ESG Risk Integration at Osmosis IM NL – June 2025

At Osmosis Investment Management NL (Osmosis IM NL), the integration of Environmental, Social, and Governance (ESG) risks is foundational to the firm's investment process across all managed assets, including Alternative Investment Funds (AIFs) and discretionary portfolio management. This integration is formalised in the Investment Due Diligence & ESG Policy, aligned with the Sustainable Finance Disclosure Regulation (SFDR), the Alternative Investment Fund Managers Directive (AIFMD), and other applicable European Union regulatory frameworks.

Sustainability Philosophy and Transition Thinking

Osmosis IM NL has adopted a distinct approach to sustainable investing known as "Transition Thinking." This method emphasises dynamic progress over static ESG scoring by focusing on a company's trajectory toward a sustainable economic model. Transition Thinking evaluates investee companies across three interrelated dimensions: Nature (environmental footprint and biodiversity), Economy (resource efficiency and innovation), and Society (equity and social well-being). Combined, these Transition Dimensions encompass several specific pathways a company can be evaluated against.

Osmosis IM NL strongly believes sustainable investing drives performance (alpha). Negative externalities like pollution or inevitable policy responses should be part of credit research and hence financial modelling. It makes the investment professional better prepared, leading to better decision making.

The firm's proprietary "Transition Beta" framework quantifies the speed and quality of a company's transition. Unlike conventional ESG scores, the Transition Beta is forward-looking and integrates financial modeling directly into credit analysis. It consists of three steps. A key belief is that actual fundamental research and understanding the credit drivers make the difference in terms of performance rather than exclusions. Transition research drives returns, while stand-alone ESG data or exclusions do not.

First there is the assessment of the current impact a company and its products have. It is about 'what' and also 'how' the company produces (e.g. considering resource efficiency and potential controversies). This step delivers a proprietary and independent investment framework like the SDG Framework or the Resource Efficiency framework. The second step is much more forward looking and looks into the green or sustainable revenues of the future. It is about green capital expenditures, green patents or the revenue trend in green products. It also evaluates the adaptability of the company to inevitable policy responses like carbon taxes or regulation / legislation. Finally, the third step is about the financial health of the company. It is important to evaluate whether a good return can be made given that is a prerequisite for clients. As such, the financial health of a company transitioning into the future may differ. Sometimes green capital expenditures translates into more cost as opposed to yielding an actual return.

These three steps comprise the Transition Beta. The higher the Transition Beta, the more an investee company contributes to the Transition towards a sustainable economy. It is a measure of change and sustainable profitability, rather than a backward looking data series. It supports performance achievements while not limiting the investment universe too much.

Governance and Decision-Making Structure

ESG integration is governed by a robust structure involving the Management Board, Investment Committee, and Sustainable Investing Committee. The Management Board holds ultimate responsibility for the philosophy and implementation. The Investment Committee, chaired by the CIO, includes key heads of research, credit, and client relationships. It meets on a monthly basis to review frameworks and evaluate legal, commercial or academic feedback. It assesses sustainable investing model updates on a quarterly basis.

The Sustainable Investing Committee meets monthly and focuses on content, data, and innovation. Analysts, data scientists, and sustainability experts collaborate to ensure models are academically grounded, relevant, and up to date.

ESG Integration in Public and Private Credit

The bottom-up credit research framework is applied consistently across public and private strategies. Analysts score companies along five standardised pillars: Business, Strategy, Sustainability, Structure, and Financials. Analysts are empowered to assign C-scores (assessing credit fundamentals) in credit committees. These scores range from -3 to +3 and represent the expected fundamental credit quality over the next 12 months given the rating and across sectors. It incorporates ESG and Transition Beta findings. Portfolio managers then determine trade implementation. These reports include backward-looking ESG data (such as Scope 1-3 emissions), as well as forward-looking modeling of transition-related costs.

Private credit strategies involve more direct engagement, including borrower interviews and questionnaires. When data is scarce, analysts use estimation techniques such as linking revenue lines to SDGs or applying location-based emissions data. Despite these differences, both public and private portfolios use the same assessment logic and Transition Beta methodology.

Technology and Automation

Osmosis IM NL makes extensive use of technology to scale research production. The research process is supported by AI, large language models (LLMs), and automation. Around 60% of a credit research report is generated through semi-automated workflows, with quality controls performed by senior analysts and cluster heads. The process starts with fundamental analysts and portfolio managers defining the credit drivers. These are defined along a limited amount of 1800 economic activities a company can be involved in (Bloomberg BICS data). Every revenue line relates to a specific and generic series of questions around the credit drivers. Hence, any company, public or private, can be dissected into revenue lines and credit drivers. The second step is about large language models and proprietary tooling searching for answers in the documents made available to the model called Sequoia (named after the slow but ever growing tree) which contains an ever growing and continuously developing (ever smarter) model. Sequoia can research endless amounts of input like annual reports, broker reports, filings, agency reports or expert networks as well as the world wide web. The third step is about the output of Sequoia, finishing the report by the fundamental analysts and portfolio managers. Hence, the opinionating part of the report and the finishing and approving of the output is just like the starting point (defining credit drivers), done by fundamental investment professionals.

Our Sequoia model drives up research productivity, speed of execution and hence basically removes research coverage limitations. Second opinions for clients, quick new issue assessments or just much better and creative research is the result. This means better and cost efficient service to the clients.

Bloomberg's AIM and PORT and OMS systems, combined in the Buy Side Solutions platform provide an integrated platform for data sourcing, risk management, and compliance monitoring. All steps of the asset management process are based on one security master. There are no interfaces needed between different databases or software solutions. It is a turn key, integrated front and middle office system which drives down errors and omissions. It lowers the total cost of ownership for IT of the company. Also, given that Osmosis IM NL has all activities in Bloomberg or on Microsoft Azure (Sequoia), cyber security of all processes is ultimately stronger.

Regulatory Compliance and SFDR Classification

All Osmosis IM NL investment strategies qualify under SFDR as Article 8 products, meaning they promote environmental and/or social characteristics. To maintain this classification, Osmosis applies at least three binding ESG elements across all strategies:

- Mandatory exclusions (e.g., tobacco, controversial weapons, fossil fuels with no transition plans).
- A minimum allocation (≥5%) to Green, Social, or Sustainability-Linked Bonds.
- Portfolio limits on low-scoring companies within the proprietary SDG framework.

These rules are encoded in pre-trade compliance systems and monitored through Bloomberg AIM, ensuring real-time risk oversight and adherence to regulatory requirements as well as fund prospectuses and investment management agreements.

Exclusions and Governance

The exclusion policy applies across both corporate and sovereign issuers. Corporate exclusions are based on sanction lists, international norms (ILO, UNGC, OECD), and proprietary ESG frameworks. Sovereign exclusions are based on political stability indices and violations of governance or human rights.

Decisions on exclusions are made by the Sustainable Investing Committee and communicated to the Investment Committee and Management Board. These decisions are executed within one month, assuming normal market conditions.

Principal Adverse Impacts (PAIs)

Although supportive of the PAI regime's goals, Osmosis IM NL has opted not to consider PAIs at the entity level due to practical limitations and organisational scale in accordance with article 4 paragraph 1(b) of SFDR. Instead, the firm integrates sustainability impacts through its Transition Beta, which implicitly addresses many PAI indicators in a more forward-looking and financially material way. This decision is reconsidered annually.

Conclusion

At Osmosis IM NL, ESG is not an auxiliary process - it is embedded throughout the investment lifecycle. By combining strong governance, deep research, automation, and a proprietary sustainability philosophy, Osmosis IM NL delivers portfolios that aim to maximise financial return while accelerating the global transition toward a sustainable economy. The result is a differentiated, forward-looking approach to ESG integration, aligned with regulatory expectations and client demands.