For certain strategies that the adviser determines to be ESG integrated, the adviser integrates financially material environmental, social, and governance (ESG) factors as part of the Fund’s investment process (ESG Integration). ESG Integration is the systematic inclusion of ESG issues in investment analysis and investment decisions. ESG integration is dependent upon the availability of sufficient ESG information for the applicable investment universe. In addition, in order for an actively managed strategy to be considered ESG integrated, the adviser requires: (1) portfolio management teams to consider proprietary research on the financial materiality of ESG issues on investments; (2) documentation of the adviser’s research views and methodology throughout the investment process; and (3) appropriate monitoring of ESG considerations in ongoing risk management and portfolio monitoring. ESG determinations may not be conclusive and securities of companies / issuers may be purchased and retained, without limit, regardless of potential ESG impact. The impact of ESG Integration on performance is not specifically measurable as investment decisions are discretionary regardless of ESG considerations.
Research / due diligence

Our research process consists of an assessment of materiality and ESG scoring:

- **Assessment of materiality**: Our fundamental analysis of securities integrates ESG risks and opportunities both pre-trade and on an ongoing basis. We assess material ESG risks and opportunities using defined frameworks for corporates to ensure a robust and repeatable process. Our framework for corporates leverages the Sustainable Accounting Standards Board (SASB) ESG topics, while our framework for sovereigns leverages some of the ESG topics outlined in the UN PRI guide to sovereign debt investing. The portfolio managers have discretion to add further ESG topics they believe could be relevant to specific positions. Our materiality assessment draws on the managers’ understanding of inherent ESG risks and opportunities across countries, sectors, industries and activities, and their knowledge of their sector of coverage and specific companies. We integrate proprietary, broker and ESG-specific third-party research and company disclosures into our assessment. The final analysis is documented for reference and to monitor exposures over time.

- **ESG scoring**: Third-party scores provide a complement to our own assessment of materiality and are an objective quantitative framework for the consideration of ESG credentials. We leverage ESG scoring and the associated analysis from MSCI, using the All Country World Index (ACWI) scores for equity and credit, and the country scores for sovereign debt, which feed into Spectrum™. Within Spectrum™, we can view our portfolios’ aggregate ESG scores, the component parts and the scores for the broader universe. We also leverage the norm-based scoring assessment from ISS-ESG, referring to its red/amber/green flags. In addition, the proprietary J.P. Morgan Asset Management data-driven ESG score, being developed by the Sustainable Investing team, will provide further breadth of ESG data using our proprietary methodology in the future.

Portfolio construction

We integrate ESG analysis into our process to mitigate material potential negative risk scenarios as a result of ESG risks and to identify opportunities for securities with strong ESG characteristics. The consideration of potential ESG risks and opportunities can influence the decision to buy, disinvest or adjust position sizing in a particular security.

Engagement

To enhance our ESG analysis and ensure active ownership on behalf of our clients, the Macro Strategies team leverages the expert insights of the Investment Stewardship team, specifically relating to proxy voting and engagement activities. Further, we engage directly with companies on certain issues where we believe additional discussion may be materially beneficial.

Documentation and monitoring

Within macro strategies, all portfolio managers are responsible for conducting and documenting ESG research on all long exposures in single name equities, bond and FX. The team holds a dedicated fortnightly ESG meeting in which they review portfolio ESG scores and discuss any material ESG updates for the portfolio holdings. During these meetings, any changes in ESG scores or norm-based analysis are discussed, as well as ESG-related company updates arising from internal or third-party research and engagement, and any industry developments.
J.P. Morgan Alternative Asset Management (JPMAAM) Hedge Fund and Alternative Credit Solutions believes that sustainability is a key factor in managing risks and identifying opportunities, and we have developed a holistic investment approach that reflects this belief. Our ESG framework primarily focuses on ESG integration in our manager due diligence process. Our proprietary framework for evaluating managers includes an extensive list of questions on ESG factors across 25 categories in relation to their operational and investment processes. We apply the full framework to every manager while recognizing the materiality of certain ESG risks and opportunities may vary by manager type, size, and strategy. This comprehensive analysis informs our view of ESG-related risks and is an important part of our investment decision-making process.

**Portfolio Construction**

We view good ESG practices as a tool to help mitigate potential risks and conflicts, and a pre-requisite to investing in a responsible way. ESG factors are taken into consideration as part of each decision to invest in a new manager, remain invested with an existing manager, or terminate a manager. The ESG integration of our platform contributes to risk management and return across portfolios by (a) helping JPMAAM avoid hedge funds that are more likely to fail by identifying key structural risks and (b) influencing managers we do select to institute best practices that strengthen their business and protect their investors. Beyond identifying and mitigating potential sources of risk, our ESG integration process also helps us to identify outperformers and guides us towards additional sources of alpha.

**Engagement**

After evaluating managers on ESG factors throughout our due diligence process, we actively engage them on any identified financially material environmental, social, or governance risks. We work closely with our managers to help them improve on ESG factors where we believe they are lacking, providing guidance and support to help them achieve best-in-class practices. We believe this improves a company’s ability to operate successfully, both now and in the future, thereby enhancing the potential of our investment. JPMAAM prides itself on helping to drive ESG principles in the industry. The platform has helped many hedge fund managers to incorporate ESG factors into their businesses and investment processes. Notably, over 90% of managers on the JPMAAM platform already have or are actively drafting an ESG policy focused on investment and/or business practices—up from 10-15% at the start of 2018.

**Documentation and monitoring**

The ESG framework used for evaluating managers’ business practices was approved by the JPMAAM Investment Committee (IC). It is led and implemented by JPMAAM’s operational due diligence (ODD) team and is supported by the investment research analyst covering each manager. The ODD team is comprised of dedicated specialists who conduct a comprehensive assessment of risk controls, operations, financial statements, legal structures, and documentation as part of initial due diligence and ongoing monitoring. They report to Brian Burke, Head of Risk Management and a member of the Investment Committee, who has the right to veto any investment due to risk and operational concerns, including those related to ESG.

On every occasion the IC meets to approve a new manager or reviewing an existing one, the ESG evaluation is included in the materials to be considered for the committee’s review. Any meaningful and material ESG risks identified at any stage of the investment process are flagged by the ODD team and escalated to the IC.

The proprietary ratings for each ESG factor are incorporated into our research database and all clientreporting. This allows ratings to be effectively monitored by portfolio managers and investment directors at the manager and portfolio levels.
For more information on our approach to ESG Integration please contact your J.P. Morgan Asset Management representative.