UN Global Compact violations, as well as its own engagement with company management and research.

The Investment Team reviews securities of issuers where it believes a significant breach of the above standards and principles has occurred and typically excludes such issuers where, after conducting its research and/or engagement, the Investment Team believes the breach is material to the sustainability of returns on operating capital, poses significant financial and /or reputational risk and the issuer has not committed to appropriate remedial action. Such exclusions are determined by the Investment Team rather than solely by third-party data. The analysis may be supported by third-party ESG controversies analysis and business involvement metrics.

## ESG Screening

The Investment Team considers that the Strategy promotes environmental characteristics through the application of a binding restriction screening process (as outlined above) as well as through the investment decision-making process. The Investment Team applies ESG criteria that seek to achieve a GHG emissions intensity for the Strategy that is significantly lower than that of the reference universe (which is defined, only for the purposes of comparing GHG\_emissions intensity, as the MSCI AC World Index). For the purpose of this Strategy, the term GHG shall be as defined by the GHG protocol and include carbon dioxide (CO<sub>2</sub>), methane (CH<sub>4</sub>), nitrous oxide (N<sub>2</sub>O), hydrofluorocarbons (HFCs), perfluorocarbons (PFCs) and sulphur hexafluoride (SF<sub>6</sub>) in metric tonnes of CO<sub>2</sub> and CO<sub>2</sub> equivalent. Further, as an essential and integrated part of the investment process, the Investment Team assesses relevant factors material to long-term sustainably high returns on operating capital including ESG factors, and seeks to engage with company management as part of this process.

## Sustainability Indicators

The Investment Team measures and monitors the relevant GHG emissions intensity for the Strategy with the use of certain sustainability indicators (as indicated below).

The table below specifies the sustainability indicators, the detail of the metric, permitted threshold and data sources:

Environmental characteristic	Sustainability indicator	Metric	Methodology	Data sources
Environmental	<b>GHG emissions intensity of company sales (metric tonnes of GHG per \$1mn of sales).</b>	GHG emissions intensity of company sales as measured by Scope 1 and Scope 2 emissions. Scope 1 emissions: emissions generated from sources that are controlled by the company that issues the underlying securities. Scope 2 emissions: emissions from the consumption of purchased electricity, steam, or other sources of energy generated upstream from the company that issues the underlying securities.	A weighted average GHG emissions intensity calculation is made for the portfolio and compared against the MSCI ACWI reference universe. The permitted threshold is up to 50% of the level of the reference universe.	S&P Trucost, MSCI ESG <sup>6</sup>

## DATA SOURCES

In undertaking the above analysis and restrictions screening, the Investment Team supplements its own analysis with data from third parties such as MSCI and S&P Trucost. The Investment Team will bear the costs in relation to the use of third-party data.

<sup>7</sup> The above data sources are primary data providers. The Investment Adviser may use ESG data and rating information from additional third-party providers to supplement these primary data sources.

## APPENDIX

### Sector and Industry Definitions

The following table defines those exclusions covered by the Strategy's restriction screening policy.

Type	Exclusion	Sub-Industry/ Factor Name	Definition
GICS	Brewers	Brewers	Producers of beer and malt liquors. Includes breweries not classified in the Restaurants Sub-Industry.
GICS	Casinos & Gaming	Casinos & Gaming	Owners and operators of casinos and gaming facilities. Includes companies providing lottery and betting services.
GICS	Construction Materials	Construction Materials	Manufacturers of construction materials including sand, clay, gypsum, lime, aggregates, cement, concrete and bricks. Other finished or semi-finished building materials are classified in the Building Products Sub-Industry.
GICS	Distillers & Vintners	Distillers & Vintners	Distillers, vintners and producers of alcoholic beverages not classified in the Brewers Sub-Industry.
GICS	Energy	Coal & Consumable Fuels	Companies primarily involved in the production and mining of coal, related products and other consumable fuels related to the generation of energy. Excludes companies primarily producing gases classified in the Industrial Gases Sub-Industry and companies primarily mining for metallurgical (coking) coal used for steel production.
GICS	Energy	Integrated Oil & Gas	Integrated oil companies engaged in the exploration & production of oil and gas, as well as at least one other significant activity in either refining, marketing and transportation, or chemicals.
GICS	Energy	Oil & Gas Drilling	Drilling contractors or owners of drilling rigs that contract their services for drilling wells.
GICS	Energy	Oil & Gas Equipment & Services	Manufacturers of equipment, including drilling rigs and equipment, and providers of supplies and services to companies involved in the drilling, evaluation and completion of oil and gas wells.
GICS	Energy	Oil & Gas Exploration & Production	Companies engaged in the exploration and production of oil and gas not classified elsewhere.
GICS	Energy	Oil & Gas Refining & Marketing	Companies engaged in the refining and marketing of oil, gas and/or refined products not classified in the Integrated Oil & Gas or Independent Power Producers & Energy Traders SubIndustries.
GICS	Energy	Oil & Gas Storage & Transportation	Companies engaged in the storage and/or transportation of oil, gas and/or refined products. Includes diversified midstream natural gas companies, oil and refined product pipelines, coal slurry pipelines and oil & gas shipping companies.
GICS	Metals & Mining	Aluminum	Producers of aluminum and related products, including companies that mine or process bauxite and companies that recycle aluminum to produce finished or semi-finished products. Excludes companies that primarily produce aluminum building materials classified in the Building Products Sub-Industry.
GICS	Metals & Mining	Copper	Companies involved primarily in copper ore mining.
GICS	Metals & Mining	Diversified Metals & Mining	Companies engaged in the diversified production or extraction of metals and minerals not classified elsewhere. Including, but not limited to, nonferrous metal mining (except bauxite), salt and borate mining, phosphate rock mining, and diversified mining operations. Excludes iron ore mining, classified in the Steel SubIndustry, bauxite mining, classified in the Aluminum Sub-Industry, and coal mining, classified in either the Steel or Coal & Consumable Fuels Sub-Industries.
GICS	Metals & Mining	Gold	Producers of gold and related products, including companies that mine or process gold and the South African finance houses which primarily invest in, but do not operate, gold mines.
GICS	Metals & Mining	Precious Metals & Minerals	Companies mining precious metals and minerals not classified in the Gold Sub-Industry. Includes companies primarily mining platinum.
GICS	Metals & Mining	Silver	Companies primarily mining silver. Excludes companies classified in the Gold or Precious Metals & Minerals SubIndustries.

GIC	Metals & Mining	Steel	Producers of iron and steel and related products, including metallurgical (coking) coal mining used for steel production.
GICS	Tobacco	Tobacco	Manufacturers of cigarettes and other tobacco products.
GICS	Utilities	Electric Utilities	Companies that produce or distribute electricity. Includes both nuclear and non-nuclear facilities.
GICS	Utilities	Gas Utilities	Companies whose main charter is to distribute and transmit natural and manufactured gas. Excludes companies primarily involved in gas exploration or production classified in the Oil & Gas Exploration & Production Sub-Industry. Also excludes companies engaged in the storage and/or transportation of oil, gas, and/or refined products classified in the Oil & Gas Storage & Transportation Sub-Industry.
GICS	Utilities	Independent Power Producers & Energy Traders	Companies that operate as Independent Power Producers (IPPs), Gas & Power Marketing & Trading Specialists and/or Integrated Energy Merchants. Excludes producers of electricity using renewable sources, such as solar power, hydropower, and wind power. Also excludes electric transmission companies and utility distribution companies classified in the Electric Utilities Sub-Industry.
GICS	Utilities	Multi-Utilities	Utility companies with significantly diversified activities in addition to core Electric Utility, Gas Utility and/or Water Utility operations.
BISR Revenue	Adult Entertainment	Adult Entertainment – Maximum Percentage of Revenue	The recent-year percent of revenue, or maximum estimated percent, a company has derived from adult entertainment.
BISR Revenue	Alcohol	Alcohol – Maximum Percentage of Revenue	The recent-year percentage of revenue, or maximum estimated percent, a company has derived from manufacturing, distributing, retailing, licensing, and supplying alcoholic products.
BISR Revenue	Civilian Firearms	Civilian Firearms – Maximum Percentage of Revenue	The recent-year percentage of revenue, or maximum estimated percent, a company has derived from the manufacture and retail of civilian firearms and ammunition.
BISR Revenue	Gambling	Gambling – Maximum Percentage of Revenue	The recent-year percent of revenue, or maximum estimated percent, a company has derived from gambling-related business activities.
BISR Revenue	Tobacco	Tobacco Total – Maximum Percentage of Revenue	The recent-year percent of revenue, or maximum estimated percent, a company has derived from tobacco-related business activities.
BISR Revenue	Weapons	Weapons – Maximum Percentage of Revenue	The recent-year percent of revenue, or maximum estimated percent, a company has derived from weapons systems, components, and support systems and services.
BISR Any Tie	Controversial Weapons	Controversial Weapons – Any Tie	Companies that have any ties to cluster munitions, landmines, biological / chemical weapons, depleted uranium weapons, blinding laser weapons, incendiary weapons, and/or non-detectable fragments.
BISR Any Tie	Depleted Uranium	Weapons – Depleted Uranium Manufacturer	Companies involved in the production of depleted uranium (DU) weapons, ammunition, and armor, including companies that manufacture armor piercing, fin stabilized, discarding sabot tracing rounds (APFSDS-T); Kinetic Energy Missiles made with DU penetrators; and DU-enhanced armor, including composite tank armor.
BISR Any Tie	Depleted Uranium	Weapons – Ownership by a Depleted Uranium Weapons Company	Companies that are 50 percent or more owned by a company with depleted uranium weapons involvement.
BISR Any Tie	Depleted Uranium	Weapons – Ownership of a Depleted Uranium Weapons Company	Companies that own 20 to 49.99 percent of a company with involvement. When a company owns 50 percent or more of a subsidiary with involvement, MSCI treats it as a consolidated subsidiary.
BISR Any Tie	Fossil Fuels	Fossil Fuels – Any Tie	Companies with a tie to fossil fuels (thermal coal, oil and gas), in particular reserve ownership, related revenues and power generation. It does not flag companies providing evidence of owning metallurgical coal reserves.

## **Important Information**

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