PFA'S COUNTRY SCREENING PROCEDURE FOR INVESTMENT IN GOVERNMENT BONDS

It is PFA's responsibility to invest in government bonds in a responsible manner. The investments must comply with the general and internationally recognised standards for responsible investment. For this reason, PFA screens countries parallel to the half-yearly screenings of corporate shares and bonds. The screening is a three-step process[1], which includes a number of indicators and country-specific information that are relevant to the assessment of a country, the population's needs and the overall situation in the country.

Country screenings represent the implementation of criteria and process in accordance with PFA's guidelines for responsible investment in government bonds. The screening process incorporates international standards and is based on the most recognised indices. The screening forms a clear and fact-based basis of decision for PFA's RI Board, which is the body that determines whether a country is suitable for investment or not. PFA does not regard engaging in active ownership over foreign states as an opportunity for investors as this is a foreign policy issue.

A developing process

No fixed criteria or principles to assess countries exist. The Danish Council for Corporate Responsibility has drawn up a guide for responsible investment in government bonds, which describes various elements that it recommends be taken into consideration.

PFA has selected the criteria that are used in PFA' screening process. The process will be evaluated on an ongoing basis, and it will, to the extent necessary, be adjusted according to the current circumstances.

Selection of criteria

In the screening process, PFA uses a combination of a sanction- and norm-based approach. This means that PFA screens for whether the country violates international sanctions, PFA's guidelines or the international standards which PFA has committed to comply with by signing UN Global Compact and PRI[2].

At all three steps in the screening process, current events which have not yet been included in the recognised sources may be considered to be of such importance that PFA's RI Board may make a decision that deviates from the immediate screening result.

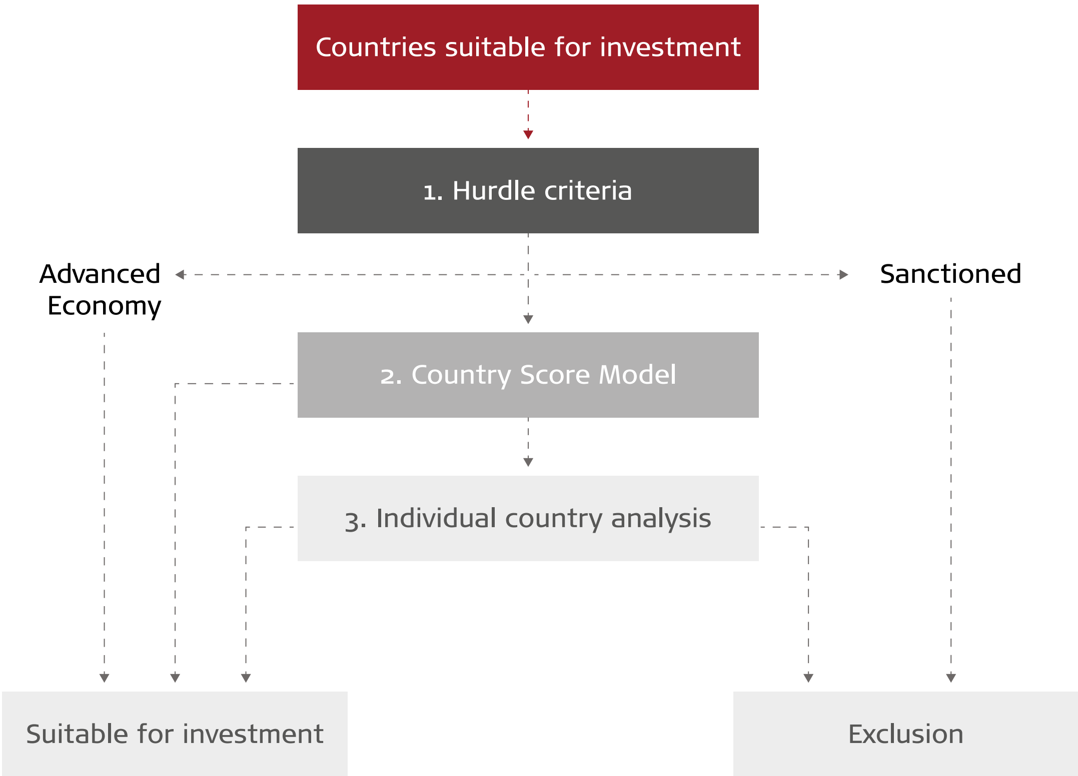
1 The three steps only assess whether a country is suitable for investment according to PFA's guidelines for responsible investment and do not take the credit and investment analysis into account.

2 The screening process is developed on the basis of the integration of the due diligence principle as described in the UN Guiding Principles on Business and Human Rights.

PFA'S COUNTRY SCREENING STEP BY STEP

The screening consists of three steps and is based on all countries in which it is possible to invest

It is possible to invest in approximately 2/3 of all countries. This means that it is not possible to invest in a number of countries, such as North Korea, Syria and Iran, along with a wide range of countries in which investment is not possible in practice because the countries have not issued any bonds or no market exists.



First step – Hurdle Criteria

The first step includes both minimum and maximum criteria and thereby directly defines a number of countries which are immediately suitable or unsuitable for investment, respectively. The rest of the countries proceed in the screening process:

A If a country is categorised as an "Advanced Economy" by the IMF, it will automatically be accepted as suitable for investment. This criterion means that countries which are approximately at the same level of development as Denmark are considered suitable for investment.

B If any international sanctions exist against purchasing national debt in the country, it will automatically be declared unqualified for investment.

Second step – Country Score model

The second step, the Country Score Model, includes a number of internationally recognised indicators and indices which cover both human rights, employee rights, the environment and anti-corruption. The model also includes relevant international financial or trade sanctions in which Denmark participates. It is a quantitative assessment of the country based on a range of different indicators that have been selected to evaluate the country's level according to the UN Global Compact's ten principles. As a starting point, the indicators used are based on official and recognised sources from the World Bank, IMF and UN. When using other sources, the nature and the purpose of the indexation are taken into account. Each country is ranked in category 1, 2 or 3 for each indicator in proportion to the other countries which are not categorised as an 'Advanced Economy' by the IMF.

Based on the results from the Country Score Model, PFA's RI Board assesses which countries should undergo a qualitative individual analysis.

The Country Score Model is based on the following indicators:
Global Peace Index
Freedom House Index
Human Development Index
Corruption Perception Index
Worldwide Governance Indicators
Press Freedom Index
Doing Business Index
Environmental Performance Index
EIU Country Risk
EIU Democracy Index
EIU Political Risk Index

Third step – Individual country analysis

The third step, the country analysis, is based on a range of descriptive indicators from internationally recognised sources, which contribute to identifying the country's and the population's situation and development in a number of areas, etc. The analysis assesses whether the situation in the country is improving, stabilising or worsening, and whether any special conditions or needs favour investing in the country's development and population. The analysis is based on a standard format which consists of a number of criteria that are reviewed based on different sources. The purpose of the country analysis is to look closer into those areas in which the country ranks the lowest in the Country Score Model. Thus, the analysis contributes to the assessment of whether the situation in the country is due to irresponsible behaviour or other causes.

Based on the analysis, PFA's RI Board decides whether the country is suitable for investment or not.

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