Nordea

Responsible Investments & Identity

Annual Report • 2013

Contents

Editorial leader	4
Engagement activities	6
Norm-based screening	12
Excluded companies	13
Occupied areas investment policy	14
ESG integration	15
Corporate Governance	17
Responsible tax policies	19
Clinical Trials	20
Field trip: Russia	22
PRI – Annual Conference Cape Town	24
Star Funds	26
International Initiatives	34

Editorial leader:

Pinch, push and shift …

"Our failure to address environmental issues is not a failure of information but a failure of imagination."

Professor John Robinson of the University of British Columbia.

While financial markets globally have undergone substantial stress and change, an increasing number of mainstream investors see ESG integration as a way to improve their long-term financial performance and to respond to the increasing client demand for sustainable investments. This trend offers companies opportunities to attract long-term investors while simultaneously reducing their shareholder turnover, aligning their investment strategy with the real needs of their business and laying down the foundation for a sustainable future. Asset owners see ESG integration as an opportunity to generate long-term performance while fulfilling their fiduciary duty, and investment managers see it as a way to improve risk management in the financial performance of their investment portfolio.

For listed companies, long-term investors constitute a more attractive investor base. First, compared to short-term investors, long-term investors generally invest over a period of time that is better aligned with companies' business cycles and long-term sustainability strategy. Second, by holding shares over a greater period of time, long-term investors reduce share turnover, which is costly for companies. While short-term investors have exacerbated what Dominic Barton at McKinsey calls "quarterly capitalism," long-term investors allow companies to reconnect their investment strategies with the real needs of their business.

Nordea Asset Management believes that aligning ESG issues with core business agendas can help companies create shareholder value in three measurable ways.

Pinch. Downside risks should be reduced or "pinched", especially in a global marketplace that is increasingly volatile, resource-constrained and socially engaged. One way to do this is by integrating ESG and financial reporting, which can increase transparency, improve understanding of ESG risks and help drive targeted mitigation strategies. Improved transparency can also help build trust with customers, investors, and employees, creating a halo effect that makes it easier for a company to earn forgiveness when things go wrong, while getting more credit for things it is doing right.

Push. Companies can also leverage social and environmental issues to create new product and service innovations that drive revenues and reduce operating costs. Deloitte's research on innovation shows that leaders on ESG issues are over 400% more likely to be considered innovation leaders.

Shift. Weaving ESG factors into the fabric of a company can improve shareholder value over time by permanently shifting the expected share price to a higher level, creating a valuation premium. Part of this shift comes from pinch and push, which strengthen a company's brand, reduce risk, and fuel innovation. Another part comes from improved operating efficiency and reduced waste, which can significantly reduce costs and increase profitability. In addition, a strategic approach to ESG issues can boost a company's value by helping to attract financial and human capital. Responsible enterprises attract more funding and enjoy a lower cost of equity capital than their less responsible counterparts. They also have an easier time attracting talent – especially younger workers, who tend to be particularly conscious of social and environmental issues. These effects can help create a lasting competitive advantage.

Growing consensus indicates that ESG analysis adds value to investments. For asset owners, ESG integration may soon reach a tipping point: **there is good reason to think that ESG considerations will become a regular component of investment decision-making in the future.**

The process we have developed at Nordea Asset Management and are gradually implementing is one way to do this that we find promising, although it will take time to have the full results and conclusions of this ESG integration work.

Nevertheless, it is our ambition to leverage ESG analysis and engagement solutions in order to embed ESG across all investments processes. We are committed to assisting clients with the adoption of responsible investment strategies that enhance long-term investment performance.

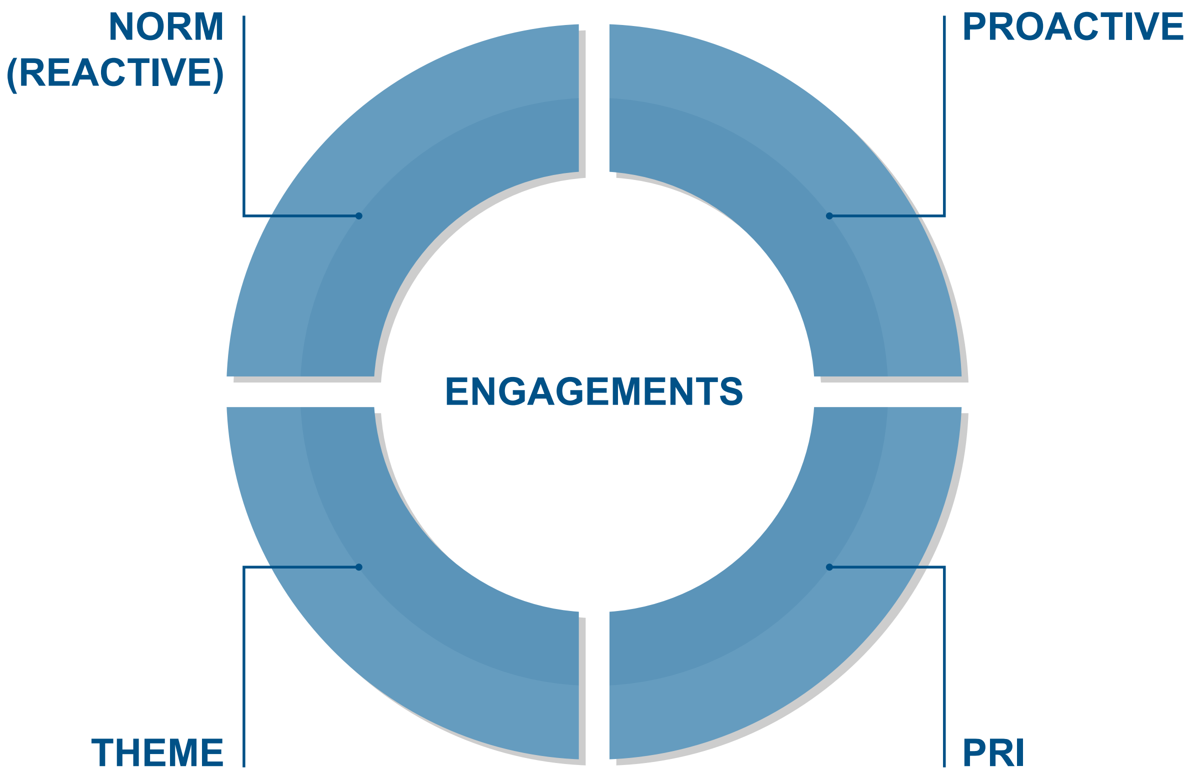
Today, we have an opportunity to steer our investments towards the future and once again rebuild portfolios for the long term. Responsible investments will create opportunities and rewards, but it will also mean challenging the pernicious orthodoxy of short-termism. As we face an inflection point in the global economy and the global environment, the imperative for change has never been greater.

Sasja Beslik
Head of Responsible Investments & Identity

Allan Polack
Head of Asset Management

Engagements – a cornerstone for active investors

We engage to change. Nordea initiates engagement dialogues to change behaviour and to enhance business performance by addressing the business practices used by companies we invest in.



Nordea engages with companies violating international norms (so-called norm engagement) and with companies where we see significant room for improvement in relation to ESG issues (so called proactive, theme and PRI engagements)

Norm-based engagements

In 2013 Nordea demonstrated active ownership in 13 international companies violating international norms. The breaches include violations of human rights, labour rights, severe environmental degradation as well as corruption.

Ended engagements due to successful progress

In 2013 Nordea successfully ended three company engagements because the companies had improved their management of ESG aspects significantly since the dialogue was started.

The norm violations conducted by these companies included suppression of workers' rights to unionise and corruption related practices. The three companies have all developed and implemented sufficient policies and procedures to address their previous norm violations. Furthermore, they have improved transparency and reporting on how they address ESG risks in their business operations.

New engagements with norm-breaching companies

Nordea initiated about ten new engagements. During the year, Nordea developed a policy related to companies operating in the Israeli occupied territories. The policy addresses companies which are engaged in settlement activity, extraction of non-renewable resources from the territories as well as companies that are providing products and services to the settlement security infrastructure. As a result of the policy Nordea initiated engagements with five new companies.

Often it takes time before we see real strategic change in the companies we engage with. But we know for a fact that the time and effort we spend on engaging with companies discussing their norm violations and overall approach to sustainability do lead to progress.

Examples of norm engagements during 2013

Human rights

The company is involved in violation of indigenous rights in connection with a dam project on the Xingu river in Brazil. We have raised our concerns with the company and put pressure on the company to improve its practi-ces. Our engagement partner, Hermes Equity Ownership Services, was the first investor that was invited to visit their site in 2013. We were then able to see and test how the company has implemented its policies on communities and indigenous people. During the visit we noticed that the company's practices related to community engagement are better than what would be suggested from their reporting. The company has committed to improve its disclosure on social issues and indigenous rights further and welcomed to work with us in this regard.

Anti-corruption

Our engagement with a South Korean company, which is alleged to have been involved in corrupted practices, led us to conduct a field visit to South Korea in November 2013. During the visit we, among other things, hosted an industry workshop where several South Korean companies attended. During the workshop we presented how we as an investor view ESG risks with a focus on issues related to business ethics. Our direct engagement with the South Korean company has progressed well and the company has implemented new systems that will better mitigate future risks. Among other things, the company now has an Ethics committee which is a sub-committee to the company's board. We encouraged the company

Engagements - a cornerstone for active investors

to be more transparent and accountable for the Ethics committee's responsibilities and activities in implementing relevant policies. Our aim with the engagement was met and we therefore successfully ended it in 2013.

Labour rights
In early 2012 Nordea initiated a dialogue with a Finnish company allegedly involved in labour rights violations in Mexico. The company had recently acquired a Mexican company that was suppressing unionisation.
Since we started the dialogue, the Finnish company has been very responsive and forthcoming towards Nordea, discussing ways to approach the labour controversies and to ensure that the rights of the workers are sufficiently safeguarded.

The company has arranged a vote, organised by a third party, on union representation among its employees and improved its employee training especially targeting its top management in Mexico, to address the issue of labour rights and rights to free unionization. In 2013, the company published its first ever Corporate responsibility report. Our target with the engagement is met and we therefore successfully ended it in 2013.

Proactive engagements

Nordea prioritises proactive engagements with companies. We initiate dialogue with the companies representing our largest holdings as well as companies identified for our RI enhanced funds during the ESG analysis process. As owners we would like the companies we invest in to address ESG risks as well as opportunities.

In 2013 we met with about 50 Nordic and global companies. It is our practice to engage in a direct face-to-face dialogue with the companies.

Three levels of interaction with companies
The first level of interaction is the information request. The aim of this dialogue is to receive basic information from the company. The information is used in our ESG analysis for the RI enhanced funds and, where necessary, to encourage the company to improve transparency.

The second level is a dialogue initiated in order to understand more about a specific key issue. The companies often have good reporting processes in place, but we may lack certain information in order to complete our assessment of the company. The dialogue is often conducted at face-to-face meetings or via conference calls.

The third level of interaction involves more intensive engagements conducted in order to improve a company's ESG management and performance. In addition to contributing to a positive development in the company in terms of ESG, the goal of such interaction is to improve the company's ESG profile so that we can invest in it through our RI enhanced funds.

This type of engagement has clear targets based on findings in our analysis and is a long-term activity.
All three types of interaction are drivers of change and will result in improved transparency and better risk or opportunity management.

Theme engagements

In 2013, Nordea initiated engagements with four new companies within the Oil & Gas and Mining sectors.
The engagements are conducted with companies that are identified to have high environmental risks. Two of the engagements will focus on natural gas and specifically hydraulic fracking. Hydraulic fracking is a fast spreading technology to extract unconventional gas, which is trapped below shale and coal bed rock formations.

There are several environmental risks associated with hydraulic fracking, such as drinking water contamination and degradation of air quality. As a first step, we will engage with the companies to raise our concerns and learn how the companies are working with the technology.

PRI initiatives for company engagement

Nordea participates in company engagements and initiatives through the PRI Clearing House. This is a hub for signatories to PRI (United Nations-backed Principles for Responsible Investment) where they can jointly support, drive and participate in different initiatives. Nordea is currently involved in five PRI initiatives.

Oil sands initiative

Nordea is engaged in a PRI initiative that targets oil sands production and the key environmental and social impacts of such production.

The initiative is run by PRI signatories in cooperation with COSIA*, an organization established by the 12 biggest oil sands producing companies operating in Canada. The aim of this initiative is a constructive dialogue focusing on how the industry may reduce the environmental and social impact of the companies' oil sands production.

This initiative was started in 2012.

Water risks engagement

Nordea is part of the steering committee for this engagement. Water withdrawals are forecast to continue to grow significantly – according to the Water Resources Group demand for water will by 2030 exceed current available supply by 40%, leading to large areas with significant water scarcity around the world. This will most likely have a significant effect on future economic growth and is therefore likely to impact long-term investors.

The aim of this initiative is to initiate a dialogue with water-intensive companies and sectors in order to address direct risks and supply chain risks related to water-demanding production and water scarcity.

This initiative was started in 2012.

Fracking engagement

Nordea is part of the steering committee for this engagement. The initiative on fracking aims at addressing several aspects of fracking operations, with a targeted group of companies. The focus of engagements varies from greenhouse gas emissions, water pollution and management to social and community concerns.

This initiative was started in 2012.

Sustainable fisheries

It is increasingly recognised that overfishing and unsustainable fishing practices could cause an irreversible decline in fish populations. This may lead to disruptions in company supply chains and represents a risk to both the companies and the investors that have invested in these companies.

The sustainable fisheries initiative was initiated and is backed by 18 investors and covers 41 companies. The goal is more sustainable fisheries practices in their business operations. Among the companies are Mitsubishi, Unilever, McDonalds, Wesfarmers and Nestlé.

This initiative was started in 2011.

Global Compact

Nordea supports the investor-backed initiative

Engagements - a cornerstone for active investors

towards companies that have signed the UN Global Compact**, but do not fulfil its reporting requirements. The goal of the initiative is to make the companies report on how they address and implement the ten principles to which they have signed up.

34 investors from over 12 countries and representing over USD 3 trillion are supporting this initiative through the PRI Clearing House. Together with the respective investors, Nordea has addressed 116 companies in total, 89 leaders and 27 laggards, on their Global Compact reporting.

This initiative was started in 2007.

* COSIA stands for Canada`s Oil Sands Innovation Alliance.

** The UN Global Compact is a set of ten principles that businesses can sign up to regarding the protection of human rights, labour rights and the environment and anti-corruption efforts. Reporting on how the company is following up on the principles is not required, but highly recommended so as to avoid so-called blue-washing. Blue-washing is when a company signs up to the UN Global Compact for branding reasons, but does not follow up on the principles or report on how the principles are followed.

Examples of company meetings – 2013

ABB	Ericsson	Tele2	Stanlib
Adecoagro	Gold One	TeliaSonera	SberbankUralkali
AstraZeneca	Husqvarna	Millicom	SKF
Alfa Laval	H&M	Naspers	Swedbank
Atlas Copco	HeidelbergCement	Nordea	Securitas
Autoliv	Hewlett Packard	Norilsk Nickel	SEB
Bank Hapoalim	Holmen	O`Key	Stockman
China Mengniu Dairy	Investor	Polyus Gold	Stora Enso
CDON	JM	Proffice	Volvo
Cia. Hering	ICA	Readsoft	X5 Retail Group
Dibs	Lundin Petroleum	SCA	ÅF
Electrolux	Lukoil	Scania	
Elekta	Limited Brands	Sandvik	

RII Field visit in a small village in the Chinese Guangxi province where Finnish / Swedish Stora Enso operates.

Norm-based screening

Twice a year, Nordea – with the support of our external partner, Ethix – screens all our funds to identify companies violating international norms related to human rights, labour rights, environmental protection and anti-corruption.

We believe in the means of active ownership and engagement to improve the behaviour of companies identified to violate international norms. We see this as a more responsible and constructive approach than simply divesting from a company.

If an engagement, however, does not proceed or the company is unwilling to change, we may decide to divest from the company.

The norm-based screening is based on the following initiatives and guidelines

- the United Nations Global Compact
- the OECD´s guidelines for multinational companies
- the Universal Declaration of Human Rights
- the International Labour Organizations´s Declaration on Fundamental Principle and Rights at Work
- the Rio Declaration on Environment and Development
- the United Nations Convention Against Corruption

Excluded Companies

If a company doesnot show true will to change its norm-breaching behaviour, Nordea's committee for Responsible Investments can decide to divest these investments from all fund portfolios. In 2012, Nordea excluded companies that contribute to the production or development of new nuclear weapon programs. Nordea sees nuclear weapons and their potential use as controversial, given their indiscriminate effect on human populations. This decision was in line with Nordea policy of illegal weapons (cluster munitions, etc.) which was implemented in 2010.

List of companies excluded from Nordea's funds:

Aeroteh S.A.	Involvement in cluster munitions
Alliant Techsystems Inc.	Involvement in cluster munitions
Aryt Industries Ltd	Involvement in cluster munitions
Babcock International Group	Involvement in nuclear weapons
BAE Systems plc	Involvement in nuclear weapons
CEMEX	Human right violations, extraction of non-renewable resources from occupied territory
Doosan Corporation	Involvement in cluster munitions
European Aeronautic Defence and Space Company EADS N.V.	Involvement in nuclear weapons
Finmeccanica	Involvement in nuclear weapons
General Dynamics Corporation	Involvement in cluster munitions & nuclear weapons
Hanwha Corporation	Involvement in nuclear weapons
Huntington Ingalls Industries Inc.	Involvement in cluster munitions
L-3 Communications Corporation	Involvement in cluster munitions
Lockheed Martin Corporation	Involvement in cluster munitions & nuclear weapons
Motovilikhinskive Zavody OAO	Involvement in cluster munitions
Northrop Grumman Corporation	Involvement in nuclear weapons
Poongsan Corporation	Involvement in cluster munitions
Potash Corporation of Saskatchewan	Violation of human rights related norms
Rolls-Royce plc	Involvement in nuclear weapons
Safran Group	Involvement in nuclear weapons
Singapore Technologies Engineering Ltd	Involvement in cluster munitions & anti-personnel mines
Textron Inc.	Involvement in cluster munitions
United Technologies Corporation	Involvement in nuclear weapons

ESG integration

"ESG issues are increasingly important in the risk/reward equation. Integration is therefore vital to our business and how we generate returns for our clients".

Christian Hyldahl, Head of Investments, Nordea Asset Management

In 2013, Nordea Asset Management decided to take the initial steps towards ESG integration into all investment processes.

Environmental, Social and Governance issues are an increasing source of risk and opportunity. Therefore we want to integrate ESG issues into our investment analysis methodology. Potentially this is a source of better performance and at the very least it is a way of controlling risk in an investment portfolio. Good returns for our customers are the focus for Nordea Asset Management and so we need to take ESG issues into account in all our investment products.

This has the added advantages for customers of increasing transparency so clients will know how we are handling ESG issues. This information can in turn be passed on to the customers' stakeholders as part of their communication on how their money is invested. ESG-integration will strengthen Nordea's profile as being one of Europe's leaders in responsible investments. "Money that has been earned in a responsible way should also be invested in a responsible way," says Allan Polack CEO of Nordea Asset Management.

Listen to Portefolio Manager Claus Worm who shares his views on full environmental, social and governance investment integration

Interview, Claus Vorm, Portfolio Manager, Stable Equities, NIM

Could you briefly explain how the Stable Equity process works?
It is an innovative process focusing on stability and valuation, designed to participate in the equity markets' performance with good downside protection.

How do you define ESG risks?
ESG risks in relation to Stable Equities are risks related to EGS issues that are severe enough to impact the future performance of a company.

Do you think ESG factors influence the short-term and/or the long-term performance of your portfolio?
I think ESG factors influence both the long-term and the short-term performance of a company. However, how it will influence the share prices depends on how the ESG factors are incorporated in the share price. For example, if ESG risks are not reflected in the share price and some ESG risk starts to materialise, the share price will react immediately.

Will ESG data integration strengthen your process?
For sure. All risks that potentially can impact the companies we are investing in are relevant. And for some companies the ESG-related risks can be quite severe.

How do you combine ESG data with traditional financial analysis tools?
The ESG data is incorporated in the fundamental risk assessment. We try to assess the risk and then evaluate if the risk premium is attractive compared to the estimated risk premium for the company.

For what specific types of companies can the ESG data help you detect/reveal hidden threats or opportunities?
In relation to Stable Equities we are mainly focused on the risk dimension and less on the opportunities given our focus on stability in our investment process. The ESG data is very efficient in terms of disclosing risk factors in a transparent and structured way, which helps us to assess the potential risks. Examples of ESG-related risks could be an energy company with poor operational procedures resulting in a high risk of pollution or a healthcare company with a very focused product line and bad quality control resulting in a high risk of product recalls.

Occupied areas investment policy

Nordea Asset Management has decided to engage with companies that are violating international norms through direct involvement and operations in the Israeli occupied territories.

- **Companies directly engaged in settlement activity**
- **Companies extracting non-renewable resources from the territories**
- **Companies providing products and services to the settlement security infrastructure**

In line with the overall responsible investment policy of Nordea Asset Management engagement is in focus as a first step of action. The decision regarding the Israeli occupied territories has resulted in engagement with five companies, monitoring for two companies and exclusion of investments in one company.

Corporate Governance activities in Sweden 2013

Nordea's funds strive to be an active owner and influence the companies in which we are invested. We strongly believe that a positive long term development in the companies is good for shareholders, employees and other stakeholders.

Nordea's corporate governance activities are primarily focusing on companies where our funds have holdings of such a size that our decisions have significant importance for a company's development and where we are expected to take an active ownership role. In the beginning of 2013 the funds had holdings of more than five percent of the capital in 42 companies and of more than three percent in 95 companies. The absolute majority of these companies are Nordic and about two thirds are Swedish.

Nordea's funds have during the year participated in well over 100 Annual General Meetings (AGM) in Nordic companies and, through proxies, we have voted at about 70 AGMs outside the Nordic countries.

During the spring of 2013 Nordea's funds were represented in 28 **nomination committees**. These committees normally consist of the three to four largest owners and have the tasks, among other things, to each year propose members of the Board of Directors to the AGM as well as evaluating the performance of the existing Board. In about 70 percent of the Boards there were changes and 24 new members were recruited by the Nomination Committees.

Before the AGMs we had dialogues with a number of Boards concerning the design of their companies´ **incentive programs** for leading executives. In addition to that, we have also considered a large number of incentive programs in companies where our ownership has not been sizeable enough to motivate direct dialogues with the companies pre-AGM. Generally speaking, we think that during the past years incentive programs largely have had a good design with clear performance requirements, own investment, reasonable dilution and costs. But there are many examples where incentive programs have become too complex.

We also noted at the AGMs in 2013 that there were a number of proposals, mandating the boards to decide on **right issues** against cash without pre-emptive rights for the shareholders. We think that this type of capital increase has clear disadvantages for existing shareholders and therefore we normally act against these proposals with the aim to change or modify them.

A specific example of Nordea's active ownership is Scania's AGM in 2013 where we voted against VW/MANs proposal to abolish the nomination committee. During the autumn, we continued to be an active shareholder in Scania and are now participating in "Scanias vänner" – a newly formed club/association of the larger institutional shareholders in Scania. The purpose is to ensure a correct treatment of the minority shareholders. More specifically, "Scanias vänner" wants to make sure that the synergy gains obtained through the cooperation between Scania and MAN are passed on to all shareholders in a fair way.

During 2013 we established a document called **Stewardship Framework** in which we have developed and formalized our principles for Responsible Investments and Governance. One corner stone of the framework is that we now integrate corporate governance together with traditional financial analysis in our investment decisions. Furthermore, we engage with invested companies on issues such as shareholder rights, board compositions, board and executive remuneration as well as risk management.

The right to vote is an essential part of a well-functioning corporate governance system and we therefore exercise this right, whenever relevant. We expect full and transparent disclosure from companies to enable wellinformed investment decisions and effective exercise of shareholder rights and responsibilities as part of the company's system of governance. We also expect companies to make available to shareholders complete materials for general meetings in advance of the meetings.

Nordea's funds portfolio is global and diverse. We invest in approx. 7000 companies worldwide. When deciding how to vote, we take into account the specific context and market in which the company is active and domiciled. In order to improve our ability to vote globally we have carried out a pre study for a proxy voting project during the autumn of 2013. The ambition is to start a proxy voting project during the first half of 2014 which will enable us to proxy vote for all our holdings globally. The voting policies would be based on the stewardship framework and our International Corporate Governance Principles. Through this project our corporate governance activities will have a stronger international focus than earlier.

Thematic research: Responsible tax policies

In 2013, RII conducted thematic research on corporate tax practices in terms of companies' policies, strategies, management practices and transparency. As part of the project RII had a number of meetings with tax experts, NGOs and company representatives.

Recent years' weak economic development has put pressure on many governments and increased their need to generate tax revenues. Simulatenously, companies' tax practices have come under scrutiny in the public debate raising risks associated with aggressive tax planning practices.

Multi-national companies (MNCs) have the legal right to minimize their tax burden by for example utilizing specialised economic zones (SEZs) or by shifting their profits to jurisdictions known as low-tax jurisdictions. Even though a majority of companies' tax schemes comply with laws and regulations they can still be aggressive and perceived as irresponsible by stakeholders. Aggressive corporate tax structures lead to several problems, such as an uneven playing field between MNCs and local businesses, while also undermining national development by eroding countries' tax bases. The latter is crucial for successful state-building, especially in developing markets; furthermore, taxation is known to render such countries more independent as it reduces their reliance on aid and foreign loans.

Business case for responsible tax practices

There are apparent reputational risks associated with aggressive tax practices. In recent years, global media has reported several cases of corporate tax avoidance, which has increased public awareness of the issue. For example, Starbucks has been covered in several media stories due to its tax avoidance strategy, which has led to boycotts as well as parliamentary hearings in the UK.

A modern way of doing business goes beyond delivering returns to shareholders; consideration is also paid to the impact businesses have on the environment and communities in which they operate. By paying taxes companies contribute to for example the development of health care systems, schools and the local infrastructure. Tax avoidance, especially in developing countries where the need for funding is often acute, may erode peoples' trust in the companies and in turn damage their local community relations and, possibly, in the long-term, their license to operate.

There are also direct financial risks associated with aggressive tax practices as it increases the likelihood of a tax audit, which in turn can lead to an increased tax liability. The Convention on Mutual Administrative Assistance in Tax Matters, developed already in 1988 and amended in 2010, is a multilateral cooperation open to all countries, which aims to tackle tax evasion and avoidance. Currently over 60 countries have signed the Convention, representing a wide range of countries, including all G20 countries, almost all OECD countries, major financial centres and a growing number of developing countries.

Key conclusions

As a responsible investor, Nordea Asset Management seeks to invest in companies that manage all relevant corporate responsibility risks and opportunities adequately, here amongst tax practices. There is a clear reputational risk associated with aggressive tax planning, which is indicated both by our meetings with companies, NGOs and tax experts as well as recent years' media coverage.

We assess that aggressive tax planning can largely be tackled through improved corporate reporting and transparency. This would limit the ability of companies to work with aggressive tax planning and would allow for them to build greater trust with their stakeholders. However, action is needed not only by companies and investors, but also by governments and regulators.

We favour companies with a responsible tax policy that is approved by its board. Companies should also have a tax strategy that explicitly considers brand- and reputational risks. In terms of transparency, we as a first step encourage companies to publish their tax policy and/or a statement reflecting their tax policy and strategy.

Thematic research: Clinical trials

One of the major criticisms of the bio-pharmaceutical industry is a lack of transparency of clinical trial results. Although regulation has improved, we as investors have a responsibility to make sure that companies are behaving correctly by looking and asking for a detailed description of how they comply when it comes to clinical research. During 2013, we therefore developed a position paper concerning clinical trials outside of Europe.

Clinical trials that test medicines for use in the European Union (EU) increasingly take place in low and middle income countries (new markets), for example Argentina, Brazil, China, India, Peru and South Africa. The relocation takes place by offshoring and/or outsourcing.

Speed, cost cutting, access to vast genetic populations and prospective markets are among the drivers of relocation.

All of these markets have a common denominator; vulnerable trial participants. All patients participating in clinical trials, regardless of location, are vulnerable as they are ill and in need of medical treatment. What makes the trial participants on these markets particularly vulnerable is a combination of poverty, illiteracy and inefficient monitoring of participants. These circumstances do not automatically make it unsuitable to conduct clinical trials on these markets. However, it makes it absolutely crucial to comply with regulations and enforce ethical guidelines.

There is one guideline that prevails and that is referred to in national legislation in several countries – the ICH GCP Guideline. All companies shall conduct clinical trials in compliance with this guideline. Patient safety and ethical conduct are at its core.

- Principle 2.3 in the ICH GCP states that "the rights, safety, and well-being of the trial subjects are the most important considerations and should prevail over interests of science and society".

The pharmaceutical company holds the legal responsibility of a clinical trial, regardless of location and whether it is an in-house or outsourced clinical trial. Over the years it has become increasingly common that companies outsource the clinical trial to contract research organisations (CROs). However, the responsibility and accountability of the pharmaceutical company remain, and regulation has tightened, which makes supply chain management essential to pharmaceuticals in the development of new products.

If a product is to be registered in Europe, the clinical trials that have rpeceeded the application must comply with the Declaration of Helsinki (the global ethical standard that forms the core of ICH GCP) and be in harmony with European standards.

Whether the management systems that are in place today are adequate in protecting trial participants is hard to verify independently due to a lack of transparency of the audit results, in combination with instances of insufficient monitoring by authorities.

The view raised by watchdogs on clinical trials in new markets differs significantly from the views presented by the industry and national authorities. The biased views make it more difficult to understand the actual state.

- The industry generallypresents policies and guidelines, description of due diligence and audit processes and claim that all clinical trials are conducted with the principle hat they must pass a third party inspection and regulatory supervision. They also present the case of access to medicine as an important positive out come of relocating clinical trials to new markets.

- Representatives from the national medical product agency claim that scrutiny is possible and effective despite offshoring and outsourcing, and that international mandatory registrations system are designed to protect patient safety and that these systems are hard to cheat. All in all, the combination of smart system design, evaluation of applications and inspections contributes to proper corporate behaviour There is no business case to perform clinical trials in an unethical or dubious manner.

- Watchdogs claim that transparency is weak and hinder interested bodies to monitor company behaviour. They further claim that accountability is very rare and that monitoring by designated authorities is inefficient in too many cases. They claim that the risk for a pharmaceutical company to be "caught" and held accountable of ethical misconduct may exist in theory, not so much in reality. The inefficiency in monitoring and the lack of accountability is considered to put trial participants at risk. They present cases of violation of ethical guidelines where patient safety has failed.

Key findings

- Clinical trials in new markets have the opportunity to bring access to medicine and know-how, if conducted properly
- Transparency could improve, enabling interested parties to monitor companies' behaviour
- Accountability for ethical misconduct is rare
- Proof of enforcement of principal ethical standards and guidelines is seldom public
- Monitoring by authorities and other national/regional bodies lacks resources and is sometimes insufficient
- Trial participants are particularly vulnerable and their rights are not always safeguarded, resulting in violation of their rights and harming their health
- Several companies seem to have elaborate systems to manage their supply chain with regard to applicable guidelines and ethical standards, but disclosure must improve to enable evaluation of efficiency

Download the full report on esg.nordea.com

Field visit: ESG trends in Russia

A deep understanding of the companies in which we invest is crucial for our assessment of their ESG risk profiles. Field visits are an invaluable source of first-hand information, especially in traditionally high-risk regions.

In January 2013, the Nordea Responsible Investments & Identity (RII) team went to Moscow to discuss ESG issues with a number of Russian companies. We met with a norm-breaching company to start a dialogue on environmental management as well as six potential candidates for inclusion in the portfolio of the ESG-enhanced Emerging Stars fund. Though Russia is a challenging market where ESG risks on different levels generally remain, we did see improvements and positive developments in the way companies address ESG risks in their operations.

Russia is a country that embodies a lot of controversies and challenges. The country ranks 133rd out of the 174 countries on the Transparency International Corruption Index and it is heavily exposed to the oil and gas sector, which involves a lot of ESG risks. Greenpeace has for example reported that there are more than 20,000 leaks or breaks in pipelines every year causing oil spills, some small, some large. Many Russian companies also show a general lack of transparency.

However, awareness of ESG risks and what these risks may mean for companies is increasing, driven by both increased legislation and demand from both foreign investors and the general public.
Among the companies we visited in Moscow, we noted a high awareness of ESG risks as well as management commitment, with systems in place to follow up on these issues. We met with companies from different sectors, ranging from retail, to banking, mining, and theoil and gas sector.

Key take-aways from our visit

Several of the companies we met with have actually implemented ESG risk management systems in line with those of their Western peers. One fertilizer company, for example has had its environmental management systems certified and also demonstrated good improvements in its environmental KPIs. However, most of the companies lag behind when it comes to reporting and communicating how they work with ESG issues.

We would like to see increased transparency among the Russian companies towards investors, stakeholders and the society at large about how they work to manage their ESG risks. Taking the positive momentum we saw during our trip into account, we do, however, believe that we will see improvements in this area in the years to come.

Field visit: Challenges and opportunities in South Africa

At the end of June 2013, members of the Nordea Responsible Investments & Identity team went to Cape Town and Johannesburg to participate in the annual PRI conference on responsible investments and to carry out ESG studies in South Africa. We also met with potential and current company investment candidates for inclucion in the portfolio of the Emerging Stars fund, to discuss ESG issues.

South Africa has a complex history and still faces severe challenges – but also opportunities. The country has a high level of inequality as indicated by its GINI coefficient of 65 (by comparison, the same figure for the Nordic countries is 25). Unemployment is high at 25.6%, with an even higher rate of youth unemployment. Social tensions and labour disputes have increased, and in general the country has a high exposure to ESG risk sectors such as mining (gold and platinum). Moreover, water scarcity is increasingly becoming a problem in South Africa, adding to the multitude of challenges the country faces.

The government, investors and companies have, however, taken vital steps to address these challenges. The government has launched a black empowerment initiative (B-BBEE), aimed at supporting black labour also for higher positions. Moreover, in 1994 the King Report on Corporate Governance, saw the light of day, and since then South African companies have implemented corporate governance practices in line with their western peers and far beyond their emerging markets peers*.
In addition, the Code for Responsible Investing in South Africa (CRISA) was launched, which aims at supporting and advocating responsible investment practices by South African investors.

We met with seven companies from different sectors in South Africa (including the retail, telecommunications, health insurance, media and palladium mining sectors). The key take-away from the trip is that although practices vary largely, also within sectors, several companies seem to have a good management approach and show commitment when it comes to addressing both ESG risks and opportunities in their operations. One retailer we spoke to works extensively with initiatives to reduce its energy consumption. It also works locally with suppliers to encourage more sustainable farming practices. By expanding access to telecommunications in different African countries, a telecom company that we met with is not only supporting its own business development; it also supports underserved and less developed areas by offering access to telecommunications services, thereby making it possible for the inhabitants in these areas to access finance and health services over smartphones and closing the digital gap. In other words, these companies are contributing to spurring economic and social development in the regions they operate in. One health insurer we met aims at more than just profiting from health insurance; it also has several initiatives in place to encourage a healthier lifestyle among its members and society at large.

Challenges in South Africa still prevail, e.g. high rates of inequality and unemployment, growing risks stemming from water scarcity and a threatened biodiversity. However, our meetings illustrate that many South African companies wish to step up to these challenges and not only address their ESG risks, but also be a positive factor and contributor in the societies in which they operate. This is positive for the development of South Africa.

* MSCI report (“ESG Country Report: Identifying ESG risks in South Africa”) September, 2013

2013 Annual PRI conference, Cape Town

Emerging Stars & Swedish Stars

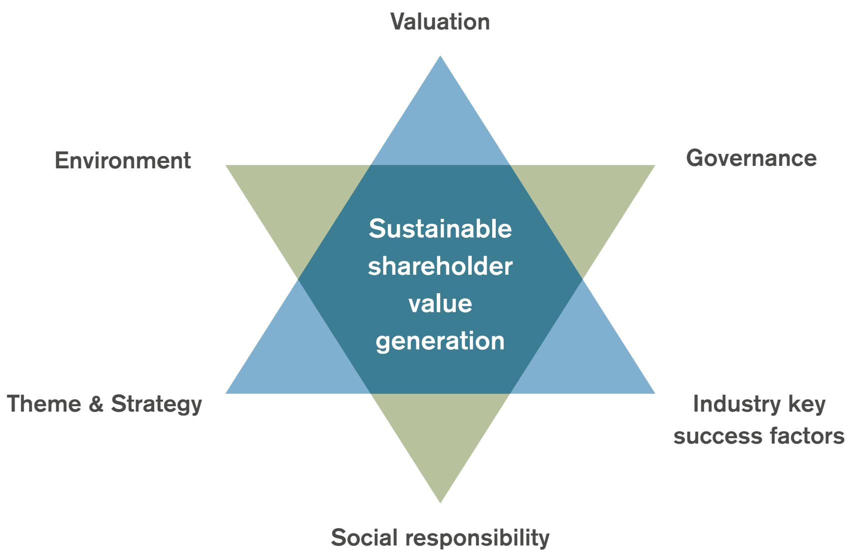
The Stars: next-generation ESG funds

Nordea has established two investment funds dedicated to creating strong returns by investing in the best companies with strong, responsible practices.

Companies in our Stars portfolios are assessed on how they manage risks and opportunities related to environmental protection, human rights, labour standards and business ethics. Our aim is to identify key issues that are of material relevance for the company to address, today and in the future.

We believe that companies actively working on these issues and having a clear governance structure for dealing with these aspects are exposed to less risk. This creates a solid foundation for better returns in the long term.

The Emerging Stars Investment Process



Swedish Stars

Swedish Stars is a focused equity fund investing in companies that are in the forefront in its management of key environmental, social and business ethics aspects. New holdings in the fund meeting our criteria are Millicom and Autoliv, while the holding in StoraEnso has been divested.

2013 was a very good year for Swedish equities. Small caps, but also financials showed the strongest performance. Swedish Stars focuses on well-run large and mid-cap companies which, together with a cautious view on banks, explains the somewhat weaker performance for the fund than for the overall market. JM, Millicom and Nibe were the best contributors in the fund, while Volvo, Elekta and Boliden contributed negatively to performance.

During 2103 Nordea re-visited H&M suppliers in Bangladesh and Cambodia after a series of allegations in global media regarding workers rights in the garment industry

Emerging Stars & Swedish Stars

Swedish Stars

Millicom

The telecommunication services company Millicom is a new holding in Swedish Stars. The company offers fixed and /or mobile services in 13 countries in Central America, South America and Africa. We think the company has several growth drivers that are underappreciated by the market such as mobile data, online investments, mobile financial services and high growth cable assets. Millicom's products and solutions also contribute to improved social standards and enable the society that the company operates in to grow. Examples are financial and health services through the mobile. Millicom has improved governance of key issues and is underway to establish new sustainability targets. The CSR board together with the head of CR, reporting to the CEO, indicate a commitment to limit risks, but also to capitalize on opportunities. Several policies addressing Environment, Anti-Bribery/Corruption and Labor issues have been established and the company is working to improve transparency of protecting privacy.

Autoliv

Autoliv, also a new holding in Swedish Stars, is a global market leader within automotive safety with a global market share of 35-40%. Going forward, the current shift to active safety products will be a main volume driver for the industry. We believe Autoliv will be one of the winners also within active safety as the combination of Autoliv's dominating size and R&D efficiency support innovation and new product launches. Autoliv has increased its commitment to sustainability and also transparency is going to be improved. The company has identified key ESG risks and opportunities and relevant policies are in place, but management and reporting of the performance related to environmental and social risks could still be developed. We have visited their factory in Turkey and have had several meetings with the company during the year. The company's processes to handle health and safety risks, working conditions and unionization are far more developed than what has been publicly communicated. Major risks for the company are related to supply chain management and labor management of the production sites.

StoraEnso

In early May of 2013, we visited the pulp and paper company Stora Enso's operations in China. The purpose of the visit was to evaluate the social consequences of the company's establishment of large eucalyptus plantations. In light of the risks we identified and the substantial room for improvement in the way the company has handled these issues, we chose to sell all shares in the company.

Case: Millicom

Millicom provides telecom solutions to a number of emerging market countries in Latin America and Africa. One of its current hot spots is DR Congo, which is primarily known for long lasting civil wars – but also as a growing market for mobile financial services.

Nordea is among the single biggest investors in the Global telecom brand Millicom. Follow Nordea's head of Responsible Investments and Identity Sasja Beslik to DR Congo when he investigates how Millicom services can improve social conditions in the local communities.

Listen to Millicom's local CEO, Stéphane Teyssedre, who shares his views on how to create a sustainable and profitable business model in one of the worlds most war thorn markets, DR Congo

Emerging Stars & Swedish Stars

Emerging Stars

Emerging Stars is an equity investment fund investing in the global emerging markets. The fund focuses on investing in a small selection of the very best companies: the "Stars". The selection methodology integrates environmental, social and governance (ESG) aspects into the heart of the investment process with a clear purpose. The best companies are also defined as those that run their businesses in the most sustainable and responsible way.

The ESG research methodology is a combination of two distinctive approaches. Star companies conduct their business responsibly versus all their stakeholders, be they employees, suppliers, customers, investors or the society at large. At the same time, star companies position their products well in relation to sustainable megatrends such as climate change or changing demographics.

Since inception of the fund almost three years ago, we have conducted detailed ESG analysis in-house with the help of our research partners MSCI, Eiris and Solaron. Based on this analysis we have identified 180 companies with the corporate responsibility profile required to be a 'Star'. Detailed financial analysis determines the final, concentrated, long-term, low-turnover investment portfolio of 40-60 equities with an average holding period for each stock of around three years.

The investment performance has been exceptional. Since its inception in 2011, the fund has outperformed its reference index by over 10% in total. The risk-adjusted performance has been particularly good, with the information ratio hovering above 1.5 and clearly indicating that sustainable and responsible companies can improve both the return and the risk metrics of an investment portfolio.

We have met with senior representatives of all the companies in the portfolio, and we frequently travel the global emerging markets to discuss both financial and ESG issues, to make sure that all investments maintain their Star potential. Moreover, we seek to engage with companies that have financial potential, but expose themselves to unnecessarily high ESG risks. We have encouraged many companies to improve their ESG management on all continents and as a result, we understand the ESG issues in emerging markets better. But more importantly, we have also influenced some companies to run their businesses in a more sustainable and responsible manner.

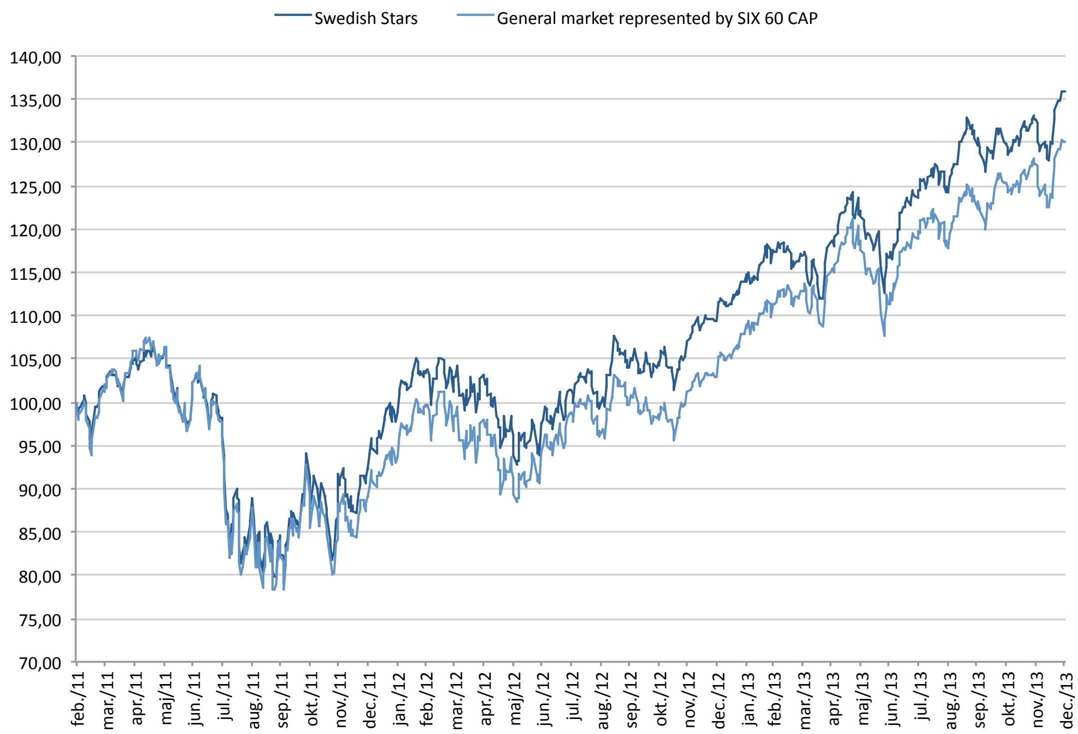
While the merits of ESG integration can and should be debated, we are confident that our "Stars"-approach not only boosts investment performance, but also makes the world a little bit better.

“Stars” Case: China Everbright International

China Everbright International (CEI) has positioned itself as the environmental investment arm of its parent. CEI primarily engages in environmental protection projects such as sewage water treatment, waste-to-energy power plants and solid waste disposal. As an established waste-to-energy and wastewater treatment player in China, CEI should be a key beneficiary of the rapid growth in the Chinese environmental protection sector. In addition, the company's project pipeline is relatively transparent with projects worth CNY 5bn currently under construction, including investments in wind and solar power. To summarize, CEI's product portfolio is very well suited for "Stars" portfolios.

CEI demonstrates strong commitment to sustainable development and corporate responsibility. This is evident not only in its line of business, but also in the way it operates. The company focuses on fostering talent and recruiting and retaining the best employees. It has a strict non-discrimination and fair compensation policy as well as training and health and safety policies in place. These are all important factors in fast-growing economies, but particularly in China where well-educated employees are not easy to recruit and retain. CEI has a thorough code of conduct in place, which is upheld through internal audit. The audit follows international best practice, and reports are sent directly to the company's independent audit committee. This is important from a risk management point of view as the company is operating in a country marred by high rates of corruption among businesses dealing with government authorities and is therefore predisposed to corruption.

Performance chart: Swedish Stars



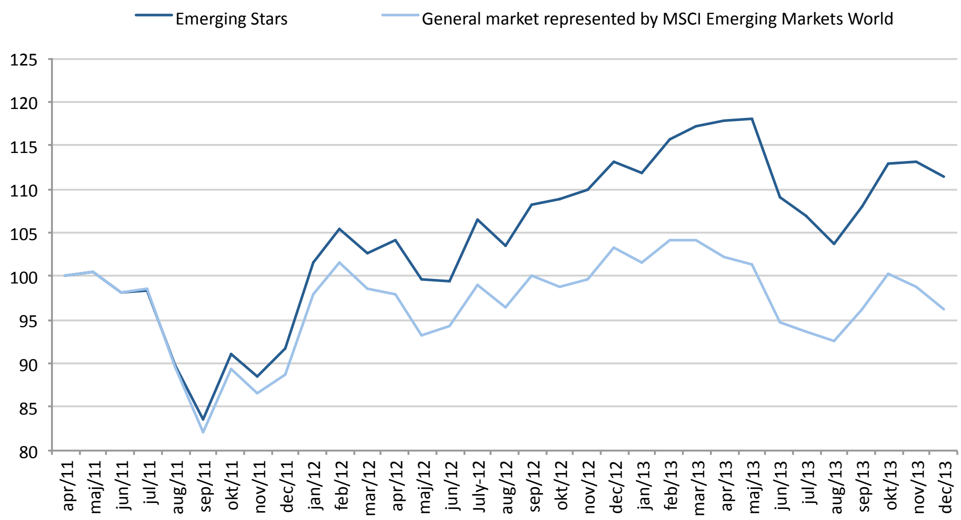
Swedish Stars Biggest holdings %

Volvo 7,6
Millicom 7,3
Sandvik 7,2
H&M 7,1
ABB 6,8
AlfaLaval 4,4
SEB 4,3
Tele 2 4,3
Elekta 4,1
Getinge 3,8

Major changes

Buying Millicom and Autoliv
Selling Swedbank, Stora Enso and Nibe

Performance chart: Emerging Stars



Emerging Stars Biggest holdings %

Samsung Electronics 6,4
Tencent 5,2
Taiwan Semiconductor Manufacturing 4,5
Naspers 3,8
Ping An Insurance Group Co of China 3,7
Media Tek 2,9
China Everbright Int 2,6
Eurasia Drilling 2,6
China Mobile 2,5
Tata Motor 2,3

Major changes

Buying China Everbright Int.
Selling SQM and Bradesco

Nordea's participation in international initiatives

As the largest asset manager in the Nordic region we seek to encourage best practice through active participation in international initiatives.

Principles for Responsible Investment

As one of the first major banks in the Nordic countries, Nordea on the1st of November 2007 signed the United Nations Principles for Responsible Investment (PRI). At the same time our policy for responsible investment was launched. This policy shows how we adhere to the six principles. We report on our activities and progress in implementing the PRI. This report is public and available on the PRI website.

In 2013 Nordea participated in collaborative PRI engagement activities focusing on minimising ESG risks associated with oil sand operations and fracking. We have also been involved in an engagement focusing on water scarcity and the related risks to investors.

UNEP FI

Nordea co-chairs the United Nations Environment Programme Finance Initiative's (UNEP FI) Water and Finance Work Stream (WFWS).

CDP

Nordea is a signatory to the CDP, a project which aims to collect and spread information on greenhouse gas emissions and climate change strategies. Nordea uses the database information in its ESG analysis. The CDP is a cooperation arrangement between 655 institutional investors combined representing assets of USD 78 trillion.

Water Disclosure Project

Nordea is a signatory to the Water Disclosure Project. The project is an initiative run by the CDP and is supported by institutional investors. The aim of the project is to collect and spread information concerning water-related risks and possibilities and addresses more than a thousand global companies with water-intensive production or water-related challenges.

CDP Carbon Action

Carbon Action is an investor-led initiative to accelerate company action on carbon reduction and energy efficiency activities, which deliver a satisfactory return on investment. 190 investors with US$ 18 trillion in assets under management ask the world's highest emitting companies to make emissions reductions (year-on-year) with publicly disclosed targets.

Extractive Industries Transparency Initiative (EITI)

Nordea is a supporting investor to the Extractive Industries Transparency Initiative (EITI). The initiative is a multi-stakeholder coalition of governments, companies, investors and civil society organisations. The aim of the initiative is to ensure transparency and accountable management of revenues from natural recourses.

Sustainable Investment Forums

Nordea actively participates in local sustainable investment forums, so-called SIFs, which are independent national forums that promote responsible investment. Nordea became a member of SWESIF in 2008 and DANSIF in 2010. Nordea was further a founding member of FINSIF launched in June 2010 and NORSIF launched in February 2013.

Nordea is represented on the boards of FINSIF (as vice chairman) and NORSIF.

The Institutional Investor Group on Climate Change

Nordea is a member of the IIGCC, together with 80 other pension funds and asset managers. This is a forum for collaboration on climate change for investors. IIGCC encourages public policy, investment practices and corporate behavior that address long-term risks and opportunities associated with climate change.

An ongoing process

- **2002**: Nordea launches first ethical funds. Nordea has been working with governance issues since the 1980s
- **2007**: Signs UNPRI and launches policy on Responsible Investment
- **2008**: Initiates engagements in new companies
- **2009**: Signs Carbon Disclosure Project
- **2010**: New Strategy and Policy. Initiates engagements in new companies. Establishes in-house ESG method
- **2011**: Launches unique RI funds. Initiates engagements in new companies
- **2012**: Excludes companies involved in nuclear weapons
- **2013**: Implements integration project

Responsible Investments & Identity

Annual Report • 2013

Published by: Nordea Investment Funds
Photo: RII-team, Panthermedia
Graphic design: IMMERFRISCH
Sources: Ethix SRI Advisors, Hermes Equity Ownership Services, MSCI, UNCTAD
March 2014