

# RESPONSIBLE INVESTMENT

REPORT 2016

# CONTENTS

Preface .....	3
Financial Performance .....	5-8
Updates in the financial policy .....	9
Agenda 2030 .....	10
A sustainable financial sector .....	11
Engagement with a focus on the climate .....	12

---

## CONTACT US

**Anders Thorendal**  
Treasurer and Chief Investment Officer  
anders.thorendal@svenskakyrkan.se  
Phone: + 46 018-16 95 88

**Gunnela Hahn**  
Head of Responsible Investment  
gunnela.hahn@svenskakyrkan.se  
Phone: + 46 018-16 94 21

---

# Preface

*This is the sixth year in a row that the Church of Sweden is issuing the Responsible Investment Report.*

*As of last year, it is being presented in a slightly different format. Information on financial performance, current topics (this year Agenda 2030), new investments and ongoing corporate engagement are presented in this document, i.e. the actual Annual Report, which has been produced by the Asset Management Unit in consultation with the Church of Sweden's Asset Management Council.*

*You will also find a number of links to further information on the Web. Other documentation regarding our responsible investment within asset management such as our working methods, our partners and governance, previously presented directly in this report, are now found together with other, more in-depth information on the Church of Sweden's website.*

*On the website you will also find other important previously published information about our holdings, financial policy and more.*

[🌐 https://www.svenskakyrkan.se/responsibleinvestment](https://www.svenskakyrkan.se/responsibleinvestment)

---

## **TO MAKE IT A BIT EASIER...**

Here are some links that take you to specific texts and documents within this area. Please have patience if the English version on the web has not yet been updated in full.

**Our working methods** – contains information on our investment process and financial policy as well as other information:

[🌐 https://www.svenskakyrkan.se/managing-assets-against-the-stream](https://www.svenskakyrkan.se/managing-assets-against-the-stream)

Information on our position as asset owners on issues regarding the climate and how we invest with a focus on providing benefits to society:

[🌐 https://www.svenskakyrkan.se/combine-investment-and-benefits-to-society](https://www.svenskakyrkan.se/combine-investment-and-benefits-to-society)

**Our partnership/co-operation** with other asset owners and investors, seminars we participate in and articles we have written:

[🌐 https://www.svenskakyrkan.se/combine-investment-and-benefits-to-society](https://www.svenskakyrkan.se/combine-investment-and-benefits-to-society)

**Governance** – regards the Church of Sweden's Asset Management Council as well as other subjects:

[www.svenskakyrkan.se/styrning](http://www.svenskakyrkan.se/styrning)

[🌐 https://www.svenskakyrkan.se/the-investment-process](https://www.svenskakyrkan.se/the-investment-process)

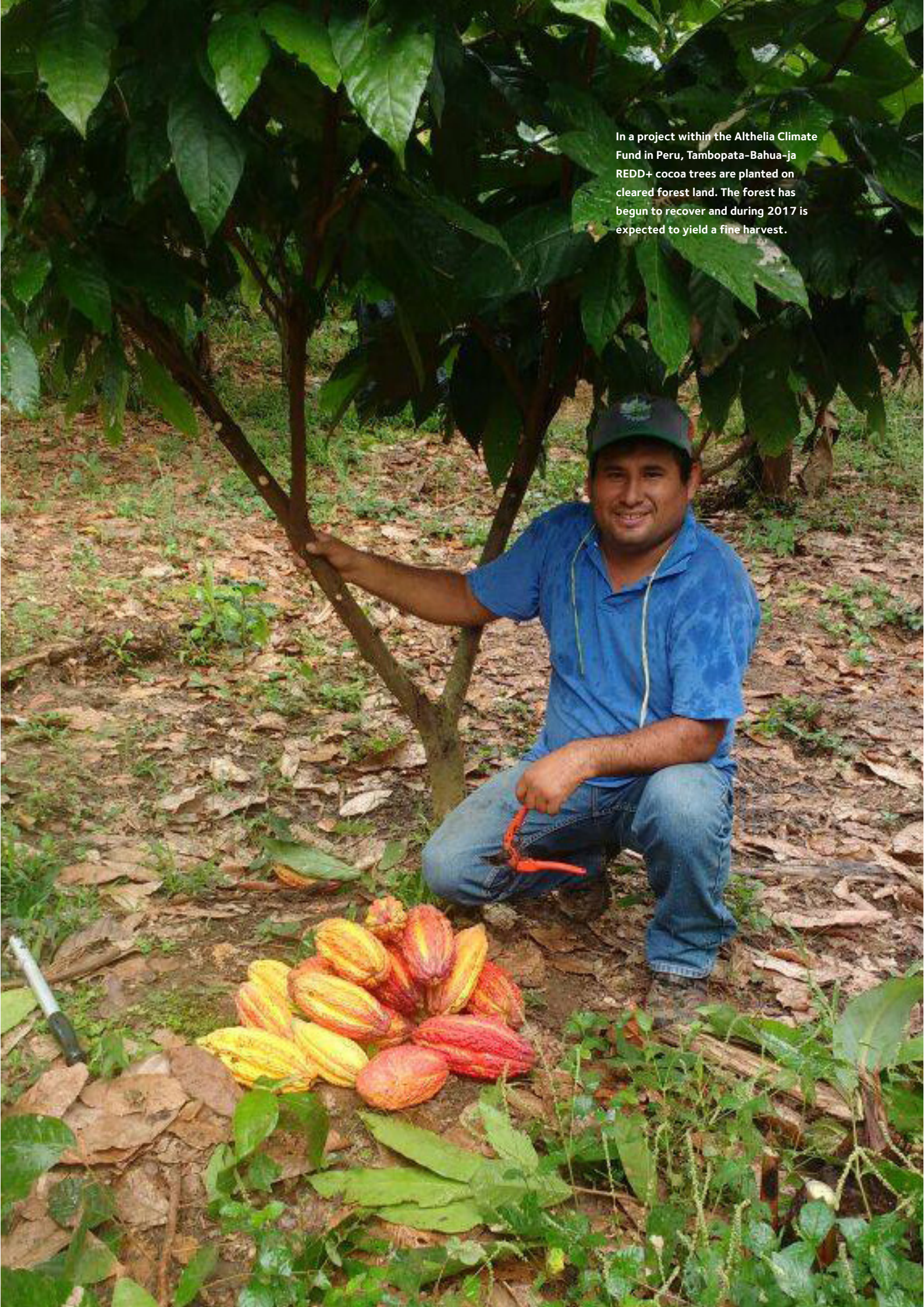
**Annual Report** on Responsible Investment:

[🌐 https://www.svenskakyrkan.se/reports-on-responsible-asset-management](https://www.svenskakyrkan.se/reports-on-responsible-asset-management)

---



In a project within the Althelia Climate Fund in Peru, Tambopata-Bahua-ja REDD+ cocoa trees are planted on cleared forest land. The forest has begun to recover and during 2017 is expected to yield a fine harvest.





# FINANCIAL PERFORMANCE

*When the Asset Management Unit at the national level for the Church of Sweden level presented its financial performance for 2016 it stood at SEK 628 million. This corresponds to a return of 9.3%. For the fifth year in a row, the overall portfolio outperformed its benchmark index. The Church of Sweden has created a balanced portfolio consisting of equities, fixed-income securities, real property and alternative types of investments. These investments make beneficial contributions to society and also demonstrate that sustainability is a pre-requisite for the long-term return on our investments..*

The commission from the Central Board of the Church of Sweden clearly states that the asset management shall focus on long-term performance. Our target return is 3% per annum over inflation measured in rolling ten-year periods. To meet this target, we have created a balanced portfolio containing equities, fixed-income securities, real property and alternative types of investments. We have chosen to invest in real property and alternative investments because we want to limit the risks in our overall portfolio by supplementing it with asset classes whose returns are not expected to follow the equities and fixed-income markets particularly closely. Making alternative investments, often made in unlisted holdings, also provide the opportunity to make investments of a more focused nature that are beneficial to society and where the Church of Sweden's investments can make a difference. However, all investments must fulfil our financial requirements. At the same time there are no purely social investments in our portfolio. More on real property and alternative investments in the section of the same name (Real property and alternative investments).

In the strategic reference portfolio, i.e. the allocation of the different asset classes that we have determined demonstrate the greatest potential, based upon a ten-year perspective to meet the return target at a reasonable risk level, we have allocated 50% of the overall portfolio to listed equities, 30% to fixed-income securities including corporate bonds and 10% to

real property and alternative investments respectively. However, our asset management strategy offers the option of deviating from the reference portfolio within established limitations (tactical allocation).

On 31 December 2016, assets under management totalled SEK 7 388.3 million (previous year 6 759.4).

## TEN-YEAR PERFORMANCE AND RETURNS

For the ten-year period 2007-2016, our returns were 67.9% corresponding to 5.3% per annum. The return target for the same period was 53.8%. The graph on page 7 illustrates this. The annual real return during this period, i.e. above inflation, was 4.2% on average. Since 2010, the return target in real terms has been 3.0% and previous to this, 4.0% per annum.

Viewed over the entire ten-year period, this means that on the whole the portfolio has contributed SEK 763 million above the return target and SEK 2 471 million above inflation.

## PERFORMANCE AND RETURNS 2016

Performance in 2016, including bank and administration fees amounted to SEK 628 million (326.3 million the previous year). Returns for the overall portfolio totalled 9.3% (5.1%). This is 6.2 percentage points higher than the real return target and 0.5 percentage points better than our benchmark index. This is the fifth year in a row that returns exceeded the weighted reference portfolio's return.

During 2016, all asset classes made a positive contribution to the portfolio's result. The largest contribution to performance was made by global equities at SEK 337.6 million, corresponding to a return of 15.3%. Our single largest investment, the Generation IM Global equity fund, with a return of 18.0% in SEK, is found in this asset class.

The emerging markets asset class yielded a return of 14.6% which is not as good as its benchmark index (19.5%). Managers of Swedish equities exceeded their benchmark index by just over one percentage point.

Fixed-income management yielded 2.7% and the corporate bonds fund 5.2% for the year. In both cases, this was somewhat better than their indexes.

The real property asset class contributed with a full 9.5%. Within alternative investments, Generation Credit contributed with the highest return followed by SEB's microfinance funds. The fixed-income hedge fund Excalibur also contributed with a positive return during the year.

Overall during 2016, it was the tactical asset allocation that contributed to the total return of the portfolio being 0.5 percentage points better than the weighted benchmark index.

The tables on the next page provide more information on performance for 2016 and our historical returns for five and ten year periods. We consider the ten-year performance to be the most important benchmark.

## REAL PROPERTY AND ALTERNATIVE INVESTMENTS

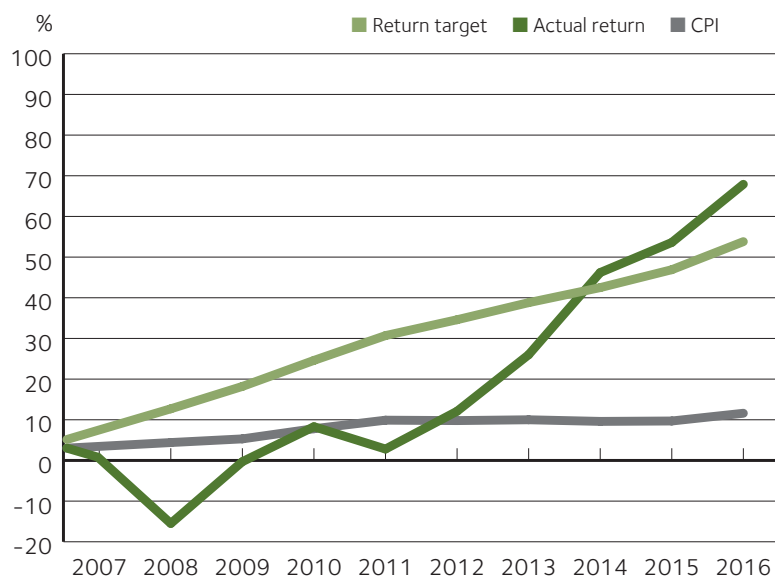
Since the end of last year, the value of the properties has increased from SEK 352.9 million to SEK 429.9 million as a result of previous commitments and thanks to the strong growth in value (9.5%) of the investments that we have made. The percentage of properties has increased from 5.2% to 5.8% of the assets under management since 2015. When all of the investments in real property that we have made commitments for are in place, the share of real property in the portfolio will be close to 10%.

In the alternative investments asset class, we made an investment at the beginning of 2016 in a fixed-income fund called Green for Growth Fund. The fund focuses on climate issues by lending money to projects with a focus on energy efficiency and a conversion to renewable energy in selected countries, e.g. Albania and Kosovo within the new markets (frontier markets) that are less developed than in countries that are included in the growth markets. The two microfinance-funds that we have invested in managed by SEB have yielded a continued stable return during 2016 of an average of 6.1%. Two of the impact-funds within alternative investments, Althelia Climate Fund and SFRE have the characteristics of a private equity investment, i.e. there is a well-defined start-up phase associated with costs during the initial years which means that it not meaningful to carry-out a financial evaluation before the fund has come a bit further in its life-cycle. Both of these funds had negative return rates during 2016.

During 2016, the value of alternative investments showed a net increase from SEK 664.2 to 699.3. The percentage of the overall portfolio is now 9.5%. The different investments during the year were offset as one of the earliest investments, SEB's Credit Opportunity III, was finalized. The fund yielded an annual return of 6.2%

---

[1] Our weighted benchmark index is based upon long-term strategic allocation. Our allocation among asset classes for 2015 in the reference portfolio was as follows: global equities 20%, Swedish equities 20%, Emerging Market equities 10%, fixed-income securities 25%, corporate bonds 5%, real property 10% and alternative investments 10%. The table on pg 7 shows the benchmark index we use for each asset class.



\* The graph shows only returns for each respective full year, with one measurement point per year. The real return target was 4 % during the period of 2005–2009 and was adjusted to 3 % in 2010.

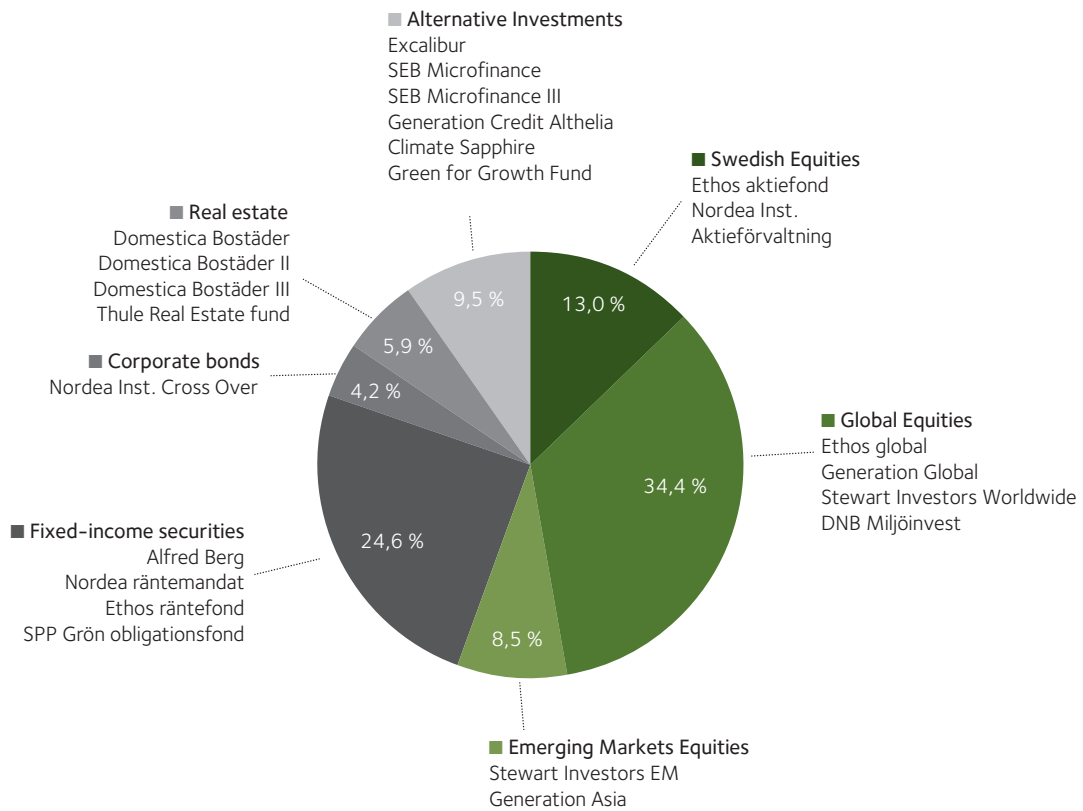
Asset type	Profit 2016 mnkr	Return full year 2016		Return full year 2015		Average annual return 2012–2016		
		Portofolio	Index	Portofolio	Index	Portofolio	Index	Benchmark
Swedish Equities	92,9	10,7 %	9,6 %	5,2 %	10,4 %	14,3 %	15,9 %	SIX RX
Global Equities *	337,6	15,3 %	15,5 %	11,2 %	3,6 %	17,3 %	14,1 %	DJSI World
Emerging Markets	79,9	14,6 %	19,5 %	-2,8 %	-7,8 %	12,7 %	7,0 %	MSCI EM
Fixed-income securities	49,6	2,7 %	2,6 %	0,2 %	0,5 %	2,8 %	2,7 %	OMRX Bond
Corporate bonds **	14,8	5,2 %	4,5 %	1,2 %	-0,5 %			Merrill Lynch EMU
Real estate***	34,5	9,5 %	4,8 %	8,8 %	3,1 %			KPI + 3 %
Alternative investments	19,0	2,9 %	4,8 %	1,2 %	3,1 %	5,3 %	3,9 %	KPI + 3 %
<b>Total</b>	<b>628,3</b>	<b>9,3 %</b>	<b>8,8 %</b>	<b>5,1 %</b>	<b>2,6 %</b>	<b>10,3 %</b>	<b>8,4 %</b>	

\* In this asset class, that is in total compared to DJSI, the DNB Miljöinvest is included (return 13,6 %, benchmark Wilderhill New Energy index 0,5 % for 2016).

\*\* Holdings total over 42 months, which is why there is no long-term average return.

\*\*\* Holdings total over 48 months, which is why there is no long-term average return.

**DISTRIBUTION AMONG ASSET CLASSES (31 DEC 2016)**



**THE TEN LARGEST HOLDINGS**

**Swedish Equities**

Atlas Copco  
 Nordea  
 Volvo  
 SEB  
 Hennes & Mauritz  
 Autoliv  
 Swedbank  
 Sandvik  
 SCA  
 Tele2

**Global Equities**

Microsoft  
 Cerner  
 Deere & Co  
 Unilever  
 CSL Limited MasterCard  
 Ingersoll-Rand Alphabet  
 Thermo Fisher Scientific  
 Ansys

**Emerging Markets**

Taiwan Semiconductor Manufacturing  
 Unilever  
 Marico  
 Tech Mahindra  
 Natura Cosmeticos  
 Tencent Holdings  
 Delta Electronics  
 Banco Bradesco  
 Dr. Reddy's Laboratories  
 Unicharm





Girls from a school in Deir Alla in Jordan pose for the camera when the European Bank for Reconstruction and Development is on location to make a film for a report on the Jordanian microfund for women.

## Updates in the financial policy

To further elucidate the financial policy, the Central Board of Church of Sweden made a number of changes in it in December 2016. The previous restrictions on making investments in companies with links to tobacco, alcohol and gaming for money (i.e. casinos etc. and not computer games) have been replaced by a percentage limitation. A company may at most derive 5% of its sales from the production of alcohol or gaming for money and 0% from the manufacture of tobacco products. Previously, a company needed, among other things, to have a policy for a responsible marketing of its products.

In the financial policy, we have also added a paragraph on international conventions, e.g. on child labour and

women's rights as well as a mention of Agenda 2030 and the global goals for sustainable development. In addition, we have further explained the climate criteria.

In the investment instructions for ethics and sustainability, which explain how the financial policy should be interpreted (which is necessary for all asset managers who state that they adhere to the financial policy), we have principally further explained and simplified the climate criteria for companies within coal, oil & gas and energy companies.

🌐 Link to the financial policy:

<https://www.svenskakyrkan.se/responsibleinvestment>

# Agenda 2030 – The global goals for sustainable development

*In September 2015, world leaders adopted seventeen common goals for sustainable, global development leading up to 2030. These goals, Sustainable Development Goals, replace the Millennium Goals. The goals in Agenda 2030 are comprehensive, e.g. Goal 1: Eradicate all forms of poverty everywhere, and is therefore divided into 169 sub-goals.*

The Church of Sweden is a part of an investment group that Sida has invited to participate in discussions exploring how Swedish investors can work with Agenda 2030. Our standpoint is that the goals, to be meaningful, shall be used to channel more money into solutions to the challenges that the goals reflect. Some investors think that they should instead interpret their current work in terms of Agenda 2030 by continuing to engage with companies as they have done previously, though now with the goals as support. Our focus in the investment group is Goal 11, Sustainable cities and Goal 6, Water and sanitation. In Sweden, as in other parts of the world, the need to invest in infrastructure for water is extensive and neglected, so we are also looking into how we can match the need of investment and assets at home. If we should succeed in finding and developing structures and models that we can later export, we could ramp them up to suit markets larger than those found in Sweden.

Investors the world over have shown great interest in Agenda 2030's goals. There are numerous equity funds and other financial products that state they adhere to the agenda's goals, and many asset managers who work with how to measure that contributions are actually made to them with investments. It is

more difficult to measure these effects than can at first be understood. This is why common measurement methods are needed so that it is possible to compare different funds. Being overly eager to measure can sometimes go too far and drain off energy from core operations or lead to incorrect decisions being made. Measurements and figures are a method of attempting to provide meaningful information and contribute to creating a beneficial, comprehensive overview but can never replace common sense. Is a fund that makes it possible for an African coffee grower to have solar energy more beneficial, or less beneficial, than a fund that reduces an Indian cotton grower's use of water? The question borders on the absurd since both investments are needed and provide benefits to society. This is relatively clear without having to look at the numbers. We have to accept that complex conditions and interrelationships are best described by conducting discussions on goals, means and outcomes, and complementing them with well-chosen measures for quality and quantity.

Many companies have embraced one or several of the goals and incorporated them into their business concepts. In addition, it is important to see opportunities for new business models and not just create add-ons for existing ones.



# A sustainable financial sector

*Aside from Agenda 2030, comprehensive activities are ongoing in different parts of the financial sector around the world on how to incorporate a long-term perspective and sustainability into work processes and investments. Also, several states within the powerful G20 group, such as China, have ambitious programmes for green finance.*

There has been much discussion about finding ways for how public assets can create leverage by co-investing with assets based in the private sector and in sovereign wealth funds (like the Norwegian “oil fund”), i.e. assets that are outside of tax-financed budgets. Most of all available assets are found in these sovereign wealth funds, pension funds, companies and individuals’ finances.

The banks play an important role in both climate adaptation and establishing a long-term perspective in the financial market. The Church of Sweden has been engaged in discussions with global banks since 2014 in an effort to get them to be an active force in working to limit climate change and creating financing solutions. Through the granting of credit, a central element in the life-blood of the economy, banks have great opportunities to make a difference and hasten the conversion to renewable energy supply. During 2016, important steps were taken by several banks, but there is much work left to be done in redirecting the flow of global assets.

Read more here:

<http://news.bostoncommonasset.com/on-borrowed-time/>

The Church of Sweden addresses climate issues in a variety of ways but primarily within its international operations. For example, we partner with other religious communities to accelerate the conversion to renewable energy sources with a special focus on the needs of impoverished countries and groups of people. Before the climate meeting in Marrakesh in the autumn of 2016, in conjunction with over 300 other religious and spiritual leaders from 58 countries, the Church of Sweden urged the world’s countries to redirect the global asset flows from fossil energy sources to climate-smart solutions. The need of combating energy poverty through renewable energy solutions and helping impoverished nations to handle the ongoing climate change was emphasised.

Find out more about the inter-religious statement here:

<http://ifcs-greenfaith.nationbuilder.com>

*“... green finance is a major opportunity. By ensuring that capital flows finance longterm projects in countries where growth is most carbon intensive, financial stability can be promoted.”*

**MARK CARNEY, Bank of Englands högste chef och ordförande i det brittiska Financial Stability Board.**

# Engagement with a focus on the climate

*The Church of Sweden's Financial Unit is often invited to speak at different events – primarily about our climate strategy. For example, during Almedalen Week, where Swedish politicians gather to discuss and debate current issues, we participated in several panels and roundtable discussions to discuss sustainable finances.*

Church of Sweden has also participated in a climate anthology “Climate Politics – if I were the Prime Minister”, which was recently published by the Swedish Foundation for Strategic Environmental Research (Mistra) and the Environmental Objectives Committee. Our contribution regarded what the financial sector needs from politicians to be able to play the key role the sector has in climate work.

Measuring emissions of greenhouse gases (such as carbon dioxide) as a “carbon footprint” in equity holdings has become popular among many fund managers. The Minister for Financial Markets and Consumer Affairs, Per Bolund, has stimulated the insurance industry and fund management companies to take action by threatening them with legislation. Over the last few years, the Church of Sweden has presented the weaknesses and most especially, all of the risks associated with this type of measurement to the different actors in the financial market as well as the sector's international news agencies. These types of measurements can be a good first step for an asset manager when working with developing a climate strategy or climate analysis. However, it is difficult for a customer to compare the carbon footprints of different funds. For example, a Swedish equity fund with just one steel company can push its carbon footprint sky high as compared to another Swedish equity fund without the steel company. This is because enormous amounts of energy are needed to manufacture steel, so even the most energy efficient steel company in the world can still cause the fund's footprint to be extremely high. In the other fund, all of the companies it contains may be performing poorly in relation to the climate, but the fund can in any case still have a lower carbon footprint. Another problem with this method of measurement is that for the most part it only takes into account emissions that originate in a company's own production from purchased or self-produced energy. Most emissions are released in the supply chain or when the product is used.

This means that a manufacturer of petrol and diesel vehicles can have a lower carbon footprint than a solar panel manufacturer. The emissions associated with the manufacture of vehicles primarily have their origin in the supply chain and when the vehicle is used - not in the factory when the parts of the vehicle are assembled. On the other hand, solar panel manufacturers use quite a bit of energy in their manufacturing process. For this reason they have a higher carbon footprint than a car manufacturer. The fact that solar panels save energy when they are used is also not included in calculations.

During the year, we discussed the climate issue at a Triple Bottom Line Investment (TBLI) conference that was held at the stock exchange in Stockholm in September 2016. Also, during Östersund's Climate Day, we were invited to hold a presentation on how investors can be climate smart and maintain or even achieve better financial returns.

At the beginning of 2017, the Church of Sweden was interviewed by international media. This can be viewed here:

<http://nordsip.com/2017/03/14/lack-of-sri-investment-funds-worsens-trade-off-for-responsible-allocators/>



Aside from achieving financial targets the Church of Sweden has two investment ambitions: making a difference when investing its assets and stimulating development in the (financial) sector to promote long-term thinking and sustainability. We have invested in several funds that clearly benefit society, e.g. within the areas of energy efficiency, renewable energy and green small enterprises.

## CORPORATE ENGAGEMENT

The Church of Sweden has conducted advocacy work with a focus on the companies in its equity portfolio, primarily through the GES Investment Services consultancy, who have upon assignment from us and other investors, engaged with companies that have not adhered to the international conventions regarding, e.g. working conditions, environment and anti-corruption. Currently, about ten such engagements are ongoing with companies that we invest in. We were in direct contact with about twenty individual companies during 2016, primarily in connection with different investment initiatives we have participated in, so that these companies can improve their risk management within different sustainability areas (e.g. engagement with banks on climate or telecom operators, see below).

### Global Network Initiative

Since 2013, the Church of Sweden has been a member of the board of the Global Network Initiative:

[www.globalnetworkinitiative.org](http://www.globalnetworkinitiative.org)

This multi-party organisation has recently met with success as a number of telecom operators have become members thus committing themselves to following-up and revising their work regarding the protection of the freedom of speech and integrity on the web. See press release here:

<http://www.globalnetworkinitiative.org/news/key-telecommunications-players-collaborate-global-network-initiative-freedom-expression-and/>

