RESPONSIBLE INVESTMENT QUARTERLY

QUARTER 3, 2023

QUILTER CHEVIOT
INVESTMENT MANAGEMENT

Approver: Quilter Cheviot Limited, 16 October 2023

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WELCOME

Following the busy AGM season, the summer has been an opportunity to focus on our stewardship priorities for the next few months. Data gathering is an important element of any stewardship activity and the team has been particularly focused on the climate commitments of the companies and funds that we invest in. This is an ongoing and evolving engagement and is critical in determining how we think about climate transition within our investments. Alongside this Greg and Margaret are leading engagements with two companies as part of the IIGCC (The Institutional Investors Group on Climate Change) Net Zero Engagement Initiative. For our human rights theme, Greg and Kirsty are key members of the 30% Club 'fix the exec' working group and will be leading engagements with four companies.

We published the first part of our long-term **thematic engagement with investment trusts** in early September. The response has been extremely positive from the wider investment industry and we will be following this with our findings on private equity, infrastructure, property and other alternatives investment trusts.

Adelaide Claydon joined us in August for eleven weeks as part of Quilter Cheviot's intern programme; Adelaide will be talking about her experience in an upcoming RI Reels.

Finally as part of Quilter we retained our signatory status to the UK Stewardship Code in 2023. In order to be a signatory, we submit a report that outlines our stewardship activity on behalf of our customers. Stewardship includes engagement with the companies and funds we invest in, using our voting rights and the consideration of environmental, social and governance factors within investment decision making.

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VOTING ACTIVITY

Over the third quarter we voted at:

82 COMPANY MEETINGS

Over the quarter we voted on:

1,300 RESOLUTIONS

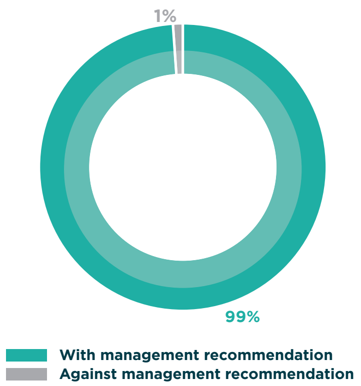
for 14 resolutions we did not support management (this includes shareholder proposals).

We enabled clients to instruct votes at 15 meetings

It is important to note that on a number of occasions having engaged with the relevant company we did not follow ISS' recommendations.

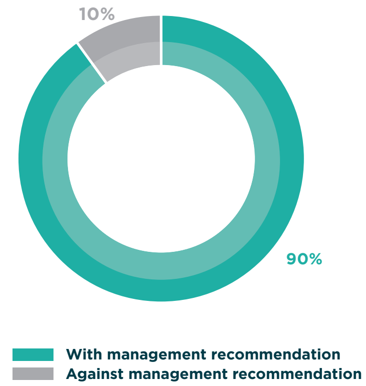
MANAGEMENT RESOLUTIONS VOTED IN Q3 2023

(excluding shareholder proposals)



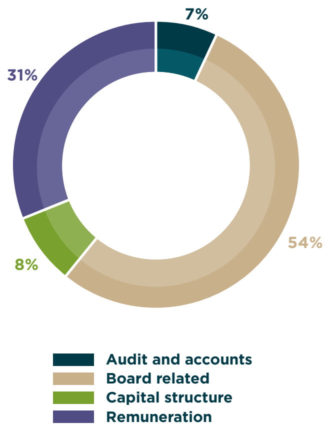
MEETINGS WITH VOTES AGAINST MANAGEMENT IN Q3 2023

(including shareholder proposals)

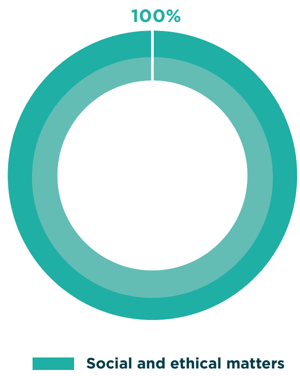


MANAGEMENT RESOLUTIONS VOTED AGAINST BY TOPIC IN Q3 2023

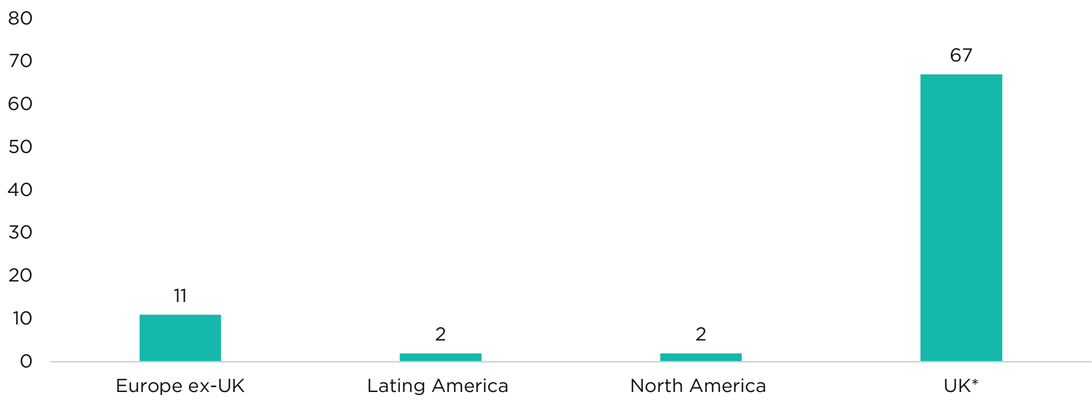
(excluding shareholder proposals)



SHAREHOLDER PROPOSALS SUPPORTED IN Q3 2023



MEETINGS VOTED IN EACH GEOGRAPHY IN Q3 2023



** Includes the Crown Dependencies of Jersey and Guernsey*

Q3 2023 VOTING

We have summarised the key voting issues of the period.

Key voting activity:

Voting activity slowed down across Q3 in comparison to the peak AGM season (March-June), with fewer meetings held and fewer shareholder resolutions filed. This was evidenced by only one environmental related item filed across the quarter in comparison to 56 in Q2. Across Q2 we saw the majority of companies across Europe and North America hold their annual meetings, where shareholder appetite to file environmental and social proposals remained high.

Considering this change of pace, the focus across the period turned to traditional governance related items, namely compensation and director elections. Following the updated EU listing rules regarding board diversity, we are paying close attention to companies regressing on progress made or showing a lack of commitment in meeting the soon to be updated targets. This quarter, we voted against the election of a director at LondonMetric Property due to board gender diversity concerns. Board composition is a topic we have engaged the company on previously and progress made in this area had fallen back prior to its 2023 AGM. In this instance, we voted against the incoming chair of the nomination committee.

Building on Q2, shareholder demands for enhanced transparency on remuneration practices and policies are increasing. Across the quarter, we voted against remuneration reports where in-flight adjustments had been made to incentive awards and where bonus opportunities were increased without a robust rationale provided by the company. In the absence of adequate disclosure on executive compensation, we utilised our voting rights to register our disapproval and encourage improved disclosure.

Environmental voting activity by numbers

1x vote in favour of supporting management in approving climate-related plans (management item)

We supported Scottish and Southern Energy's (SSE) Net Zero Transition Report. With medium and long-term targets covering both intensity and absolute GHG emissions, the report is in line with industry peers.

Company voted on: SSE

Social voting activity by numbers

1x vote in favour of gender pay gap reporting (shareholder proposal)

We supported this proposal as shareholders would benefit from knowing the median pay gap statistics to improve transparency on this issue.

Company voted on: Nike

Governance voting activity by numbers

7*x votes against electing / re-electing director (management items)

We have voted against the election of directors for a number of reasons, including: independence concerns, time commitment issues and a multi-class share structure with unequal voting rights.

Companies voted on: HarbourVest Global Private Equity, Jet 2, LondonMetric Property, MIGO Opportunities Trust, NIKE, Ryanair Holdings (x2)

5x votes against management on compensation related resolutions (management items)

We have voted against remuneration reports and policies where there are not robust long-term incentive performance metrics and vesting periods in place. Additionally, we placed votes against resolutions where fixed performance targets were lacking and special bonuses were awarded during the year, raising concerns about excessive pay- outs.

Companies voted on: GB Group, Jet 2, LondonMetric Property, Prosus, Ryanair

1x vote against management on authorising share repurchase (management item)

We voted against the repurchase of shares, in this instance, as the proposed amount does not fall within the recommended limit.

Company voted on: Prosus

** Withheld and abstention votes have been included within votes against figures.*

ENGAGEMENT ACTIVITY

Here, we outline examples of our engagement in the three months to the end of September 2023. In line with the Shareholder Rights Directive II (SRD II) disclosure regulations, we have included the name of the company or fund in the majority of cases. In some cases, we will not, as this would be unhelpful in the long-term to the ongoing engagement process.

We use ISS as our proxy voting service provider and based on our responsible investment principles, ISS provides recommendations on each resolution companies put forward to shareholders. We do not follow the ISS recommendations, as we believe it is important that responsible investment is integrated into our investment process, and that Quilter Cheviot makes up its own mind.

ABRDN Private Equity – Governance

Objective: We initiated an engagement with the company to discuss the board recruitment and evaluation process. Additionally, we wanted to gain insight into the company's responsible investment disclosures and encourage development in this area. This engagement was part of the overall investment trust thematic engagement and the first-time meeting ABRDN Private Equity Opportunities' (APEO) board.

The board is looking for one, and potentially two additional directors to join the board. The chair will reach his nine-year tenure by the next AGM, but it is likely that he will serve ten years while the search for his successor continues. The ESG integration process is explained in the annual report, but we advised that adding specific examples of engagement would enhance the disclosures. The chair recognised that this is an area where there is room for improvement and assured us that the board will address this with the manager.

The board conducted an external board evaluation three years ago. Due to the changes with the manager, the board has decided to postpone the next board review until next year. Lintstock was retained for the last evaluation and will also conduct the next.

Historically, the marketing and public relations (PR) have been conducted internally by ABRDN. However, on appointment as chair, he took the decision to appoint two external PR agencies. Additionally, the chair admitted that the website would benefit from enhancements to become more engaging and accessible.

Outcome: Overall, the board has strong private equity experience and meets required diversity targets but has room for improvement in responsible investment disclosures and marketing, including the website. The board is working through a succession plan for the chair and, while the details have not yet been announced, it is expected that he will serve ten years which we will support on this occasion.

Asia Dragon Investment Trust – Governance

Objective: To discuss the proposed merger with the ABRDN New Dawn Trust and the implications for shareholders.

We met with the chair to discuss the proposed merger, which we believe is beneficial. It appears logical to increase the size of the trust, thus conceivably better liquidity, and lower fees. ABRDN has agreed to bear the costs of the transfer, which we also believe is a good precedent for other boards when discussing potential mergers.

The New Dawn shareholders will have a tender opportunity as part of the merger, and we expect for this to be taken up in full (25% of the trust). Asia Dragon shareholders must wait until 2026 for a potential liquidity event which will be smaller in quantum. The chair acknowledged that it is a difficult balance, and that scale is important. As there is already a tender offer in prospect for Asia Dragon, the board could not see the benefit of an offer now, whereas for New Dawn there was no forthcoming tender. One of the benefits of the merger is to increase in size and enter the UK250. Undertaking a tender offer for Asia Dawn would mean that the overall size of the new combined trust would not really increase. The chair explained that the merger is accretive to net asset value (NAV) owing to the New Dawn tender at NAV less 2%. It was important that the transaction was accretive and not costing shareholders. We agree that the long-term embedded discount in both trusts has been an issue.

We suggested the board should look at the conditions of the tender in 2026. In our view the performance is materially disappointing and that the board should give shareholders the right to exit and increase the 15% tender level.

Regarding board composition, we explained that we would expect the new board to be free of any manager representation. The chair understood our position; however, the board composition is not yet public and therefore he was unable to comment further. The board will go through a period of transition, increasing to eight non-executive directors (NEDs) and then reducing back for to five, after a six-month period. When we raised FCA expectations, the chair confirmed that the new board will be compliant with diversity expectations. As part of this process, he undertook a skills matrix exercise for all the NEDs and then projected forward on the skillsets and succession planning as it is important to look to the future.

Outcome: Overall, a reassuring meeting, however we will monitor the composition of the board in terms of manager representation and escalate our concerns as required.

Assura – Environment Governance

Objective: The focus of the discussion was on existing sustainability-related disclosures, alongside our expectations for the future.

Assura is reviewing its social impact, and sustainability strategy and targets and is collaborating with a specialist consultant. As part of this, Assura is engaging with stakeholders. Assura has made considerable progress in sustainability-related disclosures and is working towards a net zero plan that will be validated by the Science-Based Target initiative (SBTi). Additionally, it is focused on its first assessment by GRESB (the global real estate ESG benchmark) and on improving on its CDP score from 2022.

We also discussed executive ESG-related targets and we highlighted that we prefer those that are tangible and can be measured by investors. For example, environmental performance certificates (EPC) metrics are a clear target. We also addressed executive remuneration, stating our preference that the bulk of the variable remuneration is paid out as shares to strengthen shareholder alignment.

Outcome: We welcome the company's proactivity in reaching out to shareholders for feedback. Assura's responsible investment disclosures have room to improve. However, the direction of travel is positive, and we will monitor progress.

FRP Advisory Group Plc - Governance

Objective: To raise concerns regarding the Chief Financial Officer's (CFO's) long-term incentive plan (LTIP).

The CFO's long-term variable pay is structured as follows: 80% of this award is subject to performance conditions including earnings-per-share (EPS) growth and absolute total shareholder return. Only 20% is subject to continuing employment (i.e., no performance conditions being applied). We engaged with the chair of the remuneration committee to understand the rationale for this structure, and to outline expectations to see better alignment with best practice moving forwards. During our call, the committee chair clarified that the LTIP structure was a historic arrangement between the partners and CFO, confirming ambitions to extend performance metrics to all aspects of the LTIP, starting next year.

Outcome: This should be the final year of the current structure. We believe that conditional support is appropriate this year, with the expectation that the structure will be changed in 2024.

HG Capital Trust (HGT) - Governance

Objective: Through this engagement, we wanted to develop our understanding on the trust's succession planning and executive search, alongside gaining further insight into the firm's oversight of responsible investment. This engagement was part of the private equity investment trust thematic engagement and the first-time meeting HG capital trust's (HGT) board.

HGT takes majority stakes in private companies, mainly in the software sector. These controlling stakes allow it to influence the underlying companies and apply its responsible investment policies. The trust assured us that responsible investment is often addressed at board meetings However, there are times when the agenda cannot be fully covered, leading to additional ad hoc meetings. In addition, the board conducts monthly learning sessions featuring experts who discuss a variety of topics – recently, these sessions have included valuations and responsible investment. We were pleased to hear of the trust's enthusiasm to scope out learning opportunities in this area.

The board has gender parity but falls short of the Parker Review targets. Given that the trust is in the UK 250, it has until 2024 to either comply or explain. The chair confirmed that the board intends to meet this target before the end of the year. The next non-executive member to retire will be the senior independent director (SID); she will reach a nine-year tenure at the next AGM. The audit committee chair has been on the board for 15 years and plans to retire in 2025. We questioned the succession sequence. We shared our position that the best practice for tenure is nine years, however the chair disagrees, preferring at least one director to have a lengthy tenure. In his view, as private equity investments have long term horizons, sometimes reaching ten years, longevity of NEDs is helpful. We will agree to disagree.

Outcome: The board is making some changes to the board composition and will be looking to comply with the Parker Review targets by the end of the year. Going forward we would not expect tenure to exceed nine years, aligning with industry best practices, and expressed our opposition to longevity of NEDs.

Intermediate Capital Group - Environment Social Governance

Objective: We met with the newly appointed chair to engage on the group's diversity strategies, the recently approved remuneration policy and the company's net zero commitments.

Our discussion covered a range of topics as this was very much a check-in conversation with no material concerns to raise. This was our first meeting with the chair, William Rucker (appointed in 2022). The company continues to be a relatively strong performer when it comes to gender diversity, with 41% of top management positions being held by women. Board gender diversity recently dropped to 36% following a NED departure. In response to us raising the topic of diversity strategy, we were assured that diversity will be a key focus in hiring new members in 2023/24. The company recently amended the structure of the remuneration policy, switching to a more traditional percentage of salary framework for executive long-term incentives. The board was looking to simplify compensation while keeping levels competitive - we supported these changes. The company has made progress on its Net Zero Strategy, aiming to reach that target by 2040 and have SBT aligned commitments in place. The funds tend to have lower GHG emissions, as they do not have large allocations to energy and mining (not seen as their traditional areas of expertise). All funds also exclude companies with significant coal, oil, and gas activities. Given the nature of the asset class, engagement is a focus of the responsible investment process. Some investments have limited capacity for engagement, particularly secondaries (where they do not typically hold a board seat).

Outcome: This was a useful catch-up conversation with the recently appointed chair. No material concerns raised as the company continues to progress verified net zero commitments and maintains a focus on talent, retention, and diversity.

Pantheon International - Governance

Objective: Following on from out meeting in May, we wanted to follow up with the chair regarding the recent shareholder feedback he received. Additionally, we wanted to approach the topic of succession planning to understand the board's plans for its composition. This discussion formed part of our overall investment trust thematic engagement.

The chair gave us an update on his recent shareholder engagement; he emphasised that he was prioritising shareholder feedback and trying to implement it as far as possible. The chair mentioned that the discount was raised as an issue by a number of investors. Therefore, the board decided to announce the £200 million shareholder buyback in response to the large discount.

The board has added two new directors, one who has extensive audit experience, and the second one who was previously affiliated with Unilever and has a strong marketing background. The board used Sapphire Partners to help with the executive search. The board will be looking for an additional two directors ensure a smooth transition. This will increase the total board size; however, the chair thinks it is beneficial to have substantial overlap periods between directors.

We had a discussion regarding the ownership of shares by non-executive directors. The chair holds a significant position in the trust and believes that it is considered best practice for directors to have shares. However, he also agrees that personal circumstances may affect the ability of some directors to purchase shares.

Outcome: We welcome the board being proactive in listening to shareholder feedback, particularly with the recently announced efforts to tackle the discount.

Polar Capital - Governance

Objective: To discuss our expectations for governance and disclosure for investment trusts.

Polar Capital is an investment adviser responsible for managing several investment trusts. The company secretary, along with the sustainability team, is engaging with the top five shareholders of each trust to gather feedback on governance preferences.

During our conversation, we discussed our recently published paper on investment trust expectations. We were satisfied to hear Polar Capital recognises that investment boards are obligated to align with FCA diversity guidelines.

Outcome: We welcome the manager taking a proactive approach to engagements. Additionally, Polar Capital stated that, although the trusts it manages are not required to do external board evaluations, it is considering how to implement these following the recommendations outlined in our paper.

Princess PE - Governance

Objective: Following various issues with the trust including two non-executives stepping down ahead of the AGM; we engaged with the board to discuss the future plans for the trust.

In late 2022, we had a meeting with Richard Battey, the former chair of the board, following the announcement of the dividend suspension and decision to stop new investments. During the meeting, we expressed our concerns regarding the board's independence and the lack of experience in private equity. We also sent a formal letter to the board, stating our intention to vote against all directors unless suitable changes were made.

We engaged again in March 2023. The day before our engagement, the trust announced that the chair (Richard Battey), who was approaching 14 years on the board, would step down at the next AGM, with plans for Steve Le Page to succeed him as chair of the board. During this engagement, we welcomed the board change, but we made clear it was not enough. We sent a revised letter to the board expressing our opposition to the reappointment of Felix Haldner, a manager representative, and Henning von der Forst, due to his lengthy tenure, and stated our intention to vote against their re-election.

Shortly before the 2023 shareholder meeting, the trust announced that two directors would stand down: the manager representative and the incoming chair. The remaining board consists of Henning von der Forst, whom we do not consider independent owing to his tenure, and two other directors based in Guernsey, neither of whom have private equity experience. Fionnuala Carvill, one of the Guernsey-based directors, will serve as interim chair until a replacement is recruited.

The board is looking to recruit for a total of three directors, however, it will start with the chair as he/she will influence who the other two directors are. We clearly outlined the skill set we expect in regard to the chair and the board as a whole. The board has confirmed a preference for a candidate who has previously served as chair of an investment trust.

The board has not yet decided whether it will replace the manager's representative on the board. At the meeting and through communications since, we have advised the board that we will vote against any manager representative appointed to the board; and indeed, following further internal discussion we have informed the board that we will vote against all board members if a manager representative is appointed as NED.

On a separate note, the trust has ended its foreign exchange hedging strategy. This move should help with the dividend stability, which it has reinstated at the previous level of 5%, however we are concerned that the dividend rate is too high. The board should prioritise ensuring is the dividend is not cancelled again, as another cancellation could mean irrevocable damage to the trust's reputation. The chair explained that many shareholders rely on the dividend for income, making finding a solution more difficult.

Outcome: We have informed the board of our voting intentions regarding the re-election of the over-tenured NED as well as the appointment of any future manager representative. We have taken a particularly hard stance with this trust owing to the past failures of the board and the manager in communicating with each other and with shareholders.

Prosus – Governance

Objective: To discuss concerns related to the current remuneration policy.

Our proxy voting service provider recommended voting against the remuneration report. The company does not set performance-based targets for its long-term incentive plan portion of its remuneration policy, and there are concerns over the total amounts vested for long-term incentives for the 2023 financial year. We contacted the company for more information. While the company notes it incorporates strategic, operational, sustainability and financial objectives into the remuneration structure, specific performance targets and achievements are not provided, as the company prefers linking pay out to valuation. This lack of transparency is not in line with best practice. Additionally, there is a concern that the policy is overly focused on linking incentives to profitability metrics which does not necessarily align rewards to a more balanced view to long-term business performance.

In response to shareholder feedback, we identified that the company has taken steps to improve its disclosure on the specific performance targets under the short-term incentive plan which we welcome.

Outcome: Performance based targets within executive remuneration is a topic we have engaged with the company on previously. While the company has improved its disclosure regarding short term incentives, we expect a similar level of transparency for the for longer term components of pay. Therefore, we decided to vote against the remuneration report.

Siemens – Environment

Objective: To discuss Siemen's decarbonisation strategy and interrogate its existing net zero targets.

As part of the IIGCC's Net Zero Engagement Initiative (NZEI), we engaged with Siemens to discuss its decarbonisation strategy, progress against emissions reduction targets, and its associated programmes. The focus of the engagement was to interrogate the robustness of Siemens' decarbonisation strategy and discuss significant challenges particular to the business.

We began with an outline of Siemens' net zero journey beginning in 2015 as one of the first industrial companies to commit to net zero and set SBTi-validated targets[1], culminating in the accelerated goals introduced late 2022[2]. Siemens considers itself well-positioned to achieve its decarbonisation targets given that many of its products are components designed to increase energy efficiency or otherwise enhance the efficiency of large machinery.

Among the issues we highlighted in our discussion was clarifying divisions between the various Siemens companies and its climate-related targets; the apparent increase in the 2022 Scope 3 emissions; progress against their EV targets and associated policies; and Siemens' role in industry groups.

When asked about the apparent increase in the 2022 Scope 3 emissions, the company confirmed this and noted it was displeased over despite the relative improvement in emissions intensity (purchasing volume increased 16% over the previous year, while emissions only increased 2%). Siemens sees supply chain (Scope 3) engagement as key to unlocking its decarbonisation targets and is trialling a new tool 'SiGREEN' both internally and externally, where software protects a company's sensitive carbon data while producing real-time, actionable carbon measurements of a company's products.

We were interested in understanding what Siemens sees as the most significant challenges facing its DEGREE decarbonisation strategy. We touched on whether Siemens sees regional variation in climate-related regulation as a risk in global market capture, given nearly 40% of 2022 revenue came from the US and China, both considered politically inconsistent in their approach to climate policy. When asked what it considers the 'stickiest' emissions to address, Siemens reiterated the challenges of addressing supply chain (Scope 3) emissions, particularly second tier suppliers, who may have more limited resources to decarbonise their operations.

Our discussion turned to Siemens' action plan to address Scope 3, and how it views its approach as compared to peers. Siemens considers its approach to calculating these figures to be both industry-leading and in line with best practice, with Scope 3 figures which are precautionarily high and Scope 4 figures providing useful context in cases where earlier-than-planned replacements can lead to emissions savings in the longer term.

1 50% reduction in all operational emissions by 2030 [Scope 1 and 2], and 20% reduction in supply chain by 2030 [Scope 3]

2 Operationally net zero by 2030 (90%; 10% allowance for offsets of residual emissions), as well as new mid-term target of 55% reduction in operational (S1&2) emissions by 2025 (2019 baseline). Siemens also announced a further €650m investment into decarbonisation-related technologies.

Outcome: Siemens' net zero strategy appears to be clear and comprehensive, and it has evidenced ongoing progress (46% reduction in operational Scope1 & Scope 2 emissions in 2022). The fact that the company accelerated targets recently – explicitly excluding affiliates within the company that are not willing to push for more aggressive reductions – is further evidence of an organised approach and high level of commitment. The company responded to our queries with credible explanations, clarifying the slight increase in supply chain (Scope 3) emissions in 2022 and reiterating the innovative programmes (e.g., SiGREEN) they are introducing to advance both their own decarbonisation trajectory and that of the broader manufacturing industry. We have agreed with our collaborators to meet again before Siemens' AGM in February 2024, to discuss any points we might wish to raise and whether virtual attendance would be relevant.

Texas Instruments – Environment Social Governance

Objective: We engaged with the company to discuss concerns related to relative climate performance, information security and diversity practices following our biannual review of the ESG factors within our proprietary ESG dashboards.

Our review highlighted a few areas of concern: carbon emissions, information security disclosure and low relative board gender diversity. Unlike peers who have licensing agreements with third parties, Texas Instruments (TI) manufactures most of its products and therefore takes ownership of the associated scope 1 and 2 emissions. TI's focus is on a short/medium term emissions reduction plan, focusing on the main components of the scope 1 and 2 emissions (use of fluorine gases and energy inputs). On diversity, there is concern that the company may not be developing, attracting, and retaining a significant pool of talent – and performance could improve in this area, and we would encourage TI to publicly disclosed targets.

The company was able to confirm it has received certification on information security standards. It also confirmed that it does not disclose details of specific insurance policies and follow all laws where disclosure of specific breaches is required, but do not disclose anything that is not legally required. This is an improvement on the data sourced from our ESG data providers but does not provide transparency or complete comfort across their information security process.

Outcome: The engagement helped to improve our understanding of the company's GHG emissions performance management. The company does not provide a significant degree of transparency on information security standards. Gender diversity performance looks to have stalled, and the company has not outlined the targets and strategic vision that could be a catalyst for improvement. We will monitor these factors moving forward.

Thematic Engagement – Labour standards in supply chains - Social

The below meetings are part of our 2023 thematic engagement on labour standards in supply chains in the apparel sector. The aim of these conversations was to have a detailed interaction on the topic with investee companies most exposed to human rights risks in this area.

ADIDAS AG: Although some of the companies we have engaged have short production lead times (fitting the 'fast fashion' label), Adidas does not obviously fall into this category and tends to have longer product cycles and stricter supplier policies limiting changes to manufacturing instructions beyond a certain timeframe. We covered five main areas of supply chain management, including governance of labour standards, the auditing process, challenges in addressing issues beyond primary supplier, grievance mechanisms &, remedial actions and wage setting. Adidas divulged that challenges and limitations arise from operating a complex global supply chain, most notably the visibility and ability to change behaviour at non-primary suppliers. The company has reasonable measures to extend labour standard assessments down the supply chain but have been accused of using cotton from Xinjiang (a region of China where human rights abuses has been documented). The company disputes this and states it does not source cotton from this area, an example of the difficulties in monitoring Tier 3 suppliers. We consider the company's social assessment indicators (S-KPIs), used to assess suppliers, as comprehensive and probably represent a best-in-class methodology. The newly implemented living wage benchmarking system is also a strong statement on the company's commitment to labour standards.

Outcome: This was a constructive conversation on policies and processes. Adidas has a long-established supply chain auditing process run by a well-resourced labour standard auditing team. Oversight of the labour standards process is very closely controlled by the executive function. As part of future engagement, it would be helpful to explore the role played by the board in governing labour standards.

ASSOCIATED BRITISH FOODS PLC: We welcome the board focus on this issue and believe the reporting line into the ABF audit committee supports this effort. One notable gap was the lack of global coverage for a supply-chain grievance mechanism, having them only in the largest manufacturing regions. We would expect greater coverage moving forwards. The in-house auditing team is well resourced and locally based. The company has also dedicated some time to understanding whether the in-house auditing approach is effective through a study with Harvard University. Raw material traceability is also an area of strength. The 'Sustain Cotton Programme' has had a significant social and environment impact and is scalable, currently producing 50% of the cotton needed in the manufacturing of products. The use of DNA testing for raw materials to improve traceability is also a best-in-class feature of the risk monitoring process that some peers have shied away from owing to cost.
Outcome: This was a positive engagement and, broadly speaking, the company demonstrated a thoughtful approach to managing human rights risks in the Primark supply chain. Although it can be questioned if the manufacturing of 'two-pound t-shirts' can ever be sustainable, the company has made significant effort and progress in monitoring and mitigating human supply risk.
BOOHOO PLC: This was a useful discussion and goes some way to demonstrate the progress the company has made since its 2020 supply chain failures. Based on a detailed and well publicised internal investigation, the company has looked to place supply chain monitoring and management at the centre of governance structures. We welcome the fact that responsibility for monitoring sits with the Risk Committee. From an operational perspective, Boohoo has an experienced internal team led by an individual who previously ran supply chain monitoring processes at Primark. The combination of using external auditors and local direct employees is in line with best practice amongst larger apparel companies. Although this internal auditing process covers most markets, we would like to see this extended to Pakistan and India; two obvious gaps. We also welcome efforts to expand supply chain mapping to Tier 3 raw material providers, something that has been done in China and we expect this to be expanded into relevant product materials. Although the company has a strong focus on meeting national minimum wage requirements, the company does not benchmark country living wage requirements, which is something being undertaken by some larger apparel companies. It is appreciated that input costs are a key concern given the company's business model – but national minimum wages are not always a perfect proxy for living wages.
Outcome: We are comfortable with the progress made and it is clear that the company places a strong focus on fostering positive supply chain relationships and maintaining good labour standards at supplier facilities. We will continue to monitor the extension of the supply chain mapping.

JD SPORTS: The company is predominantly an apparel retailer with a small private label manufacturing process (c.7% of sales). The company is highly dependent on sourcing products from very large apparel companies like Nike and Adidas. Given the profile of the brands it works with and the well-established supply chain monitoring processes in place, JD Sports has a light-touch due diligence approach which involves reviewing policy alignment at the onboarding stage. The management and monitoring of human rights risks at the small private label activities does not appear to be as robust as other apparel companies with which we have engaged. The company does not supplement the reports through regular in-house audits, and it does not have an internal supply chain grievance mechanism in place. The company will stop working with suppliers with critical issues and will assess human rights risks when onboarding a supplier, however, we believe that it appears to capture little real-time information on labour standard performance. Again, it is noted that the private label business is a small part of activities, but it lacks some of the key tools (like in-house auditing frameworks, a third-party auditing procurement process etc.) used at other apparel producers to mitigate human rights risk in globally distributed supply chains.

Outcome: This was a useful conversation to benchmark performance. While we are comfortable with the approach to onboarding new product partners for retailing activities (which represents most sales), monitoring of human rights risks in the private label supply chain appears less robust. We have highlighted these gaps to the company and will continue to monitor progress.

MARKS AND SPENCER: The company has been an early adopter of best practice supply chain management and it was useful to discuss how the labour standards approach has evolved over this time. It is positive to see that the board plays a key role in the continued prioritisation of labour standards in supply chains. Any high-level risk supply issues are elevated to the main board for discussion, alongside being a regular topic of conversation at the audit and risk committee. The company has adopted a hybrid approach to supplier auditing, pairing third-party regular audits with in-country M&S Ethical Compliance team members. There is a focus on primary supplier monitoring and the hybrid approach allows the company to closely monitor auditing standards while engendering a more collaborative approach with suppliers. The in-country expertise is a valuable tool in keeping supply networks flexible, identifying high quality potential suppliers, and working with current manufacturers to improve practices. The company offers multiple grievance mechanisms to cover the large global supply footprint. It also conducts 'deep dive' worker surveys in seven countries (alongside NGOs). This 'Worker Voice' is an innovative practice that aims to take a detailed temperature check on working conditions and trends. Raw material sourcing transparency is a key challenge. Cotton is the main raw product used in their apparel supply chain. The company is part of the 'Better Cotton' Initiative's program to improve the social and environmental impact of cotton production. M&S uses DNA source testing to identify, as well as prevent, sourcing of the material from areas with high risk of human rights abuses. The company reiterated the need for an industry wide solution for a living wage provision within supply chains. The company has attempted to apply living wage measures on an individual basis previously, but found this an ineffective tool for sustainable, meaningful change.
Outcome: This engagement reaffirmed our view of the company's robust approach in this area. Managing and monitoring high labour standards is integral to the company's values and branding. The company maintains a balance of in-country sourcing expertise over centralised UK staffing. This approach has proved effective to date. It is positive to see that the company has maintained a focus on innovative collaborative programs (with NGOs and other retailers) to improve supply chain transparency and labour standards.

Thematic Engagement – Product safety and litigation risk – Governance
The below meetings were part of our 2023 thematic engagement on product safety and litigation risk in the pharmaceutical and healthcare industry groups. Managing product safety is key for companies as it can impact financial prospects, as well as trust amongst consumers, suppliers, and investors. Product safety breaches are described by the US Consumer Product Safety Commission (CPSC) as the unreasonable risk of injuries and deaths associated with consumer products. Failures in product safety can lead to litigation which can incur significant costs. Some of the largest corporate fines in US history have been awarded against pharmaceutical companies. The litigation process may take years, and until the case is resolved there is a degree of uncertainty that in some instances may have implications for the company's valuation. Additionally, the reputational damage of these high-profile cases may become embedded in the customer's vision of the brand. Finally, there is the human cost when drugs or medical equipment fail the patient. We discussed governance risk oversight, the operational product safety process and litigation risk.

ASTRAZENECA: At AstraZeneca, we recognise the science and quality focused approach that has been driven by the CEO and board. Digital information gathering and sharing from product development to post approval outcomes appears to be a key factor in shaping the Global Quality Team's ability to proactively monitor and react to adverse incidents. It is encouraging to see that both litigation and product quality are seen as key board matters, with reporting lines into the audit committee. For peers, quality management seemed predominantly executive driven. Although it is difficult to compare litigation strategies across the sector, given the lack of transparency, it is also encouraging to see proactive management of emerging litigation issues, close monitoring of sector wide events and regular board scrutiny of ligation strategies.

Outcome: This was an informative conversation, and we appreciated the company's openness in describing the product quality/safe journey as well as an overview of litigation strategy. We have found that other companies engaged in the campaign have been less willing to discuss litigation, so the level of transparency was welcome. This openness may be encouraged by the company's lack of major litigation events in recent years. AstraZeneca feels it has a good story to tell in terms of governance, quality processes and culture – and we broadly agree.

PFIZER: Pfizer was fined $2.3bn in 2009; one of the largest healthcare fraud settlement and criminal fines charged by US regulators, owing to unethical marketing of an off-label use product. Since that time, the company has restructured its governance and risk oversight channels, by adding a new committee reporting to the board to provide better board oversight over potential regulatory and safety breaches. The information provided on structural governance changes since the 2009 fine was helpful but, given the scale of the charge, we would have been surprised if nothing had changed. Litigation is a common event for US pharmaceutical companies so it would have been helpful to have more specific detail on how Pfizer sizes potential risks and manage potential compensation events. It is positive to see that the company has a well-resourced global quality management system, as this meets expectations.

Outcome: We welcome the company's responsiveness and openness to engage on the topic, but the discussion was very much limited to high level commitments and a general review of risk oversight structures. The conversation may not have shed light on Pfizer's value-add in this area, but as expected, it has a focus on compliance and a relatively clear chain of risk oversight structure.

ROYAL PHILIPS: Currently, Philips is facing challenges in the respiration business with a significant product safety issue resulting in a product recall for ventilators commonly used for sleep apnoea therapy amongst other uses. Concerns were identified with the sound abatement foam that was used as this could potentially degrade and result in particles being inhaled by patients. The recall has affected millions of customers and there is litigation in place claiming that the degrading foam has impacted users' health and may have even resulted in deaths. The company has enacted a voluntary recall of these products (i.e., not initiated by FDA) and aims to replace or repair 5.5 million devices (so far 4.4 million of which have now been returned or replaced). The new respiratory machines have undergone testing in five international labs, with an external medical panel assessing the outcomes. The company is still in the process of completing internal testing to understand whether foam degradation caused 'appreciable harm' to patients. The company stated it is 95% of the way through the investigation and maintains, based upon the results, the issue should not have caused 'appreciable harm'. These data have been shared with the FDA. The company is aiming to embed quality based KPIs across all business functions. As an additional oversight function, Royal Philips has strengthened a patient safety board committee that engages with customer feedback and includes both internal and external members. The board also has visibility of the QMS (Quality Management System), and the company reports it has reduced quality issues by 30% and is aiming for a further 45% reduction. The board also engages with regulators in different countries to ensure compliance. For the time being, given the magnitude of the respiratory product recall, the 'Sleep and Respiratory Care' business will be reporting directly to the CEO.

As mentioned above, following the most recent recall the need for a change in approach is recognised. This is as a result of the new leadership, a change in business culture (focus on quality) and recruiting more medical technology talent. This talent recruitment is taking place across functions including a new chief operating officer who is joining from Johnson & Johnson to oversee supply chain details. Royal Phillips has recently renewed most of its regulatory team, with many members coming from medical companies. Royal Philips has observed that 70% of its product issues stem from design related problems and it is investing in talent and compliance resources in this area. Additionally, the company currently has over 5,000 suppliers. Therefore, to reduce the risk and maintain quality standards Philips is streamlining its supply chain and severely reducing the number of suppliers. The company also believes a tighter supply chain with help with the supply issues it faced during the pandemic, during which time it struggled to move to new suppliers quickly given the deep auditing process required across a globally dispersed chain.

Outcome: Royal Philips is investing in human capital to acquire expertise from other medical technology companies. Furthermore, the company has identified the design phase as the root cause of most of the recall issues, so this is a key area that it will be focusing on. Regarding risk oversight, it was unclear how the structure operates and how the board participates in the process.

Thematic Engagement – Cybersecurity – Social

The below meeting were part of our 2023 engagement on cybersecurity risk. This is the first phase of the engagement, which we will use as a risk assessment on the cyber governance of companies within the IT software and telecommunications industry groups. The conversations are also being used to establish best practice cyber governance. Some of the key topics we covered in the meeting included: the threat landscape, board communication, skills and resources, and training.

BT GROUP: BT Group is a provider of the UK's critical infrastructure and serves multinational companies and governments globally. As a result of this, the company is a high-risk target for hostile cyber actors. The first discussion point was on BT Group's cyber security journey and its commitment to this issue. Cyber security is integral to its business, and this is exemplified through the company's resource, partnerships, and spending. The company employs over 10,000 people in its technology unit and spent a total of £604 million on research and development last year. These technology units include specialist facilities dedicated to cyber security. The company has combined the cyber, physical and personnel security teams into one function under a new expanded role of Chief Security and Networks Officer, who sits on the Executive Committee. Through this function, there are direct reports to the board on a quarterly and ad hoc basis. The audit and risk committee has the primary responsibility for monitoring cyber security closely and receives additional support from independent and external strategic cyber security assessments.

From reviewing the threat landscape, BT has identified five key risks which are referred to as vectors. These vectors include Nation States, Hacktivists, Criminal, Terrorist, and Insider Threat. These vectors can and do operate together. The two vectors highlighted for posing the most significant risks are Nation States and Criminal Groups. The threat from Nation States has grown significantly following the war in Ukraine and the company has found some evidence that these state and criminal groups are actively targeting BT and other telecommunication companies, seeking to make financial gain. With regards to emerging risks, AI and machine learning has been highlighted as a key threat. BT's internal research has found AI and machine learning could be weaponised as security threats. The company has industry, government and customer partnerships which are used as an opportunity for wider learning. These are some of the main factors being used by the company to maintain its leading position.

Outcome: This was an engagement for information which we have used to improve our understanding of best practice cyber governance. BT Group is engaged with this topic and has demonstrated its commitment through its partnerships, resources, and expertise. There were no major breaches identified against the company and we are pleased with the level of disclosure provided on all topics discussed. This evidences how the company is following best practice and we will use this to benchmark against industry peers.

DARKTRACE: Darktrace provides a unique perspective in this engagement as the company is a cybersecurity business, which sells artificial intelligence products to corporates.The central pillar of Darktrace's cyber security journey over the past five years is based on compliance with industry leading certifications such as ISO 27001 AND ISO 27018. To maintain these certifications, the company has a dedicated 'red' team who are responsible for testing controls, and this is supported with the compliance team's regular monitoring. Compliance with these certifications is seen as an effective tool to protect sensitive data across the enterprise and the company considers this a good benchmark to assess the effectiveness of industry peers. Darktrace also has a product team with responsibility for researching the threat landscape. From this research, the company has identified the move to cloud technology has created emerging risks relating to API security.

Cyber security is a key topic discussed at all board meetings and the audit and risk committee have the primary responsibility for overseeing this issue. The company Chief Information Security Officer (CISO) provides annual and ad hoc presentations to the board on key developments in this area, as well as individual meetings to ensure all board members are up to speed on the topic. These individual meetings are part of the company's cyber security training which all employees will undertake and new joiners across the business will receive individual training from the CISO. All employees must complete a semi-annual security information security test and failure to pass this will result in losing access to key systems. The development community and cyber experts will have to complete more detailed training through immersive labs. Darktrace confirmed during the meeting that there has not been a reportable breach in the last three years, there is an information security insurance policy and training is available for all employees across the business.

Outcome: This was a positive meeting, where we covered key topics such as the threat landscape, the company's journey over the past five years and overall governance of this issue. We are pleased with the perspective provided by Darktrace, as a cyber security company. We will use the suggestions provided on industry leading certifications, to monitor the other companies we will be meeting for this thematic engagement. One notable gap was identified, and this relates to the level of disclosure on information security topics such as training, insurance, and breaches; we discussed this with the company and expect to see this improved.

SAP: Cyber security is integral to SAP's values and the company has continually evolved over the past five years, in line with new threats. These threats have grown in sophistication. Increasing activity from state actors since the outbreak of the war in Ukraine has required the company to be increasingly alert. To adapt to these risks, SAP has shifted data management to cloud technology, where there are higher security standards. This has enabled the company to concentrate their business with single strategic suppliers. While cognisant of these threats, the company is also mindful of emerging issues such as artificial intelligence and the use of deepfake videos to misrepresent the company. This has not posed a significant threat at present but is expected to change in the future.

The company cultivates and maintains a broad network of partners across multiple domains (government, industry, public-private partnerships, industry trade councils, etc.) to enhance and optimize the security of its products, services, and customers. In the legislative and regulatory space, SAP works with numerous industry trade councils and public-private partnerships across all regions of the globe to advocate for more sound and efficient cybersecurity regulatory policy.

All employees are required to complete quarterly and annual training on social engineering, phishing, and regular email alerts. The company has security ambassadors who work across the business. These ambassadors undertake further tests and are responsible for providing education sessions to their dedicated teams. The final area discussed in the meeting was cyber spending as a percentage of revenue and whether this falls under finance or IT. Unfortunately, the company would not disclose this number but confirmed the cyber budget was part of the research and development budget and has a faster growth rate than the IT budget.

Outcome: This was an engagement for information which we will be using to improve our understanding of best practice cyber governance. We discussed several key topics such as board communication, industry partnerships, and the company's cyber budget. This was a positive meeting, and we are pleased with the level of detail provided on key topics.

T-MOBILE: At T-Mobile, the cyber security culture has been built around change, education, and awareness. All employees must complete 100 hours of formal and informal training, and this is personalised based on the role undertaken. The training is throughout the year and will cover key topics such as good password setting, phishing as well as watching simulations. External industry experts are invited to come in and provide a teach-in on cyber security, and all employees are subject to multi-authentication when logging in. This is used to build the culture of awareness, change and education.

These training sessions are supported with internal and third-party audits, penetration tests and scores to identify and escalate any risks.

T-Mobile has been subject to ongoing negative press relating to a large-scale data breach in August 2021, which exposed the personal data of approximately 76.6 million people. This has led to the company receiving a low governance rating from several major ESG ratings providers. We discussed these concerns in the meeting to assess how the leadership team approach serious breaches and the likelihood of reputational damages. T-Mobile participates in several cyber initiatives, relating to collaborative communication and advocacy. Through these partnerships, the company has direct lines of communication with federal agencies, opportunities to share best practices, and access to situational awareness.

The final area discussed in the meeting was cyber spending as a percentage of revenue. Unfortunately, the company could not disclose this information as it is not shared publicly. However, we received confirmation on a $150M budget in incremental spending made across 2022-2023. This is court mandated owing to the serious cybersecurity breach.

Outcome: This was a largely positive meeting, where we covered key topics such as board communication, culture, skills and resources, training, and budget. Board communication is completed on a quarterly basis by the senior officers and the recent hire of ex-IBM CFO is seen as one of the key resources on the board. The cyber culture involves extensive training, with a focus on change and awareness. Finally, the company could not disclose cyber spending as a percentage of revenue and could only confirm a budget of $150M in incremental spending has been made across 2022-2023.

VODAFONE: As part of our internal quantitative review of monitored holdings, we assessed Vodafone to identify its involvement in any relevant negative controversies prior to the meeting. Through this review, we identified the company was flagged for having limited disclosure on how it had resolved a data breach relating to VodafoneZiggo. Vodafone confirmed this issue had been resolved through the business continuity and disaster recovery unit and these large scales issues are always escalated to the board for review. In this case there were no subsequent incidents because of the leak.

Vodafone views cyber security as the responsibility of all employees. As a result, all employees will have to complete cyber security training as part of their development plan. Simulation training using phishing is completed on a bi-annual basis and if employees do not pass this then further training is required. Executives are part of this training programme.

The cyber security budget is embedded across the business, and Vodafone could not disclose how much had been spent. However, using the number of cyber security employees as a proxy for budget, this team has grown by 25% over the past three years from 800 employees to 1,000 which is one of the largest across the industry. Regarding the threat landscape, some of the most significant threats identified by the company were ransomware, hybrid attacks leading to account takeovers and state actors which are a by-product of the outbreak of the war in Ukraine. There are also some emerging threats from the move to quantum computing. This new technology is being developed to solve complex problems within hours, which would take classical computers several weeks. Quantum computing is still at an early stage and internal research has found it is currently lacking cryptographic principles that may create encryption security related risks. The company is working with business partners such as IBM to tackle these emerging issues.

Outcome: This was an engagement for information which we have used to improve our understanding of best practice cyber governance. We discussed key topics such as board communication and expertise, skills and resources, training, and cyber security budget. The level of information provided was mostly in line with the detail we have received from other target companies during this thematic engagement. There is regular communication with the board and all employees complete cyber security training. The technology committee provides additional support to the audit and risk committee on monitoring threats, and this demonstrates Vodafone's commitment to cyber security. The company did not disclose the cyber security budget; however, it provided an indicator on how this has grown by 25% over the past three years. We would welcome more disclosure relating to how the company is addressing data leaks.

FUND ENGAGEMENT

We invest in funds managed by other investment firms. Below are some of the third-party fund engagements we have carried out over the last year. We have anonymised this given the nature of the discussions. We track the developments and outcomes over time.

The engagements are split into four areas:

1. The firmwide approach to responsible investment

2. Manager and strategy approach to responsible investment

3. Engagement on ESG risk and exposure

4. The firmwide approach to net zero

Third party manager – multi-asset - The firmwide approach to responsible investment

Objective: Conduct a review of the manager's ESG integration processes via a demonstration and discuss their current ESG analysis process.

At this meeting, one of the manager's ESG directors provided a demonstration of the manager's ESG analysis process, with context around how it undertakes ESG integration in its investment process, and how it arrived at its current practices. The manager operates a proprietary ESG ratings platform on an internal system, where its research analysts grade holdings against sector-specific material issues (based on, Sustainability Accounting Standards Board (SASB) materiality map). Research analysts compile ESG scores based on the analysts' view of the company; they emphasised that they see this reliance on analysts' judgment as a better reflection of the manager's 'hands-off' approach to its investment managers' decision-making. Consideration of ESG factors in investment decision-making appears to rest primarily on portfolio manager (PM) discretion – there is no 'house view' on any ESG issues, outside of the cases where the manager has made a corporate external commitment (e.g., deforestation / Finance Sector Deforestation Action pledge).

Outcome: The demonstration and discussion were a helpful information-gathering exercise, allowing us some insights on how other asset managers are incorporating ESG integration into their investment process. The manager views its ESG research outputs as a resource for PMs to use as appropriate to the products they manage, rather than a top-down imposition on PM decision-making. It was noteworthy that the manager relies on its analysts, rather than sustainable investment team, to undertake ESG scoring.

Third party manager – private equity - The firmwide approach to responsible investment

Objective: To discuss and evaluate the ESG integration process.

The firm has been focusing on increasing its ESG capabilities. The number of people dedicated to responsible investment has exponentially grown over the last couple of years to 25 at firm level, five of which are dedicated to private equity (PE).

Regarding internal updates, the company is prioritising its climate commitment by addressing scope 1 and 2 emissions (such as reducing facilities energy consumption and employee travel), as well as improving employee well-being, with a focus on attracting and retaining the best talent. We are pleased to hear of the company's actions towards developing in this area.

The manager has also been working on producing ESG scores for each company it owns, as well as a climate alignment score, to assess their net zero compatibility. Most of the strategies do not have sustainable objectives, but for the ones that do, it also produces a sustainability score of 0-3 which rates the social and environmental impact of the company's activities. The combined sustainable strategies are approximately £1 billion, which is still a small percentage of the £111 billion under management.

In 2022, the manager became a part of NZAM and has dedicated 1.9% of its assets under management towards achieving net zero. Currently, only its sustainable funds are included in this commitment. Additionally, the manager discussed its efforts towards reducing scope 1 and 2 emissions, which although important, which we pointed out only make up a small portion of the overall emissions.

The firm has obtained five stars in its 2021 PRI submission, and it has produced its first TCFD report this year, which we regard as positive steps.

There was also discussion around the various ESG committees that oversee the integration of ESG-related factors into the investment process. The firm has also joined several initiatives in the private equity sector to enhance data disclosure: a major concern in the industry.

Outcome: There has been a significant improvement in the manager's responsible investment capabilities in recent years. However, there is still room for improvement, particularly in terms of disclosing how ESG factors are integrated into practice.

Engagement on ESG risk and exposure

Third party manager – Asian equity – engagement on Whitehaven - Engagement on ESG risk and exposure

Objective: To understand the manager's engagement strategy with new coal holding (Whitehaven) as part of broader conversation about ESG integration in the manager's products

Following the annual meeting with the fund manager in May, there were a number of outstanding questions around the fund taking a new position in Whitehaven, a large thermal coal producer in Australia. The manager arranged for a follow-up meeting with the regional analysts from the Sustainable Investing team in Australia. The manager has engaged with Whitehaven as part of the firm's thematic engagement around thermal coal producers. Whitehaven is currently missing both stated climate targets and internal climate policy, both of which are required as part of the firm's 'minimum climate requirements' for companies. After engagement, Whitehaven did not make any timing commitments on climate targets, nor did the company commit to no new greenfield coal developments (a key goal in the manager's coal engagement). The manager is waiting until Whitehaven's 2022 sustainability reporting is published in September to evaluate whether Whitehaven has met the firm's requirements and request further engagement.

We queried the manager's approach to ESG scores and received confirmation that ESG scores are not required for all companies in the manager's holdings unless they are included in a sustainability fund/product. The sector analysts, who undertake ESG scoring, dictate whether and when a company is rated based on what they view as the best financial opportunities for portfolio managers (PMs). We noted our concern that carbon-intensive companies or carbon 'laggard' companies are included within the investment universe without ESG ratings. While the firm has taken some steps to provide ESG ratings for its PMs' consideration, the case of this fund's new holding in Whitehaven has revealed how 'loose' these screens are. PM and research analyst discretion dictates whether companies receive ESG ratings, which casts some doubt on how thoroughly the manager is vetting both existing and new holdings for ESG-related risks.

Outcome: This discussion provided a useful case study in how the manager approaches ESG risks in carbon-intensive holdings (e.g., thermal coal) for an Article 6 fund. Given that Whitehaven does not satisfy the manager's stated 'minimum climate requirements,' still lacks an ESG rating months after joining the fund's portfolio and the company's noncommittal response to the manager's engagement, the manager's policies on ESG integration appear to be inconsistently applied. We believe this has left notable gaps in how firm-level policies are implemented at fund-level.

Third party manager – Asian equity – engagement on Asia Cement - Engagement on ESG risk and exposure

Objective: To query inclusion of Asia Cement's exceptionally high contribution to portfolio emissions.

Asia Cement was flagged in a report for its exceptionally high contribution to portfolio emissions. Despite making up only 0.02% of the overall portfolio that was being reported on, the company accounted for nearly 10% of the portfolio's emissions exposure. Given the significance of this outlier, this figure was investigated by the Responsible Investment team (RI team) and prompted a follow-up call with the fund owning Asia Cement.

The 10% figure (Contribution to Portfolio Emission Exposure) is a measure of the proportion of a company's emissions are 'owned' by the fund investing in them, based on the value of the fund's investment compared to the company's value. This figure is especially significant for Asia Cement, in part because of the low company valuation of $1 billion (average valuation of peers in comparison table was $182 billion), which determines the degree of 'ownership' the portfolio has of a company's emissions. This increased 'ownership' of Asia Cement increases the amount of its emissions the investment is linked to, producing higher-than-peer emissions exposure.

A meeting was arranged between Quilter Cheviot and the manager to discuss its Asia Cement holding and our concerns about emission intensity. The manager acknowledged that Asia Cement has much higher emissions per tonne product than peers, but stated this is due to state-imposed cement content requirements in compliance with earthquake-resilience regulations. As a result, the per tonne emissions footprint is approximately 25% greater than peers (e.g., Cemex, CRH).

The fund managers are aware of the comparatively poor carbon performance of Asia Cement, but believe the company is generally trying to do the right thing in a challenging environment and has financial advantages over peers. Asia Cement provided an overview document summarising its environmental/ carbon targets and recent relevant progress. However, there remain a few yellow, if not red, flags in the progress against the targets described. Notably, the summary promotes planned reduction of coal use in the near-term (2025), but coal usage across different facilities appears to equate to no reduction.

Outcome: Although the manager was forthcoming in addressing some of our concerns, it is unclear whether Asia Cement is making sufficient strides to reduce its poor emissions performance. It is worth observing whether it retains its financial advantages given the somewhat turbulent economic conditions in China. In follow-ups with the fund managers, we will focus on whether they hold any similar positions, and what conditions would need to be met for them to sell those holdings. For example, whether carbon performance has any weight at all in certain heavy-emitting sectors like cement.

Third party manager – US equities - The firmwide approach to net zero

Objective: Interrogate the fund's alignment to the firm's NZAM commitments.

This was the first meeting in our thematic engagement assessing how closely a firm's group-level NZAM commitments are reflected in the net zero-alignment of their funds. The firm is included in both the top 20 NZAM-aligned firms Quilter Cheviot invests in as well as the top 20 funds by value which are managed by NZAM signatories within our centrally monitored universe.

The firm provided an overview of its net zero commitments, and how it chose its target approach – SBTi / Science Based Target (SBT) coverage of portfolio. The firm considered SBT coverage to be the most robust, least 'gameable', measurement of companies' climate policies and performance. The firm cited concerns over the 'loose' definitions and somewhat subjective categorisation approach of some frameworks that may be considered misleading, increasing the risk of greenwashing claims. Using a third party-verified, industry-agnostic, and clearly defined standard (e.g., SBTi), had evident advantages to the firm, including a straight-forward engagement framework to build on.

We asked the firm about its climate engagement framework, which includes all companies in its holdings without SBTs. The firm believes strong relationships and reasonably significant ownership in its holdings translate to transparent, supportive engagements with those companies still lacking SBTs, and that in most cases, companies have strong cases for why this is the case (e.g., lack of existing guidance for their sector). The firm's engagement function is embedded in its investment team, and the firm believes it has good access to its companies and is able to maintain open dialogue over the firm's expectations of SBT alignment.

The firm has holdings in several relative climate laggards (e.g., Conoco Phillips), which was raised at the last meeting with the manager. We enquired how the firm approaches these companies within its SBT engagement; the firm considers most of these companies to be taking appropriate steps to adhere to the firm's NZAM target. Conoco Phillips is a member of the SBTi-convened industry advisory group and has voiced concerns over the inclusion of Scope 3 emissions in emissions reduction targets, which the firm interprets as supportive engagement. The firm is sympathetic to the quantity of sustainability-linked disclosures companies like Conoco Phillips is facing and is satisfied with the limited progress evidenced thus far.

Overall, the firm was confident in the achievability of its NZAM targets. Although the company recently grew its portfolio (from 45 holdings to 60) to include more mid-cap companies, it believes its hands-on approach will overcome the challenges mid-caps face in setting appropriate climate targets. Despite the fund focusing on American companies, the fact it does not cater to American investors insulates it from the political headwinds faced by American-based firms. The manager is unconcerned about 'net zero nervousness', as it believes that the bulk of American companies take a moderate 'middle ground' approach to climate risk in their business.

Outcome: The firm presented a solid case for its SBT alignment approach to its NZAM targets. The small size of the boutique firm and integrated engagement-led investment approach appears well-suited to the use of SBTs as its net zero alignment metric. The external, independent, and increasingly universally acceptable and applicable nature of SBTi provides a level of assurance against greenwashing, which seems to have weighed significantly in its approach to net zero. Although there remain some minor points of concern – some over-confidence in the optics versus the substance of companies' climate engagement – overall, the firm presented a cohesive and reasonably robust explanation of its approach and progress on its NZAM targets.

IN THE SPOTLIGHT

ARTIFICIAL INTELLIGENCE – FRIEND OR FOE?

Toby Rowe, Sustainable Investment Specialist

Source of image: iStock

With the advent of Chat GPT at the end of November 2022, a lot of questions have been asked about Artificial Intelligence (AI). What is it? How does it work? Is it safe? Important questions which haven't stopped the sector leading a technology rally year to date. On top of these common questions, our team has regularly been asked how AI fits in with a sustainable strategy. It's an interesting question because the two wouldn't seem a likely pair, AI and sustainability, but we have considered the technology through the lens of our five positive themes.

For the full report please click **here**.

UPDATE ON THE PUBLICATION OF PHASE ONE OF OUR INVESTMENT TRUST THEMATIC ENGAGEMENT

Ramón Secades, Responsible Investment Analyst

Source of image: iStock

On 6 September, we published a paper outlining the completion of the first phase of our investment trust thematic engagement and our expectations for investment trust boards. This first repot focused on equity investment trusts and this RI Reel provides a flavour of the content.

The report, which included an introduction by the chief executive of the Association of investment Companies (AIC) was well received, with a number of financial media outlets reporting on it, as well as a broker. It also prompted a lot of requests by investment trusts who were keen to know their ratings. Whilst we are very happy discussing feedback with boards, at this stage, we are not sharing the individual trust ratings. The ratings are there to give a broad indication of the trust's current positioning, and in our view, boards should concentrate on the feedback we have provided in order to meet the best standards of corporate governance and transparent disclosure.

We hope that the report serves to increase the level of engagement not only from boards but also from other investors. Even though it is still early days, we have already heard some encouraging feedback from chairs who seem keen to implement changes following the report.

It has been over a year since the start of phase one of this engagement, and over the next twelve months, we will be looking at engage with our private equity, alternatives, property and infrastructure investment trusts. At which point we will restart the cycle and revisit the equity investment trusts with a focus on those where in our view there is material scope for improvement.

ENCOURAGING THE COMPANIES, WE INVEST IN TO DISCLOSE MORE ENVIRONMENTAL DATA

Ramón Secades, Responsible Investment Analyst

CDP (formerly known as the Carbon Disclosure Project) is a non-profit organisation that operates a global disclosure system for investors, companies, cities, states, and regions to manage their environmental impacts. It was launched in 2000 and originally focused on climate impact disclosure but has since expanded to include deforestation and water security[1].

CDP Non-Disclosure campaign (CDP NDC)

The Non-Disclosure Campaign (NDC)[2] is a yearly collaboration between CDP and investor signatories to engage with companies that have not responded to a CDP disclosure request. Investors are able to participate in two ways:

1) Signing on to the letters CDP sends to the target companies.

2) Leading engagements with the target companies.

In 2022 we participated for the first time as a signatory and this year we have led engagements with nine companies to encourage them to disclose in line with the CDP framework. The companies were in the investment trust and REIT (real estate investment trust) sectors.

We use CDP data in a number of ways; firstly, as part of our investment process, CDP data feed into our proprietary equity ESG dashboards, which the research team uses to monitor our investment universe, and which drive the categorisation of our centrally monitored holdings in line with our clients' responsible investment preferences. We also use CDP data for thematic engagements, such as analysing water usage data. This year, 278 investors signed up to support the campaign, which is an increase on the 260 financial institutions (representing nearly US$30 trillion) for 2022.

We identified nine companies within our centrally monitored universe that had not responded to CDP's submission request. We chose the companies based on the materiality of our holdings, and additionally in most cases, we already had an open dialogue to build on. Following on from CDP's letter to the companies we contacted them to discuss this further.

Outcome

In general, the engagement was a positive one. The purpose of the engagement was the raise awareness of the importance of CDP disclosure. We did not expect companies to disclose in this reporting cycle, especially as it would be their first time making a submission.

A number of the companies have indicated their intention to do so in the next reporting cycle. Several of the companies were grateful for the opportunity to have an open discussion around the value of CDP disclosure from investor's perspective and appreciated the opportunity to ask questions directly of CDP (a representative from CDP joined our engagements). We will continue to engage with our investee companies to monitor those interested in completing CDP disclosure and continue to encourage the adoption of CDP reporting across our holdings.

1 What we do - CDP
2 Non-Disclosure Campaign - CDP

Company	Communication method	Outcome
A	Email exchange	It is currently focusing its efforts on TCFD reporting and will consider CDP in the future, once this has been finalised.
B	Email exchange	It has already initiated its CDP response.
C	Email followed by video call	It will consider a submission in the upcoming reporting year.
D	Email followed by video call	It will consider completing a submission in the future, but it is currently prioritising other projects such as TCFD.
E	Email followed by video call	No clear indication that it will commit to reporting in line with CDP
F	Email exchange	Its focus this year has been on its GRESB score (the global ESG benchmark for real estate) and its net zero plan. The CDP framework is on the agenda for the future.
G	Email exchange	Aggregated submission at the group level.
H	Excluded	We excluded this company from the engagement as it subsequently announced it was winding up
I	Email followed by video call	It will consider a submission in the upcoming reporting year.

RI REELS

Insights into Quilter Cheviot's approach to responsible investment, as well as topical issues.

Thematic Engagement: Investment Trusts

Kirsty Ward, Responsible Investment Analyst; and Ramón Secades, Responsible Investment Analyst

Kirsty and Ramón discuss our latest thematic engagement and our expectations for Investment Trust boards.

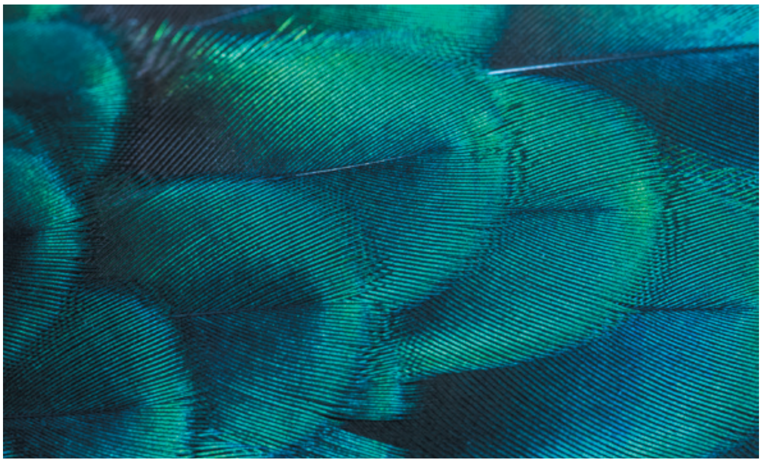
WATCH VLOG

Climate - responsible investment

Kirsty Ward, Responsible Investment Analyst; and Margaret Schmitt, Responsible Investment Analyst

Margaret, who's recently joined the responsible investment team as a climate specialist talks about her role and her main focus.

WATCH VLOG



Climate Assets Funds

Kirsty Ward, Responsible Investment Analyst; Claudia Quiroz, Head of Sustainable Investment

Claudia discusses our Climate Assets Strategy.

WATCH VLOG

Source of images: iStock

OVERVIEW

Overview of our activity across our discretionary holdings at Quilter Cheviot:

Activity	Universe
Voting	Discretionary holdings within the global equity monitored lists where we have voting rights including: • MPS (Managed Portfolio Service) Building Blocks • Climate Assets Balanced Fund and Climate Assets Growth Fund • Quilter Cheviot Global Income and Growth Fund for Charities • Quilter Investors Ethical Fund • AIM Portfolio Service This includes our global equity and investment trust monitored lists; as well as holdings in the AIM Portfolio Service and UK holdings where we own more than 0.2% or £2 million of the market cap. *Additionally, clients are able to instruct voting on their behalf.*
Engagement	• Global equities within the monitored list • Funds held on the centrally monitored list • AIM Portfolio Service holdings • UK holdings where we own more than 0.2% or £2 million of the market cap.
ESG integration	All holdings within the centrally monitored universe of equities, funds and fixed income.

We use the ISS proxy voting service in order to inform our decision making, however we do not automatically implement its recommendations. When we meet a company to discuss governance issues, the research analyst does so alongside the responsible investment team as we are committed to ensuring that responsible investment is integrated within our investment process rather than apart from it. In 2022 we received confirmation that we had retained our signatory status of the FRC's stewardship code. This status was granted on the basis of our 2021 report. In order to maintain our signatory status, we submit a Stewardship Code report to the Financial Reporting Council (FRC) every April. We have successfully maintained our signatory status in 2023.

UK STEWARDSHIP CODE

Where clients wish to vote their holdings in a specific way, we will do so on a reasonable endeavours basis; this applies whether the investment is in the core universe or not, and also to overseas holdings. We have ensured that two clients were able to instruct their votes over the last quarter.

For information regarding our approach to responsible investment, including our response to the UK Stewardship Code and our voting principles, as well as more granular detail on how we voted at each meeting please visit our website [Responsible Investment | Quilter Cheviot].

RESPONSIBLE INVESTMENT AT QUILTER CHEVIOT

Active ownership and ESG integration – for discretionary clients
We vote and engage with companies and fund managers on environmental, social and governance (ESG) matters. Integrating ESG considerations into our investment process can have direct and indirect positive outcomes on the investments we make on behalf of our clients.

We take a more targeted approach for clients that want their portfolios to reflect their specific interests or preferences.

A Direct Equity Approach* - DPS Focused
The strategies harness Quilter Cheviot's research and responsible investment process, as well as data from external providers, to implement ESG factor screening on a positive and negative basis. To ensure more emphasis is placed on ESG risks beyond the firm-wide approach to active ownership and ESG integration which forms the basis of the Aware categorisation.

A funds based approach – Positive Change
A pragmatic approach that combines funds that invest with a sustainability focus or for impact, with funds managed by leading responsible investment practitioners. Meaningful engagement by fund houses with company management is prioritised over formal exclusions on the basis that engagement can encourage change where it is needed most.

Sustainable Investment – The Climate Assets Funds and Strategy**
Investing in the growth markets of sustainability and environmental technologies, with a strong underpinning of ethical values. The strategy is fossil fuel free and invests in global equities, fixed interest and alternative investments. Five positive investment themes are at the heart of the stock selection: low carbon energy, food, health, resource management and water.

Ethical And Values Oriented Investment – Client Specific
This is incorporated on an individual client basis, informed by their specific ethical preferences and values. These will vary from client to client and will focus on industry groups, industries or individual companies.

* For UK, North American and European equity holdings
** Climate Assets Balanced Fund and Climate Assets Growth Fund.

GLOSSARY

Active ownership: This is where investors actively use voting and engagement to influence the management of companies with respect to environmental, social or governance factors. Similar principles are also used by investors in other asset classes such as fixed income, private equity or property. This will also involve active participation in industry and peer group collaborative initiatives.

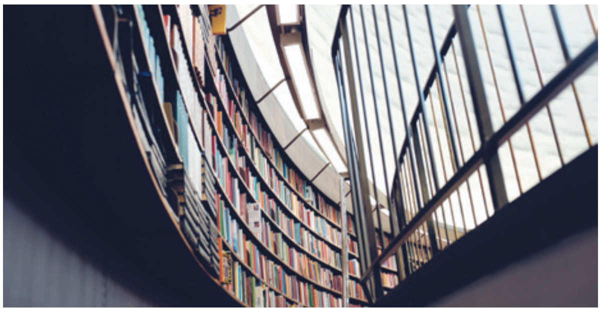
Clawback (and malus): Incentive plans should include provisions that allow the company, in specified circumstances, to ensure that a recipient:

- forfeits all or part of a bonus or long-term incentive award before it has vested and been paid – this is called 'malus' and/or
- pays back sums already paid – this is called 'clawback'.

Disapplication of pre-emption rights: Existing shareholders do not have first refusal on new shares and therefore their holdings will be diluted.

Engagement: Investors enter into purposeful dialogue with companies, funds, industry bodies, and governments to discuss environmental, social, and governance related issues in order to gain more information or to encourage and achieve change. This may be in collaboration with other investors.

ESG (Environmental, Social, and Governance): The risks and opportunities related to ESG issues. **Environmental** - relating to the environment such as resource, water and land use, biodiversity, pollution, atmospheric emissions, climate change, and waste. **Social** - relating to the relationship between companies and people, such as their employees, suppliers, customers, and communities. Examples of social issues of interest to investors include health and safety, labour standards, supply-chain management, and consumer protection. **Governance** - relating to the governance of an organisation, also referred to as corporate governance. Examples include board composition, executive remuneration, internal controls, and balancing the interests of all stakeholders.



Long-term incentive plan (LTIP): A type of executive compensation that pays out usually in the form of shares company. The reward is linked to performance metrics and the pay-out will be calibrated in line with the achievement of these. The quantum of the pay-out is linked to multiples of salary.

Net zero: Achieved when anthropogenic emissions of greenhouse gases to the atmosphere are balanced by anthropogenic removals over a specified period. Where multiple greenhouse gases are involved, the quantification of net zero emissions depends on the climate metric chosen to compare emissions of different gases (such as global warming potential, global temperature change potential, and others, as well as the chosen time horizon). *Definition sourced from the IPCC.*

NEDs (Non-Executive Directors): These are directors who act in advisory capacity only, however they should hold the executive directors to account. They are not employees of the company, however they are paid a fee for their services.

Over-boarded: Where non-executive directors are deemed to have a potentially excessive number of non-executive positions and the concern is whether they have sufficient time to contribute to the board of the company.

Pre-emption right: These give shareholders first refusal when a company is issuing shares. Premium listing: This was previously known as a primary listing for the London Stock Exchange. A company with a premium listing is expected to meet the UK's highest standards of regulation and corporate governance.

Principles of Responsible Investment (PRI): The world's leading voluntary initiative on responsible investment. Launched in 2006 it now has thousands of investor signatories globally who commit to adopt six principles for responsible investment and report against these annually. Although voluntary and investor-led the PRI is supported by the United Nations.

Proxy voting: Where a shareholder delegates their voting rights to be exercised on their behalf. Often voting rights are delegated to investment managers who exercise votes on investors' behalf. Votes are used to express shareholder opinions to company management.

Responsible investment: A strategy and practice to incorporate ESG factors in investment decisions and active ownership. *Definition sourced from the PRI.*

Restricted share plan: Some companies (and indeed investors) prefer the use of these plans as opposed to LTIPs (see above). The idea is that this type of plan encourages long-term behaviours and does not have the same use of targets that you would see within an LTIP. Therefore, it is expected that companies which adopt such an approach award a lower amount than would be seen under an LTIP which has a variable structure dependent on performance outcomes.

SID (Senior Independent Director): The SID position is taken by an independent NED. The SID often plays a critical role in ensuring communication channels are open between the board and shareholders.

Stewardship: The responsible allocation, management, and oversight of capital to create long-term value for investors and beneficiaries leading to sustainable benefits for the economy, the environment, and society. *Definition sourced from the Financial Reporting Council (FRC).*

TCFD: Acronym that stands for the Task Force on Climate-related Financial Disclosures. The Financial Stability Board created the TCFD to improve and increase reporting of climate-related financial information. Regulators are adopting TCFD and, in particular, the UK regulator (FCA) is requiring firms to apply these disclosure rules.

Tender – bid waiver: This is the right to waive the requirement to make a general offer under Rule 9 of the Takeover Code.

Total shareholder return (TSR): Is a measure of the performance of a company's shares; it combines share price appreciation and dividends paid to show the total return to the shareholder expressed as an annualised percentage.

UN Sustainable Development Goals (SDGs): The 2030 Agenda for Sustainable Development adopted by all United Nations Member States in 2015, provides a shared blueprint for peace and prosperity for people and the planet, now and into the future. At its heart are the 17 UN Sustainable Development Goals (SDGs), which are an urgent call for action by all countries - developed and developing - in a global partnership. They recognise that ending poverty and other deprivations must go hand-in-hand with strategies that improve health and education, reduce inequality, and spur economic growth - all while tackling climate change and working to preserve our oceans and forests. *Definition sourced from the UN.*

Voting Rights: Shares in listed companies typically come with specific voting rights which can be exercised at the company's annual general meeting or extraordinary meetings. They can be used as a means of expressing the opinion of the shareholder about how the company is being managed. This is also referred to as proxy voting when voting rights are delegated, for example to investment managers who exercise voting rights on an investor's behalf.

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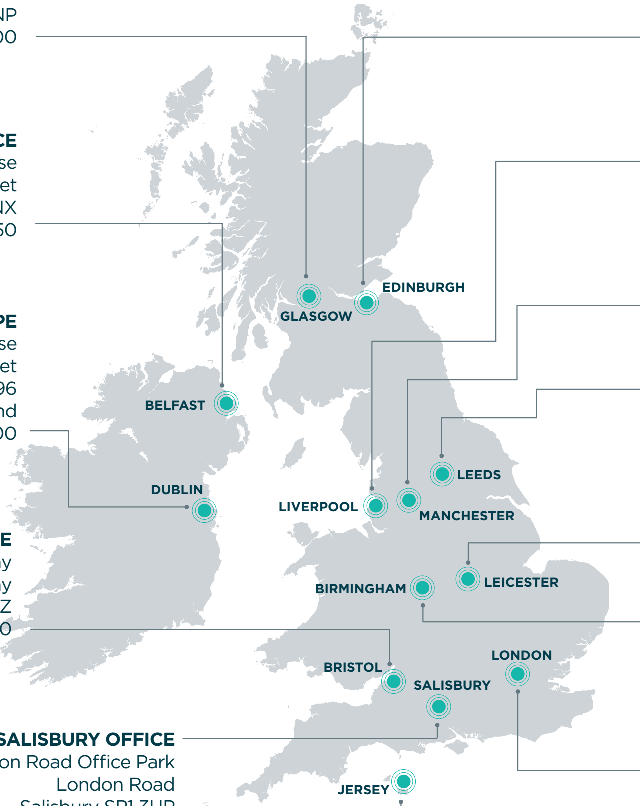

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