



# Understanding BMO's ESG ETFs

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For more information on the topics in this booklet, or for additional information on BMO funds of ETFs, please visit our website at [www.bmo.com/gam/ca/advisor](http://www.bmo.com/gam/ca/advisor)

# What is Responsible Investment?

“Responsible investment is an approach to investing that aims to incorporate environmental, social and governance (ESG) considerations into investment decisions, to better manage risk and generate sustainable, long-term returns.”

— UN Principles for Responsible Investment



## Environmental

- Climate Change
- Water Management
- Pollution



## Social

- Labour Standards
- Human Rights
- Health and Safety



## Governance

- Executive Pay
- Business Ethics
- Corporate Governance

## Why ESG matters to you

Align client sustainability preferences with investments

Build a higher quality portfolio – potential to improve risk adjusted returns

Get ahead of potential future regulation changes

Wealth Transfer - Millennials and women putting a higher value on sustainable investments

## Re-introducing ESG

Both the values-driven and the valuation-driven approaches have been practiced by responsible investors. There is no one-size-fits all, and many strong cases exist to be a responsible investor: values-alignment as well as the materiality of ESG issues. There are different strategies available to serve the diversity of responsible investors, including ESG integration, shareholder engagement, screening, thematic and impact investing.



In the early 2000's it was about values, with mandates focused on exclusions. This approach evolved to focus on valuation, and using ESG analysis to identify risks and opportunities that may not be visible in traditional financial metrics. This led to the widespread adoption of inclusionary responsible investment strategies such as stewardship and ESG integration. Since then ESG investing has evolved to include more thematic approaches focusing on specific ESG issues by investing in solutions which address them. Examples include but are not limited to, funds related to women in leadership, cybersecurity, climate or renewable energy.



There are many drivers to the evolution of ESG. Below are the four major drivers:



# BMO's ESG ETFs – Built to align values and mitigate risk

We believe that responsible investment is a mindset: as asset managers, we have a privileged and trusted position as stewards of capital, which gives us both influence and responsibility.

BMO Global Asset Management's commitment to ESG investing runs deep.

We take our responsibility seriously and that includes considering the impact of our investments on society and the environment.

We have developed a range of solutions that includes specialist ESG products, investment strategies with ESG integration and engagement incorporated, and now our ESG ETFs.

Active ownership is the cornerstone of our responsible investment approach. We believe that our responsibility as investors does not end when an investment is made. This is shown in our commitment to active ownership and engagement.

## Responsible Investment at BMO Global Asset Management by the numbers



610  
companies  
engaged



1,300  
number of  
engagement



275  
milestones  
achieved



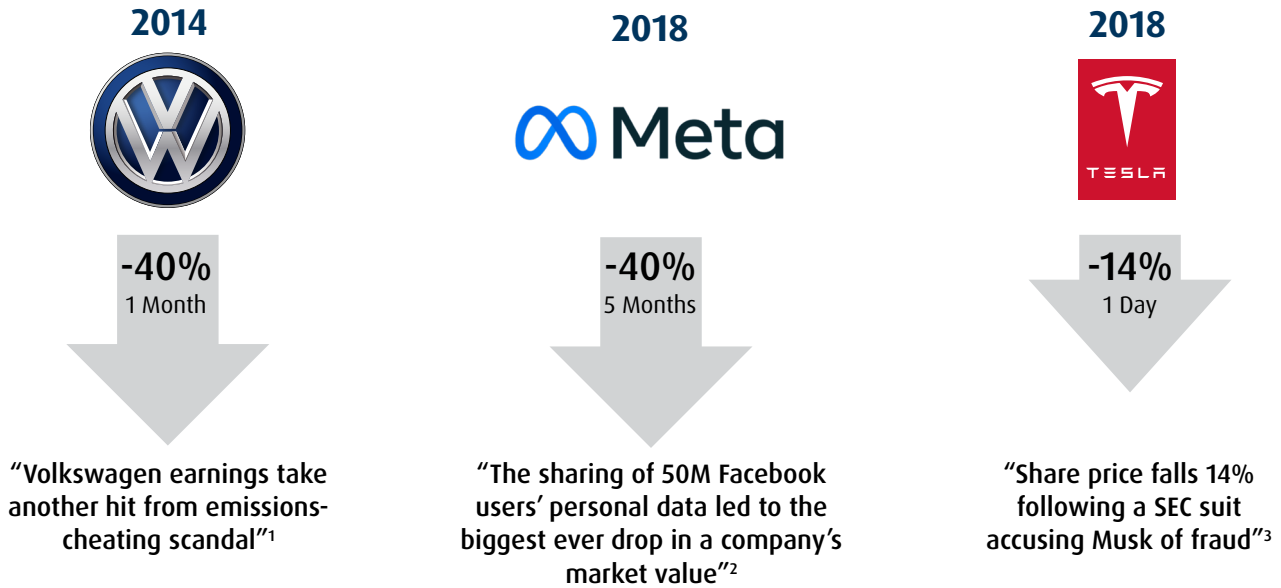
5,260  
company  
meeting voted

Source : BMO Global Asset Management Dec 31 2021

Integration of ESG (Environment, Social, and Governance) factors in the investment process enables a deeper understanding of a company's return and risk profile. A good ESG score implies that management is exerting positive influence, guiding its capital in a responsible manner to meet shareholder and stakeholder interests. ESG integration is a way to uphold an advisor's fiduciary duty and improve a client's risk adjusted returns. Investors are transforming the investment world from the bottom up through their growing interest in ESG investment solutions. With greater scrutiny on companies and emerging ESG risk factors that may impact a company's profitability, there is a greater understanding of the impacts of corporate ESG incidents.

\*PRI Assessment Report 2018

# ESG Incidents Can Negatively Impact Stock Prices



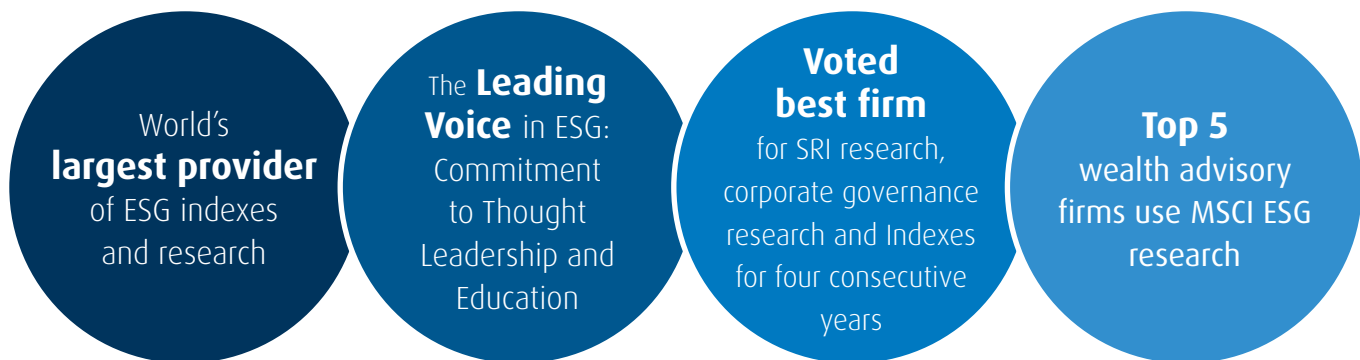
**Sharp declines in stock prices impact performance and fines impact profitability.**

<sup>1</sup>The Wall Street Journal, <sup>2</sup>Financial Times, <sup>3</sup>Bloomberg. All logos and trademarks of other companies are the property of those respective companies.

Investment professionals are recognizing that there is a potential financial benefit to investing in ESG, as evidence shows this data can help make better informed investment decisions and improve risk adjusted returns.

In addition, there have been immense improvements to the data available, allowing innovation in the tools used to measure what was once unmeasurable and to obtain higher quality ESG ratings.

## Why MSCI?



Source: The Extel & SRI Connect Independent Research in Responsible Investment (IRRI) Survey - 2015, 2016, 2017 & 2018/19.

### An in-depth approach that focuses on:

- (1) Identifying most relevant risks by sector
- (2) Recording forward-looking management data
- (3) Incorporating unique alternative data sources beyond company disclosed (or reported) data

## MSCI ESG Ratings by the numbers



37

Key Issues selected annually for each industry



1,600+

Media publications monitored



Data on  
65,000

individual directors



350,000

Securities rated and scored

## MSCI Rating Methodology



Analysis begins with a **deep governance assessment**

Ownership, Board, Pay, Accounting, Corporate Behaviour



Focus on **most relevant ESG factors** by industry

Quantitative Approach + Annual Consultation



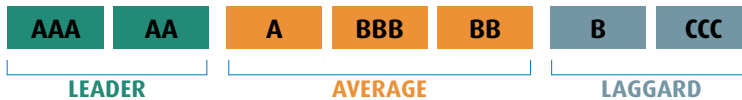
Focus on **risk exposure** not just disclosure

Scoring Models Assess Risk Exposure + Risk Management



Identify **leaders and laggards**, not business type exclusion

Industry-Relative ESG Ratings (AAA-CCC)



Source: MSCI Inc.

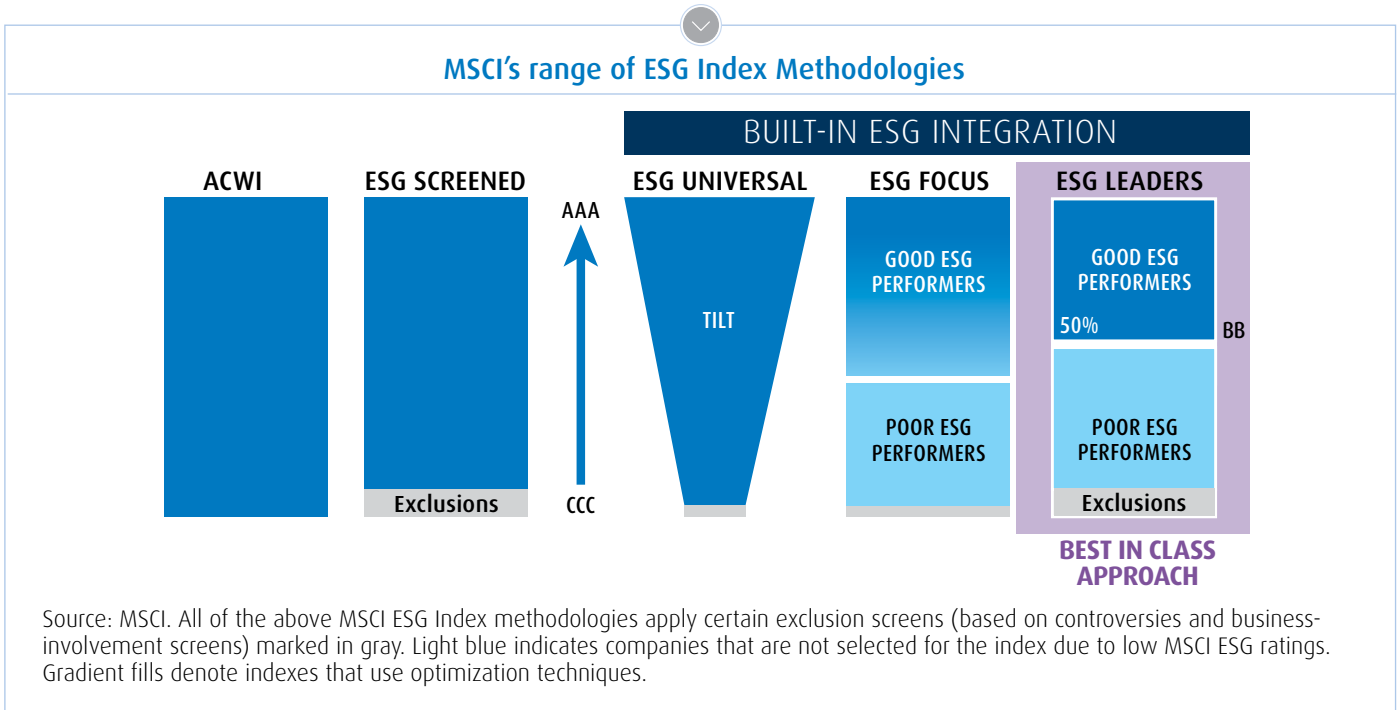
### MSCI's ESG Scoring Framework

MSCI's ESG rating framework monitors and evaluates companies on material environmental, social, and governance issues to generate an overall ESG rating from AAA to CCC. ESG data is gathered from government and NGO datasets, company disclosure documents such as proxy reports and sustainability reports, and public media sources on 37 key ESG issues selected annually for each industry to form an ESG risk assessment. Unlike bond ratings which are across the investable universe, these ratings are determined within sector and industry for a peer to peer approach. Once the Key Issues have been selected for a GICS Sub-Industry, weights are set that determine each Key Issue's contribution to the overall rating. Each Key Issue typically comprises 5-30% of the total ESG Rating. Issue scores and weights are combined to generate the overall ESG rating relative to industry peers.

## MSCI's Controversy Scoring Framework

MSCI ESG Ratings review controversies, which may indicate structural problems with a company's risk management capabilities. MSCI defines a controversy case as an instance or ongoing situation in which company's operations and/or products allegedly have a negative environmental, social, and/or governance impact. A case is typically a single event such as a spill, accident, regulatory action, or a set of closely linked events or allegations such as health and safety fines at the same facility, multiple allegations of anti-competitive behavior related to the same product line, multiple community protests at the same company location, or multiple individual lawsuits alleging the same type of discrimination. Controversies are assigned ratings from "Minor" to "Very Severe", and are formed based on severity of their impact on society or the environment.

### Example



For more information on the thresholds of these exclusions please review MSCI's Methodology:

<https://www.msci.com/esg-indexes>



# BMO's MSCI ESG Leaders ETFs

## Access the highly rated ESG companies relative to their peers

- BMO MSCI Canada Selection Equity Index ETF (**ESGA**)
- BMO MSCI USA Selection Equity Index ETF (**ESGY/ESGY.F**)
- BMO MSCI EAFE Selection Equity Index ETF (**ESGE**)
- BMO MSCI Global Selection Equity Index ETF (**ESGG**)
- BMO MSCI China Selection Equity Index ETF (**ZCH**)
- BMO MSCI India Selection Equity Index ETF (**ZID**)

## Key Features

- Best-in class approach – the indexes select the top 50% ESG rated companies in each sector
- Mitigate short- and long-term ESG risk – Designed to exclude companies involved in severe controversies
- Leverage MSCI's award winning<sup>1</sup> MSCI ESG Research and ESG Ratings to identify companies that have demonstrated an ability to manage their ESG risks and opportunities

## Strategy Implementation

The BMO MSCI ESG Leaders ETFs target companies that have the highest environmental, social and governance (ESG) rating relative to their peers in each sector of the parent index. The indexes use a best-in-class approach by only selecting companies that have the highest MSCI ESG Ratings.

Sector Representation	<ul style="list-style-type: none"> <li>• 50% target sector representation per GICs sector and Sub-Region (to avoid regional and sector biases) relative to parent index</li> </ul>
Minimum ESG Rating	<ul style="list-style-type: none"> <li>• Minimum ESG rating BB</li> </ul>
Minimum Controversy Score	<ul style="list-style-type: none"> <li>• Excludes companies involved in very severe controversies</li> </ul>
Weighting Scheme	<ul style="list-style-type: none"> <li>• Market Cap Weighted</li> <li>• Rebalanced quarterly with ongoing event-related maintenance</li> </ul>
Exclusions	<ul style="list-style-type: none"> <li>• The following activities will use the "Least Restrictive" (as defined in the MSCI ESG Research framework) screen: Alcohol, Gambling, Nuclear Power, Conventional Weapons.</li> <li>• The following activities will use the "Moderately Restrictive" (as defined in the MSCI ESG Research framework) screen: Civilian Firearms, Tobacco.</li> <li>• Nuclear Weapons will use the "Highly Restrictive" (as defined in the MSCI ESG Research framework) screen</li> <li>• Controversial Weapons will use the "Most Restrictive" (as defined in the MSCI ESG Research framework) screen.</li> <li>• Companies involved in the mining of thermal coal, unconventional oil extraction, thermal coal-based power generation are also excluded.</li> </ul>

For more information on the thresholds of these exclusions please review MSCI's Methodology:

<https://www.msci.com/msci-esg-leaders-indexes>

<sup>1</sup> Source: SRI connect and Extel survey – 2015, 2016, 2017, 2018.

# BMO ESG Fixed Income ETFs

## Best in class issuers

- BMO ESG Corporate Bond Index ETF (**ESGB**)
- BMO ESG US Corporate Bond Hedged to CAD Index ETF (**ESGF**)
- BMO ESG High Yield US Corporate Bond Index ETF (**ESGH/ESGH.F**)

## Key Features

- Best-in class approach – the indexes select highly rated issuers
- Mitigate short- and long-term ESG risk - Designed to exclude issuers involved in severe controversies
- Leverages MSCI’s award winning<sup>1</sup> MSCI ESG Research and ESG Ratings to identify issuers that have demonstrated an ability to manage their ESG risks and opportunities

## Strategy Implementation

The BMO ESG Fixed Income ETFs target issuers that have the amend environmental, social and governance (ESG) ratings relative to their peers. BMO ESG Corporate Bond Index ETF invests in investment grade corporate bonds with greater than \$150 million outstanding. BMO ESG US Corporate Bond Hedged to CAD Index ETF invests in U.S. investment grade corporate bonds with greater than \$300 million outstanding. BMO ESG High Yield US Corporate Bond Index invests in U.S. high yield corporate bonds with greater than \$750 million outstanding.

Sector Representation	<ul style="list-style-type: none"> <li>• No sector representation target (40–70% of the parent index typically eligible based on ESG Rating thresholds)</li> </ul>
Minimum ESG Rating	<ul style="list-style-type: none"> <li>• Minimum ESG rating BBB</li> </ul>
Minimum Controversy Score	<ul style="list-style-type: none"> <li>• Excludes companies involved in very severe controversies</li> </ul>
Weighting Scheme	<ul style="list-style-type: none"> <li>• Market value weighted</li> <li>• Rebalanced monthly</li> </ul>
Exclusions	<ul style="list-style-type: none"> <li>• Excludes companies deriving a significant share of their revenues from:               <ul style="list-style-type: none"> <li>– Alcohol</li> <li>– Gambling</li> <li>– Tobacco</li> <li>– Controversial Weapons</li> <li>– Conventional Weapons</li> <li>– Nuclear Weapons</li> <li>– Civilian Firearms</li> <li>– GMOs</li> <li>– Adult Entertainment</li> <li>– Nuclear power</li> </ul> </li> <li>• Companies involved in the mining of thermal coal, unconventional oil extraction, thermal coal-based power generation are also excluded.</li> </ul>

For more detailed methodology information regarding the ESG Fixed Income indices, ESG rating and controversy rating methodology, visit the MSCI ESG indices website: <https://www.msci.com/bloomberg-barclays-msci-esg-fixed-income-indices>

<sup>1</sup> Source: SRI connect and Extel survey – 2015, 2016, 2017.

# Specialty Responsible Investment Solutions

## **BMO Balanced ESG ETF (ZESG)**

- ZESG is a balanced 60/40 asset allocation ETF which offers moderate income and has potential for long-term growth investing in a portfolio of BMO ESG ETFs.
- A low cost, diversified solution that rebalances back to its target exposures

## **BMO Clean Energy Index Fund (ZCLN)**

- ZCLN tracks the S&P Global Clean Energy Index providing exposure to up to 100 companies from around the world that are involved in clean energy related businesses.
- Invests in a diversified mix of the businesses ranging from clean energy producers to clean energy tech and equipment providers
- The ETF excludes controversial businesses and applies a carbon intensity screen to remove the highest emitters

## **BMO Women In Leadership Fund (WOMN)**

- Exposure to North American companies with gender-diverse leadership
- Growing research shows that companies with a higher representation of women in executive leadership tend to outperform in terms of competitiveness and financial performance.<sup>1</sup>

## **BMO Sustainable Global Multi Sector Bond Fund (ZMSB)**

- A sustainable global fixed income solution that can go anywhere to earn income in all credit environments
- A multi-sector bond strategy is designed to invest in multiple fixed income sectors, such as investment grade bonds, high yield bonds, emerging market debt, securitized debt and government bonds.
- Investing in quality companies that follow ESG principles to align investments with values and manage risk

## **BMO Brookfield Global Renewables Infrastructure Fund (GRNI)**

- Actively managed equity strategy that invests in companies that are seeking to capitalize on the multi-decade transition to renewable energy
- Targets global opportunities in key sectors; renewable power & infrastructure, clean technology, and water sustainability, with an emphasis on infrastructure-like attributes to mitigate risk


BMO Clean Energy

<sup>1</sup> McKinsey, Why diversity matters. January 1, 2015

# BMO MSCI ACWI Paris Aligned Climate Equity Index ETF (ZGRN)

Align your investments with a growing mega-trend.

Climate change is the key issue of our time and companies are setting carbon reduction goals, beginning to transition their businesses, and improve their reporting on emissions and targets. Investors understand the threat that climate change can have on a company and are demanding greater transparency around what is being done to confront these issues (2021 Elderman Trust Barometer report). With significant investment needed to confront the threat of climate change, comes investment opportunities and risks that demand our attention.



Manage exposure to physical climate change risk and transition risk



Diversified global equities is aligned to Paris Agreement goals and targets



Benefit from opportunities in the low carbon transition

ZGRN tracks the MSCI ACWI Climate Paris Aligned Index which aligns with a 1.5°C temperature change climate scenario by integrating climate data into the investment process. MSCI's methodology uses state-of-the-art MSCI Climate analytics data with models including forward looking metrics with the goal to:



**Reduce the weight of companies that are high greenhouse gas emitters** based on their complete carbon footprint (scope 1, 2, 3).  
**Reduce exposure to physical risk** arising from extreme weather events by at least 50%.



**Shift from brown to green;** move from fossil fuel related businesses with the goal to double green revenue exposure.



**Shift towards** companies exposed to climate transition opportunities, and underweights those exposed to climate transition risks. Selects and overweights companies with **credible carbon-reduction targets and track records**.

## How to Use ZGRN in Your Portfolio:

- As a core sustainable equity allocation aligned to the low carbon transition
- As an environmental theme exposure
- As a satellite exposure to help reduce climate change risks and access opportunities to low carbon transition.

“We exist to convene,  
catalyze and empower  
change that sustains  
**growth for good.**”

Darryl White  
CEO, BMO Financial Group

## Let's connect

For more information on the topics in this booklet or for additional information on BMO ETFs, please visit our website at [bmoetfs.com](http://bmoetfs.com)

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