SUSTAINABILITY REPORT
Third Quarter 2021
SKAGEN

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IMPORTANT INFORMATION

Except otherwise stated, the source of all information is SKAGEN AS as at 30 September 2021.

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Historical returns are no guarantee for future returns. Future returns will depend, inter alia, on market developments, the fund manager's skills, the fund's risk profile and subscription and management fees. The return may become negative as a result of negative price developments.

SKAGEN AS recommends that anyone wishing to invest in our funds contacts a qualified client adviser. No offer to sell, or solicitation to buy, will be made in any jurisdiction in which such offer or solicitation would be unlawful.

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An uncomfortable duality has been playing out in the market: green need not always be good, and bad might still be necessary – whether we like it or not. Photo: Steven Diaz, Unsplash.com

SFDR and SKAGEN: A focus on process and progress

Sustainability often means different things to different people but there is a clear distinction between sustainable asset management and sustainable investing.

Whereas the former is additive and process driven, the latter centres on what is being invested into and outcomes. Lately, an uncomfortable duality has played out in the market: green need not always be good, and bad might still be necessary – whether we like it or not. This quarter, SKAGEN reached an important milestone by aligning our equity funds with Article 8 of the Sustainable Finance Disclosure Regulation (SFDR). The key hurdle was not the ambition – but communication. How do we highlight our commitment to ESG without diluting our goal of delivering the best possible financial returns to clients?

The 'light green' classification of our funds serves to answer this – they promote social and environmental characteristics but do not have these as their end investment objective. SKAGEN applies binding and routine components that anchor sustainability considerations into investment decision-making; we are about sustainable asset management.

Best suited for active managers

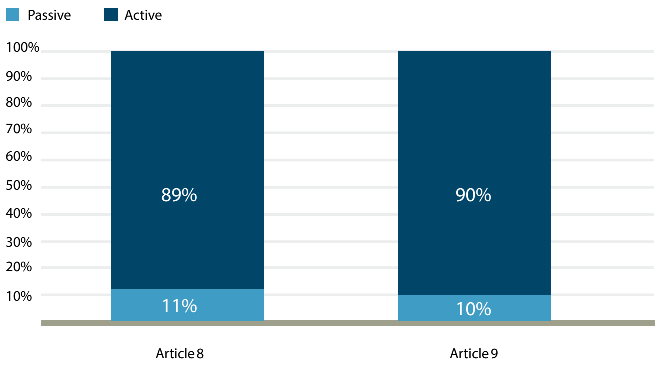
Active fund managers with concentrated portfolios and long investment horizons like SKAGEN are best equipped to scrutinise their portfolio companies and effect positive change. Successfully integrating this ability into the investment process will largely determine our ultimate

[1] Source: Morningstar, SFDR: Four Months After Its Introduction, Article 8 and 9 Funds in Review, July 2021

goal of maximising risk-adjusted returns while also pushing for social and economic progress. Here SFDR also helps by strengthening ESG integration and its disclosure to clients.

For this reason, we were unsurprised when Morningstar's four-month review of SFDR revealed that active strategies dominate both Article 8 and Article 9 products[1].

Exhibit 9 Article 8 and 9 Funds - Active vs. Passive



Source: Morningstar Direct. Data as of 10 July 2021, AUM as of 30 June 2021. Excluding money markets, feeder funds, and fund of funds.

Pragmatic patience is a virtue in its own right

We fundamentally disagree with the notion that investing in virtuous companies guarantees higher returns. Less popular companies have a higher cost of capital and thereby higher expected returns to compensate for additional perceived risk, and vice versa. Just as employing constraints (divestment) cannot enhance absolute returns, aligning portfolios with virtues will not automatically translate into vertiginous financial rewards.

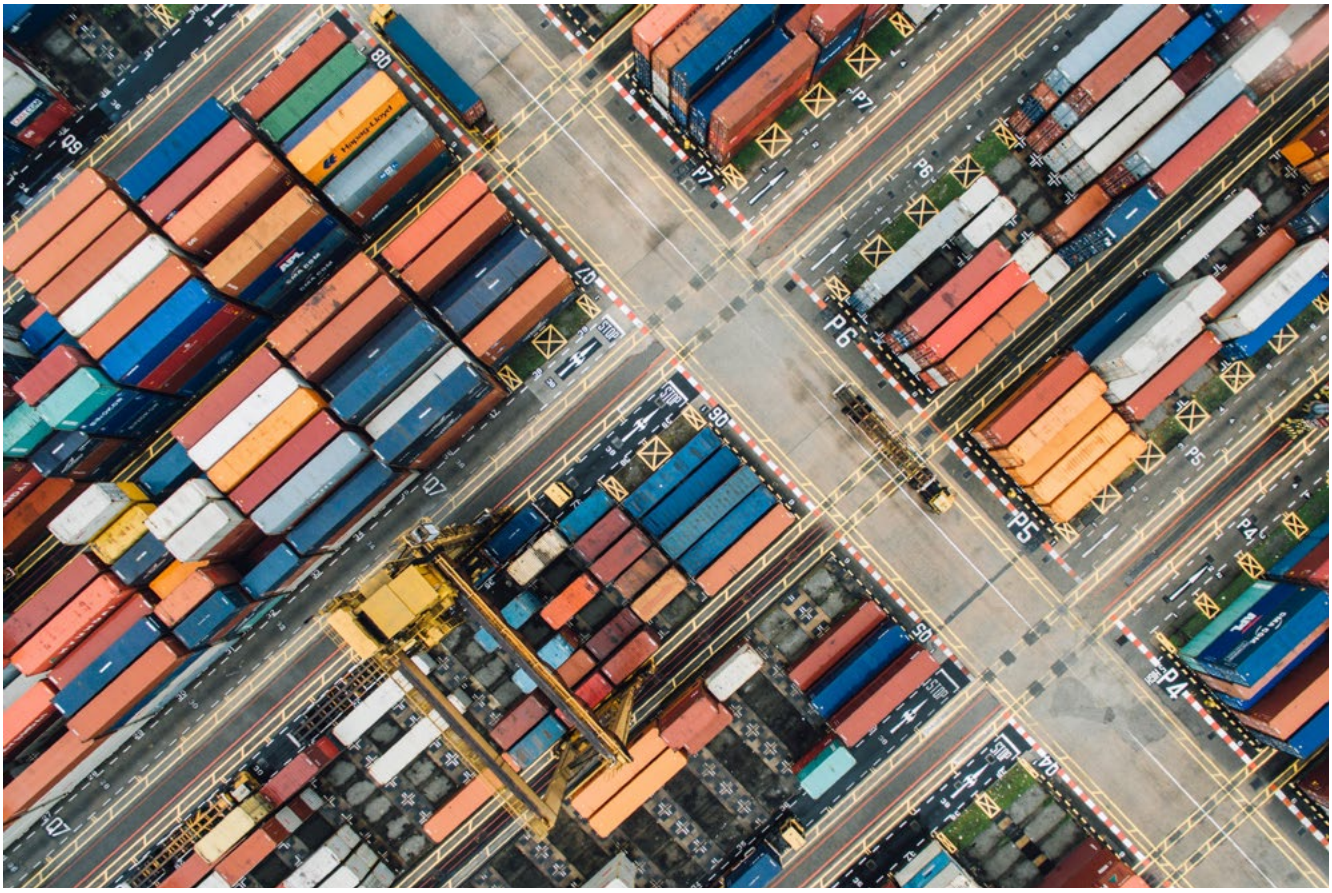
We believe in active fundamental company analysis. Yes, a company that invests in its workforce and respects the local community will inevitably attract better qualified employees than less scrupulous competitors and thereby generate superior long-term returns. Likewise, taking advantage of high commodity and energy prices and investing in mining and oil companies that some consider 'sinful' may be the best way to discharge your fiduciary duty of maximising risk-adjusted returns.

It is a choice; passively avoid "sin" stocks or proactively find the long-term winners regardless of which sector they belong to. Active stock-picking – guided by a firm belief in value – can lead you to invest in companies with ambitious plans to cut emissions and provide consumers with materially greener power, which most accept will still be needed for several years. That we enter the fourth quarter amid a European energy crisis only highlights the frictions of our transition.

A big step in the right direction

In conclusion, SFDR has come at the right time for investors bamboozled by the proliferation of ESG funds, many of which over-state their sustainability credentials. While confusion also surrounds the new regulation, the dust will settle in the coming months. The extraordinary pace at which we are moving presents challenges for all, but SKAGEN will continue to learn and fortify the integration of sustainability into our investment process. There are no short-cuts in ESG or equity investing – patience and hard work are the only way to deliver progress, both for the companies we invest in and our clients' returns.

Alexandra Morris
CIO



In one of the engagement cases this quarter, SKAGEN engaged with Danish transport and logistics company DSV to discuss an agenda item at their upcoming AGM. Photo: CHUTTERSNAP, Unsplash.com

Third quarter engagement report

As long-term investors, we regularly engage with our portfolio companies to promote and encourage improvements.

Engagement activity was lower than usual in the third quarter. This was in part due to the absence of ESG risks and events that required our immediate attention as well as a focus on directing resources towards implementation of the Sustainable Finance Disclosure Regulation (SFDR).

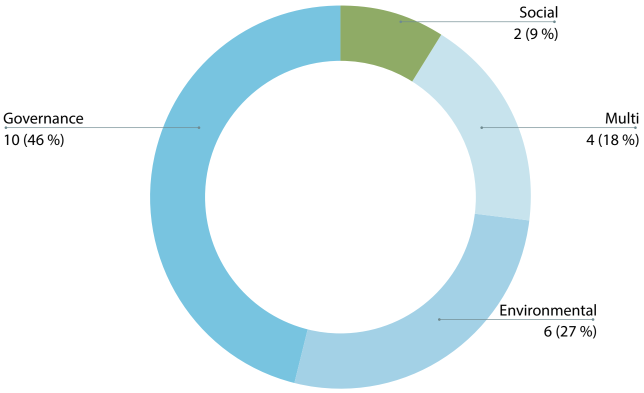
During the quarter, we initiated four new engagement cases and continued our dialogue on an existing case with a Nordic company. Year-to-date, we have 22 ongoing cases with 19 different companies.

A focus on governance

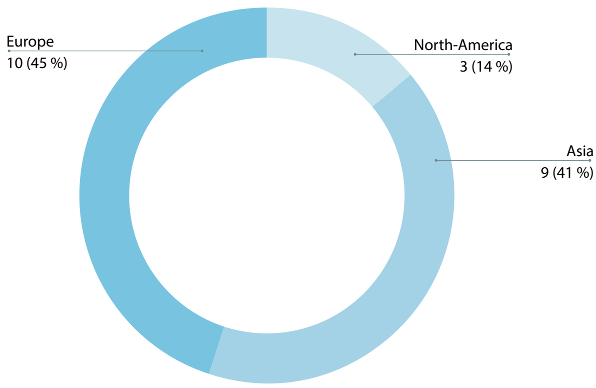
The new engagement cases in the quarter focused largely on governance topics. In one of the cases, SKAGEN's ESG team joined SKAGEN Global on a call with Danish transport and logistics company DSV to discuss an agenda item at their upcoming AGM. DSV was seeking to raise capital by up to 20% without pre-emptive rights, which is an action that SKAGEN typically votes against.

However, the DSV case is a good example of how we take an independent and contextual view of different AGMs rather than blindly relying on third-party recommendations. In this case, we made an exception to the rule and SKAGEN aligned with management on the item in question. We agreed that the action is of strategic importance to the firm's merger and acquisition (M&A) activities, which have fuelled share price growth over recent years. Moreover, DSV will use the share capital directly to pay for M&As, meaning that SKAGEN avoids the risk of the equity landing in the hands of larger shareholders in return for cash. The agenda item was approved by a majority of the votes.

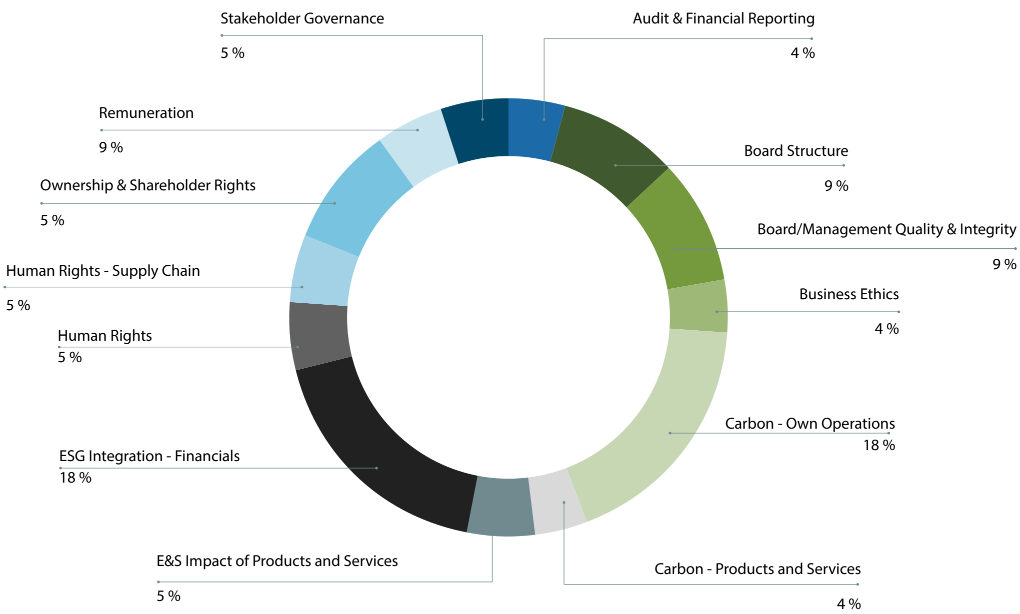
Engagement cases by category YTD



Engagement cases by geography YTD



Engagement cases by topic YTD



Voting activities

Voting is an important tool for investors, allowing us to signal what we believe to be the best course of action for a company and for us as a shareholder. Voting gives us an additional channel through which to address concerns and influence companies in a direction that we believe is sustainable without necessarily being present at meetings.

SKAGEN's funds' voting activities

Voting is an important tool for investors, allowing us to signal what we believe to be the best course of action for a company and for us as a shareholder. Voting gives us an additional channel through which to address concerns and influence companies in a direction that we believe is sustainable without necessarily being present at meetings.

Year	Q3 2021	Q3 2020	Q3 2019
Number of meetings voted	38/39	36/37	26/26
% of meetings voted in	97.44%	97.30%	100%
Number of ballots voted	77/79	74/75	42/42
% of ballots voted on	94.47%	98.67%	100%

Voting activities

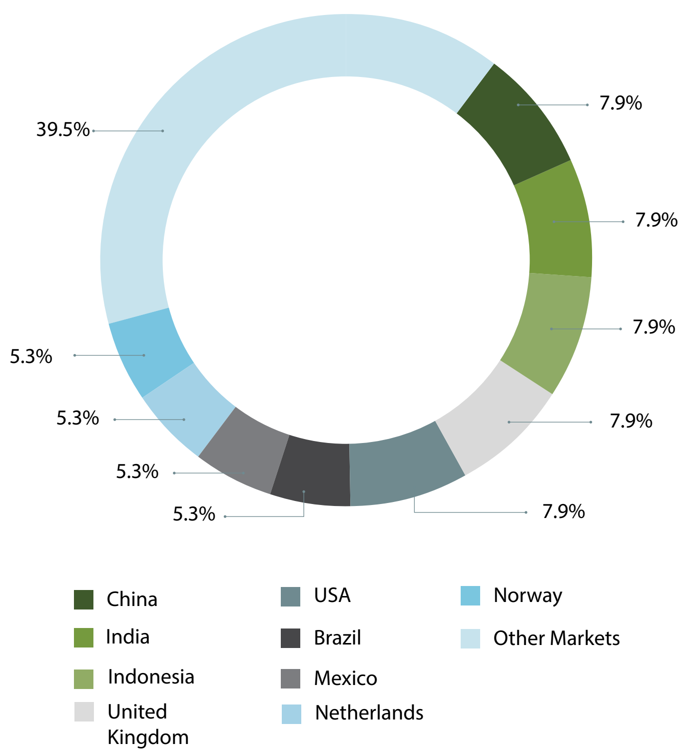
During the third quarter of 2021, there were 39 voteable meetings and 79 voteable ballots at our portfolio companies, with 314 voteable items on the agenda. SKAGEN voted on 99.04% of the items, which is an increase from the third quarter of last year, where we voted on 96.80% of the items.

Votes were in line with management recommendations 88.42% of the time, while 11.58% of the time we voted against management recommendations on one or more items on the agenda. All voting activities can be found in the proxy voting dashboard on our website. All votes are published the day after the votes have been cast, and in the cases where we have voted against management recommendations, an explanation is provided.

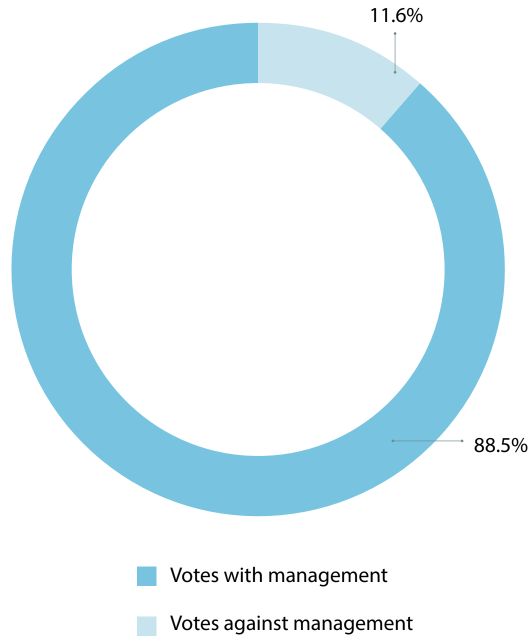
All voting decisions are made by the fund in question, with the objective of securing the best possible risk-adjusted returns for their unit holders.

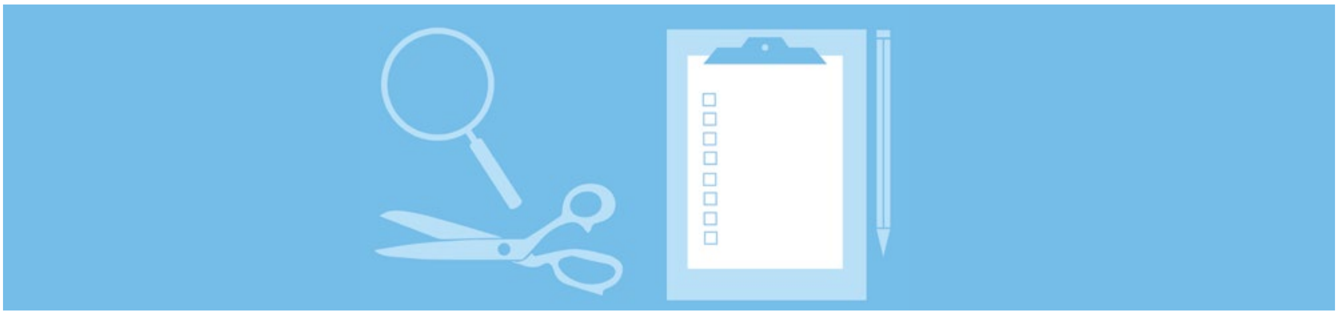
Our full voting record is available here

Meetings voted by market



Votes cast statistics





SKAGEN has reclassified equity funds as Article 8 under SFDR

New categorisation as "environmental and socially promoting" funds to reflect the continued strengthening of SKAGEN's approach to integrating sustainability into its investment process.

The World Day for Cultural Diversity:
SKAGEN's equity funds have been reclassified as Article 8 under the EU Sustainable Finance Disclosure Regulation which applies "where a financial product promotes, among other characteristics, environmental or social characteristics or a combination of those characteristics, provided that the companies in which the investments are made follow good governance practices". They were previously categorised as Article 6 which covers funds that are not promoted as having ESG factors or objectives.

The equity funds are now managed in accordance with Article 8 with the reclassification formally taking place from 1 July 2022 when more detailed Level 2 rules and disclosure requirements of SFDR come into effect.

SFDR: A reminder

The EU Sustainable Finance Disclosure Regulation (SFDR) came into effect in March 2021 and requires fund managers to provide a series of declarations and disclosures concerning the sustainability of the funds they manage. The rules aim to increase transparency over the ESG impact of their investments and are designed to drive sustainable investment and reduce greenwashing by classifying funds as Article 6, 8 or 9.

Read more here >>

ESG integration enhanced
The move to Article 8 reflects the continued strengthening of SKAGEN's approach to integrating sustainability into its investment process. There will be no changes to the current portfolios as a result of the reclassification but in future the funds will formalise and disclose how environmental and social factors are informing stock selection and subsequent decisions throughout the investment process.

We are also enhancing the integration of ESG risk analysis into our investment process, which will now be built on the following four pillars:

1. **Exclusion**: All potential investments are screened and approved against the SKAGEN Sustainable Investment Policy.
2. **Enhanced due diligence for companies in high emitting industries:** Any investment will be subject to an added due diligence process to identify and assess potential climate risk.
3. **ESG factsheet identifying ESG factors:** Produced for each investment case and includes a dedicated ESG overview – including material ESG data, potential engagement plan and KPIs as well as a traffic light assessment of overall ESG profile.
4. **Active Ownership:** Engage and collaborate with holding companies by voicing our views on how to achieve ESG improvements over time.

The result of these changes will be greater rigour in our ESG process and more detailed disclosure on how SKAGEN embeds sustainability in its investment process to achieve the best possible risk-adjusted returns for our clients. Further details about our approach to sustainability can be found here.

Timothy Warrington, CEO of SKAGEN Funds, commented: "With a long track-record of successfully integrating sustainability into our investment process and actively engaging with portfolio companies, SKAGEN is well positioned for the introduction of SFDR in Norway and abroad. Our equity funds are now categorised under Article 8, reflecting SKAGEN's ambition to secure the financial security of clients in a way that leaves the world a better place."

Frequently Asked Questions

1. What is the Sustainable Finance Disclosure Regulation (SFDR)?
SFDR is a new set of EU rules for increased comparability and reduced greenwashing among financial products.

The regulation will increase the information available for investors about both the potential positive and negative impact of their investments and the related ESG risk.

2. What are these Articles?
The SFDR sets out strict criteria for the classification of funds that are defined as sustainable. These criteria are described in the regulation's Articles 6, 8 and 9:

- Article 9 (also known as 'dark green') funds are products that have sustainable investment as their objective.
- Article 8 (also known as 'light green') funds are 'environmentally and socially promoting' products.
- Article 6 covers funds that are neither Article 8 nor 9, however sustainability may still be part of the portfolio manager's process.

3. How will I as a client notice the change from Article 6 to Article 8?
The strategy and objective of our equity funds remain the same as before.

What you might notice in the wake of this change is an increase in client communication and reporting. Transparency and honesty have always been integral to SKAGEN and we will continue seeking to ensure that you have all the information you need to understand how we systematically work with sustainability and responsibility principles through the investment process of our equity products so that you can use this information to make an informed decision about the fund you would like to invest in.

4. What does it mean for the investment process/management of my funds?
It means that clients can be confident that the sustainability and responsibility factors of an investment are rigorously assessed and acted upon through several steps in our investment process.

This includes the initial screening of a new investment idea, analysing specific ESG factors and their potential financial risks and opportunities, exercising ESG engagement and active ownership once invested, and ultimately holding companies accountable to our ESG Policy and principles.

5. What is SKAGEN doing, in practice, to improve its ESG work?
It is important to note that improving our ESG work will always be a continuous learning process but in the wake of these changes, we are introducing some key initiatives.

The first is to bring onboard additional resources to meet regulatory expectations and requirements as well as bolster the analytical insight throughout the investment process.

We have also expanded and revised our ESG integration framework meaning that ESG will be an area of even closer collaboration and focus across the investment team. This will provide our portfolio managers with even more information to make the best possible investment decisions on behalf of you as a client.

6. Will the article change improve returns in SKAGEN's funds?
SKAGEN's objective will always be to maximise risk-adjusted returns for our clients. Sustainability is an important part of this, both to reduce potential risks to our investments caused by ESG factors and using them positively to identify opportunities to improve fund returns.

Whilst the ESG risk of a company provides an assessment of current ESG risk, it does not necessarily capture future momentum and positive potential. Photo: Karsten Würth, Mölsheim, Germany, Unsplash.com

ESG Risk Rating: Assessing the full picture

To understand companies' exposure to material ESG issues and how they may impact shareholder value, SKAGEN uses the ESG risk ratings compiled by the research and rating firm Sustainalytics. These ratings are expressed as absolute scores between 0 and 100, with 100 indicating the highest level of ESG-driven financial risk. These scores fall into five levels of risk: negligible (0-10), low (10-20), medium (20-30), high (30-40) and severe (40-100). The ESG risk rating is made up of two components: the general ESG risk exposure that a company has (ESG exposure), and how well that risk exposure is managed (ESG management).

A company may have high exposure to ESG risk by virtue of the industry it operates in (e.g. oil & gas) but also have good practices to manage those risks, thereby bringing down the overall ESG risk.

SKAGEN's ESG integration framework is built on four pillars:

1. **Exclusion:** All investments are screened and approved against our Sustainable Investment Policy.
2. **Enhanced due diligence for companies in high emitting industries:** In order to identify and assess potential climate risk.
3. **ESG factsheet identifying ESG factors:** Produced for each investment case and includes a dedicated ESG overview.
4. **Active Ownership:** Engage and collaborate with companies by voicing our views on how to achieve ESG improvements over time.

Large caps provide more disclosure

The ESG management score tends to favour larger and/or older companies, as smaller and/or newer ones rarely have the resources or capability to provide solid management programs and policies. Younger companies also tend to have less experience in conducting materiality consultations and integrating ESG factors into their corporate strategy. We therefore often see that these companies receive a low ESG management score, despite being involved in few controversies. As some of our funds tend to invest a significant proportion of their portfolios in small cap companies, this should be kept in mind when considering the score.

Future potential

Whilst the ESG risk of a company provides an assessment of current ESG risk, it does not necessarily capture future momentum and potential. Returning to the oil & gas industry as an example, a snapshot assessment of the exposure companies in the industry face might not capture the renewable energy efforts that are being developed and the gradual pace of sustainable transitioning. Active ownership and our engagement with companies can help us identify such dimensions.

Importantly, there are no objectives or expectations for the funds to have a specific ESG risk at portfolio level or to be better than the benchmark. ESG integration in the investment processes is used to prioritise and execute active ownership as a tool to influence the risk and reward profile of an investment. ESG data provides crucial input in our investment processes and serves as guiderails for investment decisions. It thus informs our sole purpose: to provide the best possible risk-adjusted return to our clients.

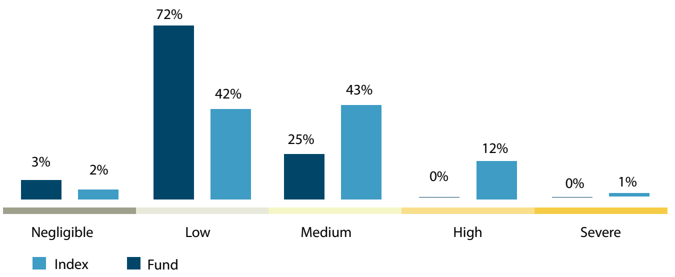
ESG RISK RATING

All risk ratings on this page are powered by Sustainalytics.

SKAGEN Global

	SKAGEN Global	MSCI ACWI
Coverage rate:	100%	100%
ESG Risk Rating:	17.1 (Low)	21.9 (Medium)
ESG Exposure:	34.2 (Low)	40.3 (Medium)
ESG Management:	54.1 (Strong)	48.8 (Average)

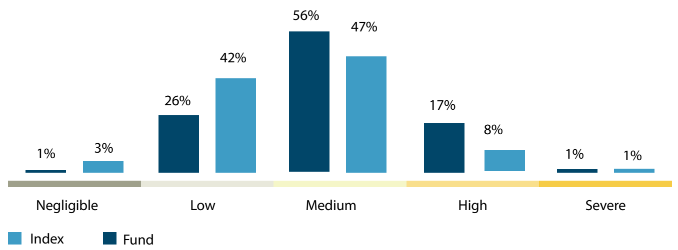
ESG Risk Category by aggregate portolio weight %



SKAGEN Vekst

	SKAGEN Vekst	MSCI Nordic/ ACWI ex Nordic
Coverage rate:	97%	99%
ESG Risk Rating:	24.3 (Medium)	21.2 (Medium)
ESG Exposure:	45.5 (Medium)	40.1 (Medium)
ESG Management:	49.3 (Average)	50.1 (Strong)

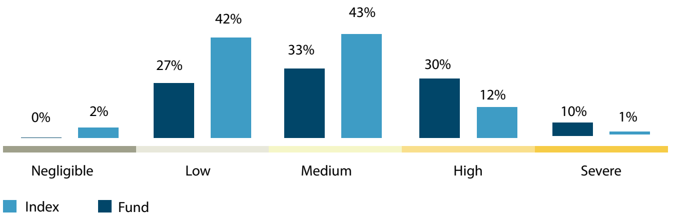
ESG Risk Category by aggregate portolio weight %



SKAGEN Focus

	SKAGEN Focus	MSCI ACWI
Coverage rate:	91%	100%
ESG Risk Rating:	28.5 (Medium)	21.9 (Medium)
ESG Exposure:	44.7 (Medium)	40.3 (Medium)
ESG Management:	38.5 (Average)	48.8 (Average)

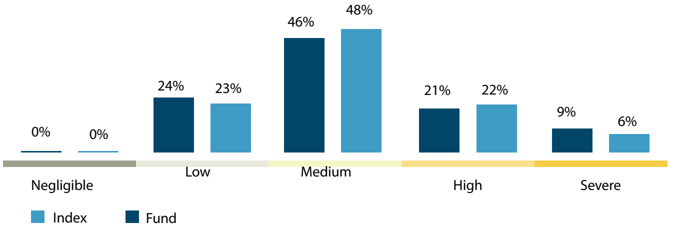
ESG Risk Category by aggregate portolio weight %



SKAGEN Kon-Tiki

	SKAGEN Kon-Tiki	MSCI EMI
Coverage rate:	90%	99%
ESG Risk Rating:	26.7 (Medium)	26.3 (Medium)
ESG Exposure:	44.1 (Medium)	42.1 (Medium)
ESG Management:	42.1 (Average)	40.8 (Average)

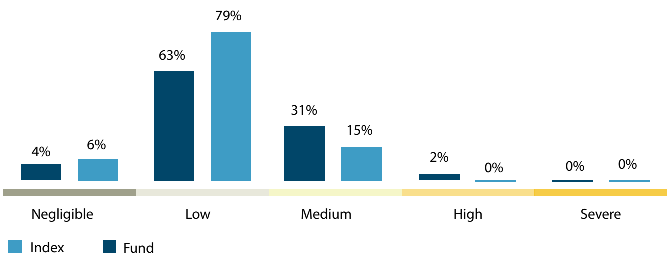
ESG Risk Category by aggregate portolio weight %



SKAGEN m2

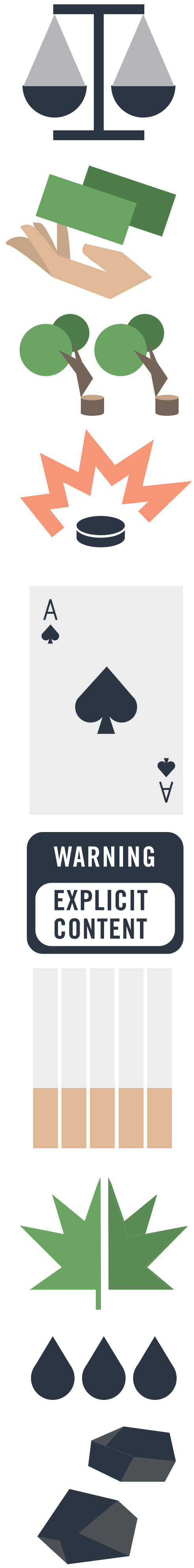
	SKAGEN m2	MSCI Real Estate
Coverage rate:	94%	99%%
ESG Risk Rating:	16.9 (Low)	15.0 (Low)
ESG Exposure:	28.8 (Low)	26.2 (Low)
ESG Management:	43.0 (Average)	43.7 (Average)

ESG Risk Category by aggregate portolio weight %



Exclusion as a last resort

As an active and value based investment manager, SKAGEN has a distinct investment philosophy and process that builds on common sense and a belief that companies which understand and incorporate sustainability in their business strategy will outperform their peers over the longer term. SKAGEN excludes the following activities from our funds:



Corporate behaviour:

- Systematic breach of international laws and norms and human rights
- Systematic corruption and financial crime
- Serious environmental degradation (deforestation)
- Companies that produce or sell controversial weapons (nuclear, land-mines, cluster munitions, etc.)

Products/activities:

- Owners of palm oil plantations with unsustainable business practices
- Companies that deliberately and systematically work against the goals and targets enshrined in the Paris Agreement
- Gambling (more than 5% of revenue)
- Adult Entertainment (more than 5% of revenue)
- Tobacco (more than 5% of revenue)
- Recreational cannabis – THC (more than 5% of revenue)
- Coal (5% of revenue)
- Oil Sand (5% of revenue)

Exclusion is to be used as a last resort, and should only be applied when companies clearly fail to demonstrate change or improvements. If an excluded company demonstrates positive change that reduces the risk of recurrence, the company may be re-included.

Read more in our Sustainability policy

Exclusion list as of 30.09.2021 Exlusion category	No. of companies
Conduct-based exclusion - Environment	18
Conduct-based exclusion - Corruption	10
Conduct-based exclusion - Human Rights and International Law	37
Tobacco	23
Controversial weapons	23
Climate - Coal	131
Climate - Lobbying	5
Climate - Oilsand	9
Unsustainable Palmoil	11
Gambling	43
Cannabis	1
Total number of companies	311*

* Some companies are excluded on the basis of several criteria. We do not invest in companies that have been excluded by Norges Bank from the Government Pension Fund – Global.

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Front page:
Viggo Johansen, Dividing the catch, 1885. This painting is manipulated and belongs to The Art Museums of Skagen.

The art of common sense

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