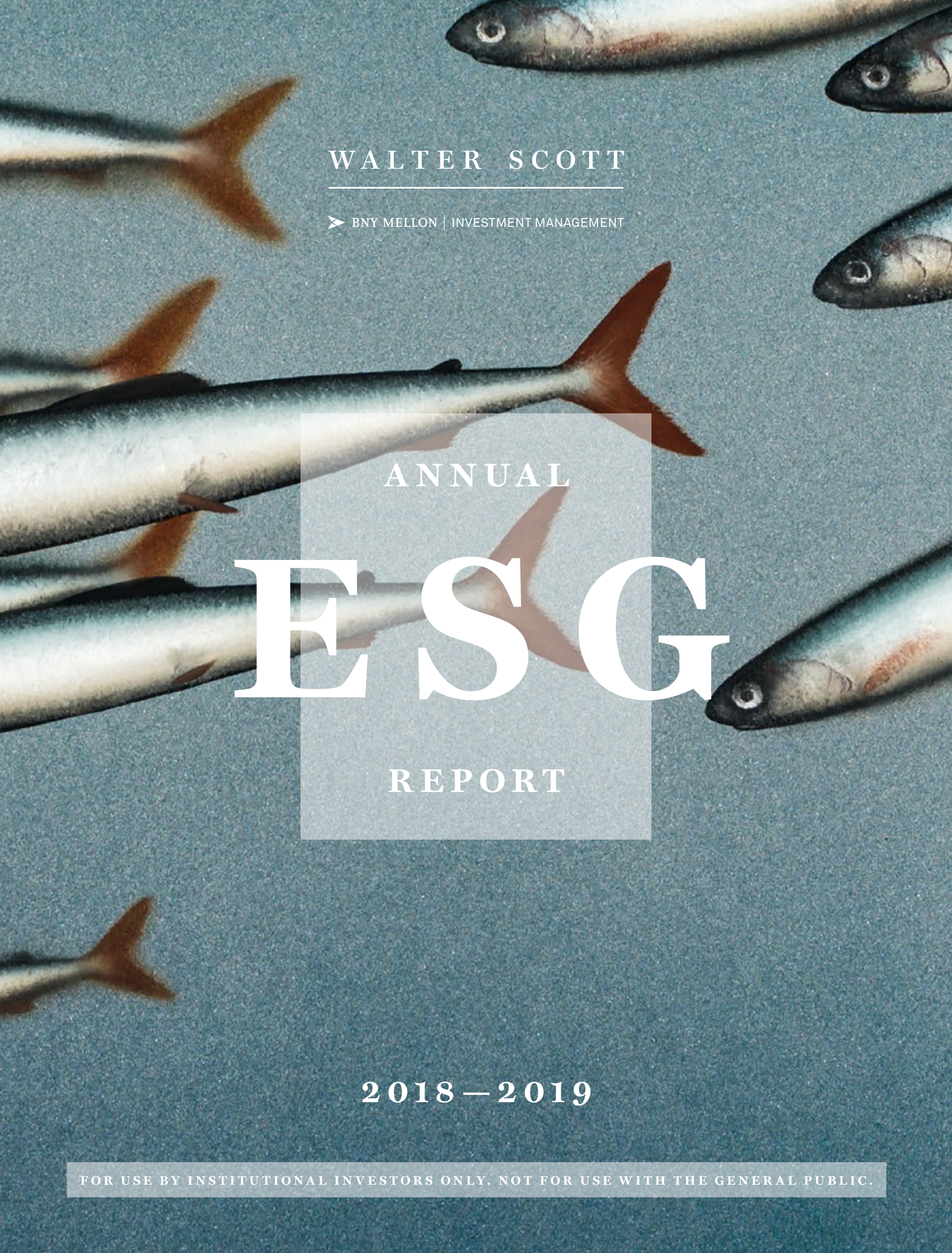


WALTER SCOTT

BNY MELLON | INVESTMENT MANAGEMENT

ANNUAL ESG REPORT

2018–2019

Stock Examples – Companies referred to in this report have been chosen for illustrative purposes only to demonstrate our ESG Investment process and are not intended to be an indication of performance. This information should not be considered a recommendation to buy or sell any particular security. There is no assurance that any securities discussed herein will feature in any future strategy run by us. Any examples discussed are provided purely to help illustrate our investment style or, are given in the context of the theme being explored. The securities discussed do not represent an entire portfolio and in the aggregate may represent only a small percentage of a strategy's holdings.

OUR COMMITMENT

Consideration of a company's Environmental, Social and Governance (ESG) factors is integral to our long-term investment approach. The investment implications that flow from ESG opportunities and challenges are as numerous as they are varied. This inaugural annual report reflects our ambition to share our thinking, and our work, around ESG matters, where the pace of evolution is perhaps only surpassed by growing importance. Our goal, in the pages that follow, has been to evidence the work that we do and demonstrate our commitment through our consistent and carefully considered approach.

> *"Our goal, in the pages that follow, has been to evidence the work that we do and demonstrate our commitment through our consistent and carefully considered approach."*

Engaging with companies is central to our investment process. Through our conversations with some of the world's leading corporations we recognise the challenges they face in pursuing change, as well as documenting it. And through our research, and the discussion amongst the team that is so central to our approach, we constantly strive to assess all the attributes that make a company a good investment, or not. Where should a company be applauded for its efforts across E, S and G and where is improvement required? How do we verify ESG corporate reporting and how do we compare the multitude of metrics applied in that reporting?

These are all frequent topics of discussion – and often spirited debate! – and we are always happy to share those conversations.

This is an area where there are few definitive answers and constant change. Engagement and conversation benefits us all.

Best wishes,

Jane Henderson, Managing Director

CONTENTS

ABOUT US

RESPONSIBLE

We are entrusted to invest on behalf of our clients around the world over a long-term investment horizon. In that context, it is inconceivable that we would not invest in a responsible way. We look for companies that meet our defined investment criteria. This places as much importance on management talent, operational efficiency, rigour and best practice, governance and culture as it does financial metrics.

INTEGRATED

Every member of the Research team is responsible for understanding how companies' sustainability credentials stack up. There is no separate ESG team. This is deliberate. These factors are too important. They are integral to our investment analysis and decision-making, not an adjunct.

CONSIDERED

With a long-term investment horizon and a highly considered, and reflective, investment process, we take time to consider every company on its merits. We don't apply broad brush rules or impose a myriad of exclusions. Instead, we collectively consider the context and make informed, and collective, judgements.

INQUISITIVE

Our research is multi-faceted. From desk-based research to engagement with management, visits to factories or shops, discussions with, and analysis of, suppliers or competitors, we must build a comprehensive picture of any company, and then challenge it.

ENGAGED

Engagement is what we do every day. It might have a specific goal, but equally there need not be a discrete objective.

We expect every company we invest in to engage on issues of sustainability. We focus on getting to know and understand every business and its industry in order to seek out the issues that matter most for the sustainability of those businesses and those industries. If a business is not well positioned, with our long-term investment horizon, it is un-investable. In this way, we take a bespoke approach for each company and industry in order to focus on the issues that matter most. We avoid box ticking.

OUR APPROACH

INTEGRATED AND INTEGRAL

Consideration of the ESG opportunities and challenges relevant and material to any investment company must be integral to our research.

This is based on the straightforward and simple premise that only by striving towards appropriate standards of corporate governance, respect for the environment and respect for all stakeholders embedded in a company's culture as well as its operations, will a company prosper over the long term.

ESG considerations can never be an aside to any investment discussion. Because of this, we do not delegate responsibility and oversight to a separate team. ESG issues are the responsibility of each member of our Research team.

With our focus on 'bottom-up' investment, our investment process is deliberately structured to discard companies where ethical, governance, environmental or social standards are deemed to put the achievement of the long-term portfolio return targets at risk.

In researching any company, regardless of geography or sector, we apply the same analytical framework. That framework forms an important part of the overall research process and is based on seven areas of investigation.

1 — Company

2 — Control of Destiny

3 — Integrity

4 — Characteristics

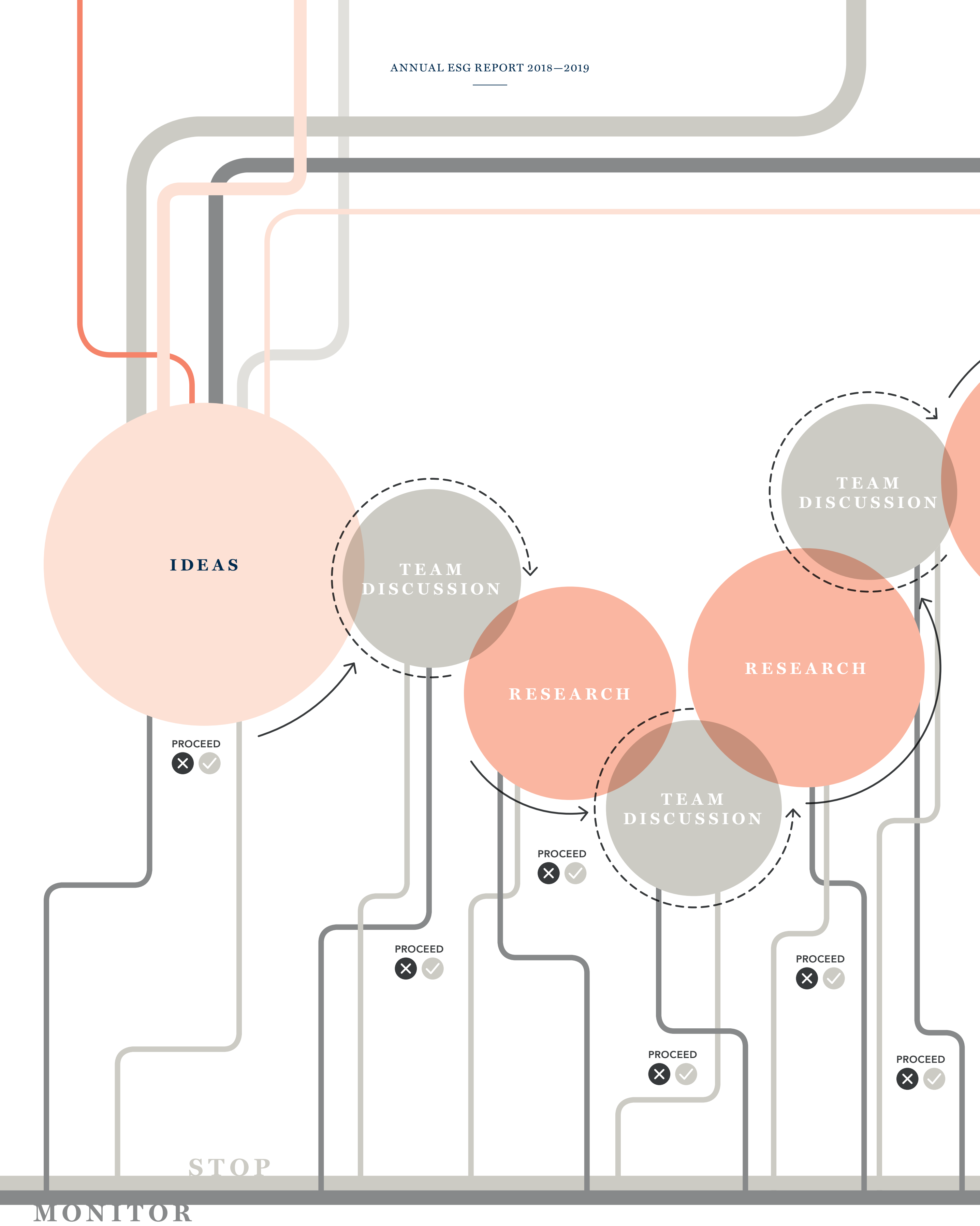
5 — Financial Profile

6 — Management & Board

7 — Valuation/Trading

It may be appropriate to consider ESG factors across almost any aspect of a company's business and therefore all seven areas.

"ESG considerations can never be an aside to any investment discussion. Because of this, ESG issues are the responsibility of each member of our Research team."


IDEAS
TEAM DISCUSSION
RESEARCH
RESEARCH
TEAM DISCUSSION
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PROCEED
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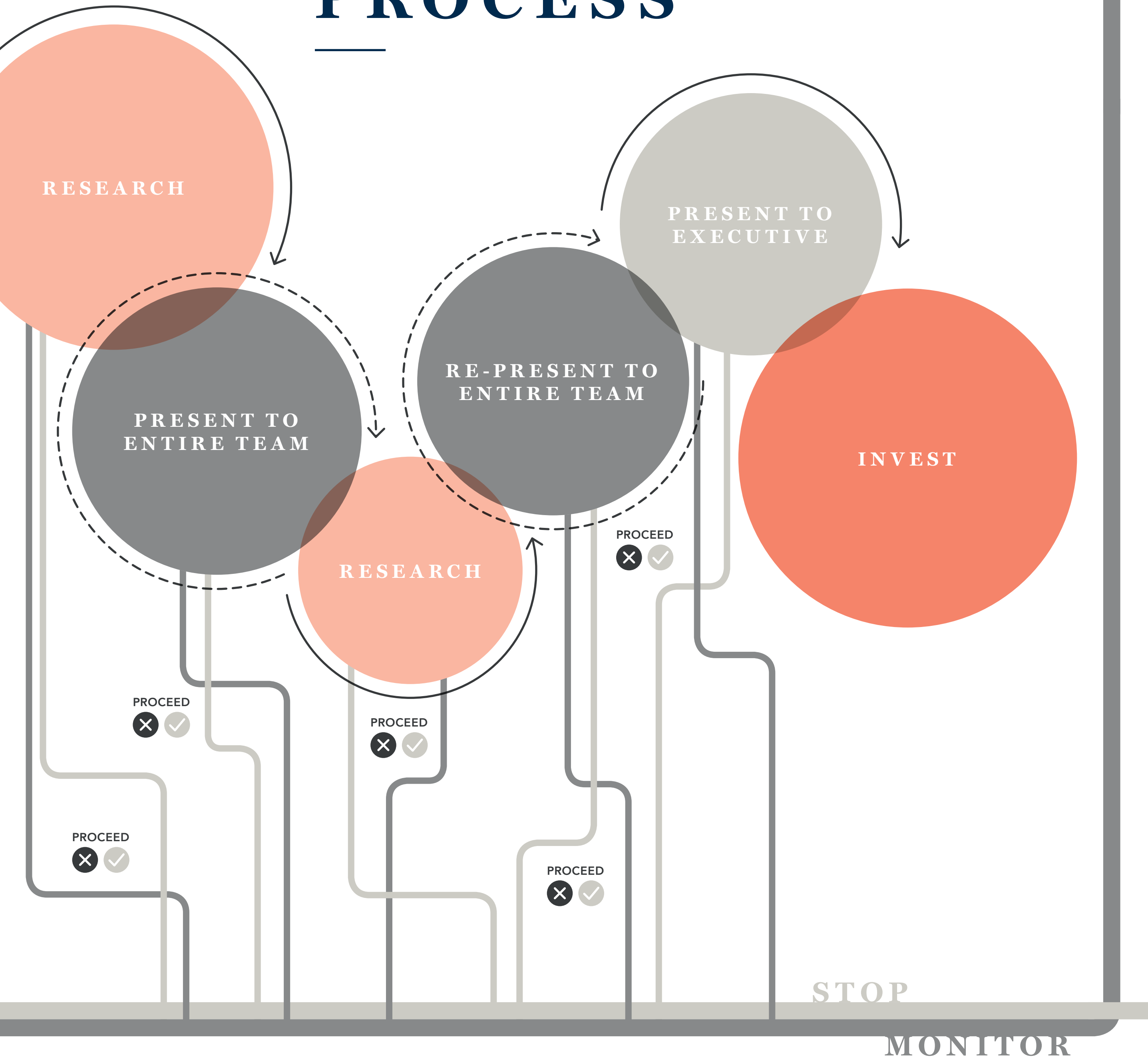
STOP
MONITOR

THE INVESTMENT PROCESS



IDEAS

Does the company operate in any area where environmental and/or social impacts are often negative?

Is there evidence of a healthy, supportive corporate culture that will sustain long-term growth?

Is there evidence of strong employee retention?

Is there evidence of robust supply chain transparency, oversight and partnership?

Are there any ESG practices that create enduring competitive advantage?

Are there any particular environmental challenges?

Is the company well-positioned to improve its environmental footprint and/or address any regulatory change?

Is there anything unusual in the ownership or governance structure?

Past scandal or controversy?

Are the company's accounts qualified in any way?

DISCUSSION

We've heard the case for growth, but what are the risks to that case?

Are there identified weaknesses across E, S or G that might derail that growth?

What are the company's ESG priorities?

What is the day-to-day influence of the founder/majority shareholder?

Has the company been forthcoming in providing information?

Can we meet the CEO?

ESG QUESTIONS & CONSIDERATIONS*

**This is not an exhaustive list of our ESG questions and considerations but all are amongst the areas frequently discussed and researched and are intended to demonstrate the breadth of our approach.*

THE INVESTMENT PROCESS

RESEARCH

What are the standout strengths, anomalies or oddities in the financial reports and accompanying sustainability reporting?

Is there anything of note from a review of qualifications and experience across the management team and board?

Cross reference with Sustainalytics controversies report, ISS voting reports and MSCI ESG research ratings? Membership of relevant ESG indices? Commitment to UN SDGs and/or any other social or environmental industry code or body?

How do environmental metrics compare with a relevant peer group?

How does the company approach supplier relations? Is the company a signatory to any industry agreement on appropriate sourcing or human rights protection? Does the company have its own agreements with suppliers to ensure proper oversight and underpin effective monitoring?

Review of critical events for the company, and its industry – how did the company respond to those key events or incidents?

Are the company's stated sustainability goals or targets credible and ambitious?

PRESENTATION

Does this company have the strength of management, culture and operational standards to succeed over the long term, and the financial security to protect and advance all those criteria?

Are we confident that the long-term interests of shareholders are aligned with those of management?

Are there any challenges within the business in its environmental output or social standards, or within its governance?

Do we believe the company has the commitment, knowledge and people to strive and to improve?

Do we have sufficient trust and confidence in the long-term sustainability of this business to invest today?

FROM THE RESEARCH TEAM

With an integrated approach to ESG, every member of the Research team is responsible for incorporating ESG factors into their analysis, be that in building an investment case for a potential new idea or in ongoing monitoring and stress-testing of current investments. Here, team members share thoughts on particular meetings, events or research projects over the past year that stand out to them, be that as examples of good or questionable practices.

E S G

ASCENDAS REIT — THE REAL DEAL

Fraser Fox

Ascendas REIT (A-REIT) is Singapore's first and largest listed business and industrial Real Estate Investment Trust. It owns a portfolio of high quality properties and has a well-diversified roster of tenants, focused on high-value added areas including technology, scientific research, and logistics. The trust listed in 2002 and in our opinion has a strong track record both in terms of financial performance and governance.

I began researching the company in early 2019. I was already familiar with the economic and regulatory landscape in Singapore but investigating a REIT raised a whole new set of questions to explore on top of our usual research process.

REITs have somewhat unusual structures and A-REIT is no exception. It has a sponsor, Ascendas-Singbridge, a REIT manager and property manager (both wholly-owned subsidiaries of the sponsor) and an independent trustee to protect the interests of minority unitholders. Temasek, the Singaporean sovereign wealth fund, ultimately sits at the top of the structure.

To further complicate matters, as my research continued, Ascendas-Singbridge was acquired by CapitaLand (with Temasek remaining the largest shareholder of the combined entity).

"We had to be confident that structures were in place to prevent minority unitholders from being disadvantaged."

I knew that the team would need to become comfortable with the trust's governance structures and the interplay between the various entities. The support of a strong sponsor like Ascendas-Singbridge/CapitaLand can be hugely beneficial for a REIT but we had to be confident that structures were in place to prevent minority unitholders from being disadvantaged, particularly when assets were being sold by the sponsor into the trust. This is normal practice in this arena but it is not without potential pitfalls.

The REIT sector is regulated by the Monetary Authority of Singapore (MAS), which I have developed a good understanding of having spent a lot of time researching Singaporean banks over the years. That provided a reassuring starting point from which to assess governance.

On each of the areas I investigated – the terms of the trust deed, AGM rules, board quality and independence, manager performance fee structures, requirements for independent valuations and minority votes on significant related party transactions – I was satisfied the interests of minority unitholders are aligned with those of the sponsor and manager. Despite its apparent complexity, A-REIT has a robust governance structure, falls under the remit of a respected regulator and benefits from the 'halo effect' of its relationship with Temasek.

E S G

D&L INDUSTRIES – UNDERSTANDING A CONTROVERSIAL INGREDIENT

Matthew Gerlach

D&L Industries is a leading manufacturer of food ingredients and chemicals in the Philippines. The company supplies multinational companies as well as local companies which gives it exposure to meaningful growth domestically and fast-growing consumption patterns across South-East Asia.

We have specifically engaged with the company on a number of occasions on the subject of its supply practices. The company's second largest raw material is palm oil, the most widely used multipurpose oil but where production has led to extensive deforestation. As part of our due diligence, this was clearly an important issue for us to consider, and one that merited specific conversations and investigation.

Over the past three years we have held seven meetings with the company and travelled to its headquarters in the Philippines to meet with the CEO, Alvin Lao.

"As well as being a signee of the RSPO (Roundtable for Sustainable Palm Oil), Lao explained that the company intends to have full traceability and sustainability of supply and suppliers by the end of 2019."

As well as being a signee of the RSPO (Roundtable for Sustainable Palm Oil), Lao explained that the company intends to have full traceability and sustainability of supply and suppliers by the end of 2019. The company appears on track to meet that goal whilst it has also developed a number of ingredients to transition customers to zero palm oil if they choose, an effort that it has expanded to its packaging businesses with the use of biodegradable plastic.

Additionally, the company counts many large multinationals, including Unilever and Nestlé, among its customers. In assessing D&L, seeing these company names on its client list gave us an additional level of confidence because having also analysed these companies we know that they have stringent requirements when it comes to ensuring the integrity of their own supply chains.

All these points were critical in convincing my colleagues as to the sustainability of long-term growth for this business as well as ensuring sufficient understanding of the environmental and reputational risks associated with palm oil.

Of course, there is room for improvement. The Philippines is significantly behind the developed world in its adoption of stricter environmental standards, so management's proactiveness on these issues is well received. Some of the company's smaller local customers may not have the financial depth to afford fully certified palm oil and D&L's internal efforts are one way to address this. We enjoy a strong and open dialogue with D&L. Through understanding the company's commitment first-hand we have gained confidence in the company's approach to this controversial ingredient and to environmental damage.

E S G

INTUITIVE SURGICAL – MORE THAN JUST INTUITION

Alex Torrens

Our research on Intuitive Surgical underlines the value we attach to our own proprietary research. It demonstrates our willingness to back our own research over third party ratings. Contrary to a number of rating agencies, we are assured of Intuitive's positive social contribution and through our ongoing engagement, we are equally assured of the company's commitment to improve upon its ESG standards, and reporting.

Based in California, Intuitive Surgical Inc is a global leader in robot-assisted minimally invasive surgery (MIS). Roughly one third of its revenues comes from the sale of robotic systems with the remainder from recurring sales of instruments and accessories, and service contracts.

To date, Intuitive's products have been used in around six million surgical procedures. There is now compelling evidence that the clinical outcomes are superior to traditional surgery, cutting recovery times for operations from weeks to a matter of days, and reducing re-admission rates. Patients, as well as hospitals, benefit from fewer days in hospital following a surgical procedure. Yet, in our opinion, the company has been misrepresented and misunderstood by mainstream media and some quarters of the investment community. In 2013, it fell victim to short-sellers when Citron Research published a damaging report about the company entitled 'Angel with Broken Wings'.

Intuitive had been under the Research team's watch for several years. We saw Intuitive as a world-class company with a great technology offering, a strong balance sheet and delivering real benefits to patients, surgeons and hospitals.

"We have continued to engage with the company and we have made a number of suggestions on how they might improve ESG reporting in particular."

In 2013 the Citron report was one of a confluence of factors that drove the share price down by a third and prompted us to revisit our research. Throughout our initial research and in ongoing work we had found the company to be responsive and engaged, and at this juncture, the company continued to be open and transparent, reassuringly so.

One of Citron's claims was that complaints about Intuitive' s procedures were increasing. Intuitive did not hide, were happy to engage and countered those claims with compelling evidence to the contrary.

More recently MSCI awarded the company its lowest possible sustainability rating and again we re-assessed our own research and engaged extensively with the company on particular points. Whilst we were confident in our research and our conclusions, which were very much at odds with MSCI's ESG rating, it was important for us to hear the company's case.

Since then, we have continued to engage with the company and we have made a number of suggestions on how they might improve ESG reporting in particular. Those suggestions have sometimes been unsolicited and on other occasions have followed a specific request from the company's investor relations team. All this has added to our conviction in our own research on the company, whilst also helping the company improve its ongoing reporting, moving away from a simply reactive stance.

Intuitive's procedures have continued to grow year-over-year. For us, that is a reliable and trustworthy indicator that patients, surgeons and hospitals agree with our view of the company and find real value in what the company does every day.

> *"Kao has also been actively investing in the search for sustainable alternatives to palm oil, with work going into algae as a substitute in detergents and shampoos."*

E S G

KAO – INNOVATIVE ENVIRONMENTAL RESPONSIBILITY

Alan Edington

KAO is a Japanese consumer goods company offering products including detergents, cosmetics and shampoos. KAO also has a chemicals arm that gives the company the advantage of using its own innovations to differentiate its products. It has established a market-leading position in part by demonstrating a clear understanding of its wider responsibilities to society.

Being vertically integrated enables KAO to apply R&D discoveries across its product lines. This includes a commitment to find more sustainable products and reduce the environmental impact of its activities.

The company's approach to sustainability reaches all through the business. By way of a simple example, through changing product packaging and adjusting the way it packs its trucks, the company has materially reduced the number of trips it has to make to deliver the same volume of goods, reducing emissions and making associated cost savings. For some time Kao has also been actively investing in the search for sustainable alternatives to palm oil, with work going into algae as a substitute in detergents and shampoos.

Another important and unique innovation has been the development of a new dispenser container. Dispenser containers for shampoos often have a complicated structure that use multiple types of plastic, one plastic for the bottle and another for the spout from which to dispense the liquid. The component parts have to be recycled separately and in some cases, the spout cannot be recycled.

KAO has developed a form of dispenser using only one type of recyclable plastic, making the job of recycling much easier. The dispenser is also different in its structure. It comprises two film sachets that sit one inside the other separated by a layer of air, which maintains the integrity of the structure and ensures it remains upright. These bottles use one tenth of the normal volume of plastic and are a genuine innovation with strong customer appeal. Through a culture of innovation and investment in R&D, KAO has become highly differentiated from its rivals, thereby preserving profit margins. The company's success dates back to its foundation in 1887. Today, its products appeal to a new generation of consumers demanding sustainable products that are created, produced and distributed in a responsible manner.

E S G

TJX – ENSURING SUSTAINABLE SUPPLY

Paul Loudon

TJX is one of the largest apparel retailers in the world. Its business model is built on procuring excess inventory from more than 20,000 vendors across the world, and delivering that to its 4,300+ stores in a flexible, dynamic and timely manner.

As a sustainable, global apparel company with a significant proportion of its products sourced from emerging markets, the company appreciates just how important it is to assess the integrity of its supply chain. In order to do so it calls upon each of its 21,000+ vendors to sign a comprehensive Vendor Code of Conduct and it regularly audits the vendors to ensure compliance.

TJX sees the long-term value of having a robust approach to sustainability. Or put another way, the company understands the reputational damage that can come from not having a clear policy and thorough processes. Of course, we must trust management, but we don't just take any management team at its word or merely accept a glossy ESG brochure full of aspirational commitments.

As part of ongoing due diligence and research on TJX, I visited the factory of a direct supplier to the company in Guangzhou where some of the company's exclusive merchandise is produced. This was an opportunity to assess first-hand how conditions are in the TJX supply chain. I was introduced to a number of

"We must trust management, but we don't just take any management team at its word or merely accept a glossy ESG brochure full of aspirational commitments."

employees on the factory floor and so far as possible, gained a direct perspective of how the vendor operates and how it treats and retains its staff. Encouragingly the factory was impressive, the working conditions were excellent, and the employee feedback seemed positive.

We have a very strong and regular dialogue with the company. We have met the CEO and CFO on dozens of occasions, both at the company headquarters outside Boston and in Edinburgh. This long-standing history of engagement ensures the key messages are consistent, and that we can hold the company to account regarding sustainability commitments.

"We communicated our concerns and the productive dialogue that followed further demonstrated the value in direct and ongoing engagement."

E S G

WHITBREAD — PUSHING FOR CHANGE

Alan Lander

When Whitbread announced the spin-off of its Costa Coffee arm in April 2018 our message to the board was clear; we failed to see the value that management claimed would be realised. Whilst not entirely convinced by the case for the demerger, we felt a trade sale might get closer to a more appropriate arrangement, and price.

Attached to those initial plans were proposed changes to management remuneration that we also felt were inappropriate. Again, we communicated our concerns and the productive dialogue that followed further demonstrated the value in direct and ongoing engagement.

The management team's revised remuneration plan included a long-term incentive plan (LTIP) structure, where half of the pay-out was based purely on execution milestones related to the spin-off, whether it created value or not. We felt this was excessive and suggested that they re-jigged the pay plan so that it demonstrated better alignment with stakeholders.

Our relationship with the board of Whitbread and in particular the chairman, Adam Crozier, has always been a constructive one. We have established regular dialogue with the company over the years and on several occasions management

"The announcement of the proposed spin-off brought interested bidders to the table and four months later the business was sold to Coca-Cola for £3.9bn in cash, a higher price than we had anticipated."

have expressed their thanks to us for our thoughts and feedback. Placing value in our long-term strategic approach our views are listened to. In fact, during the events of 2018 they saw us as a very good antidote to the activist shareholder group led by Elliott Capital Advisors that had pushed for the original demerger.

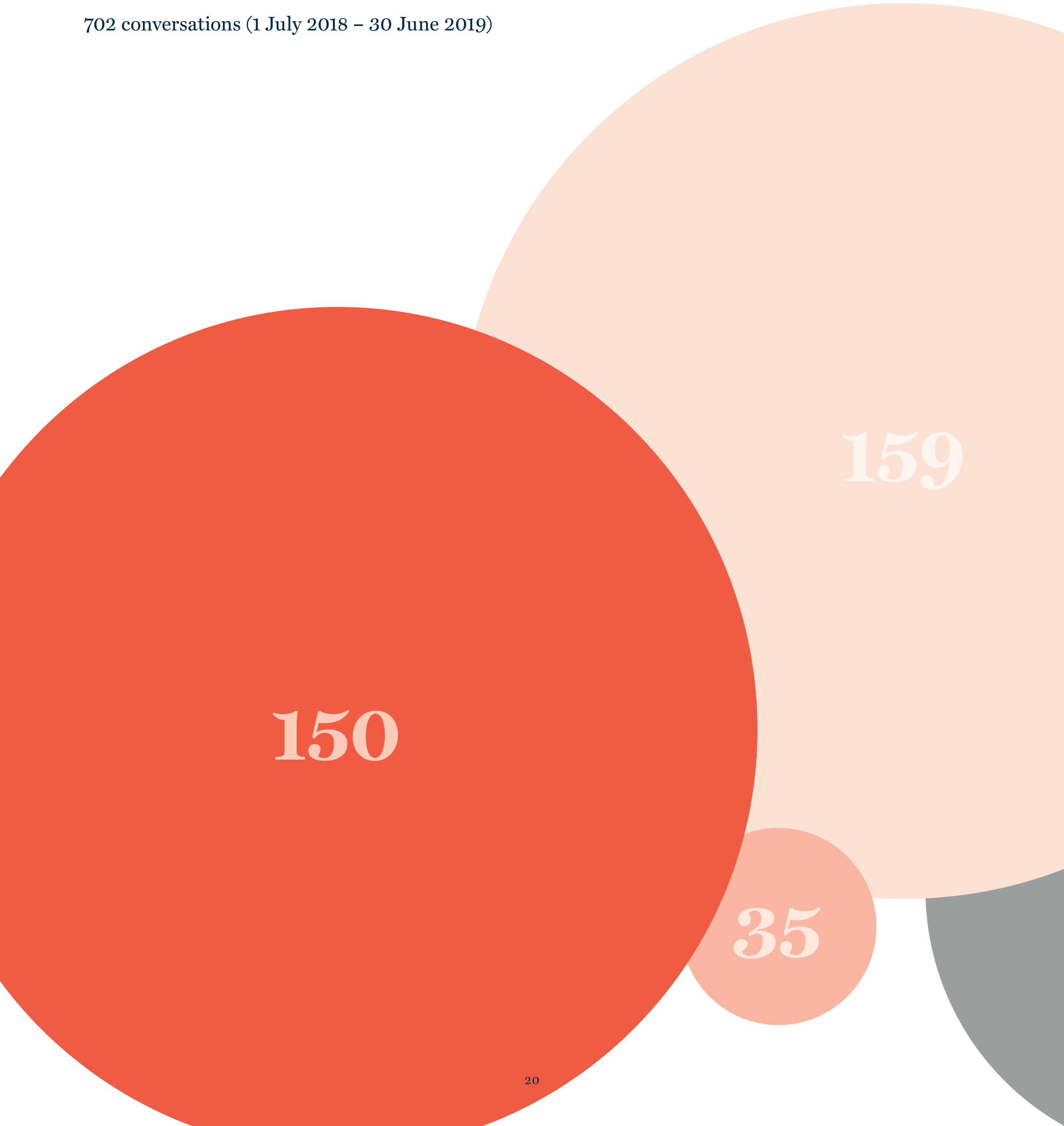
The company's remuneration committee returned with a revised plan which better aligned the interests of shareholders with those of the company's management team. Under the new compensation structure, part of the LTIP was now based on the company's total shareholder return (TSR) in relation to a basket of listed leisure and retail companies.

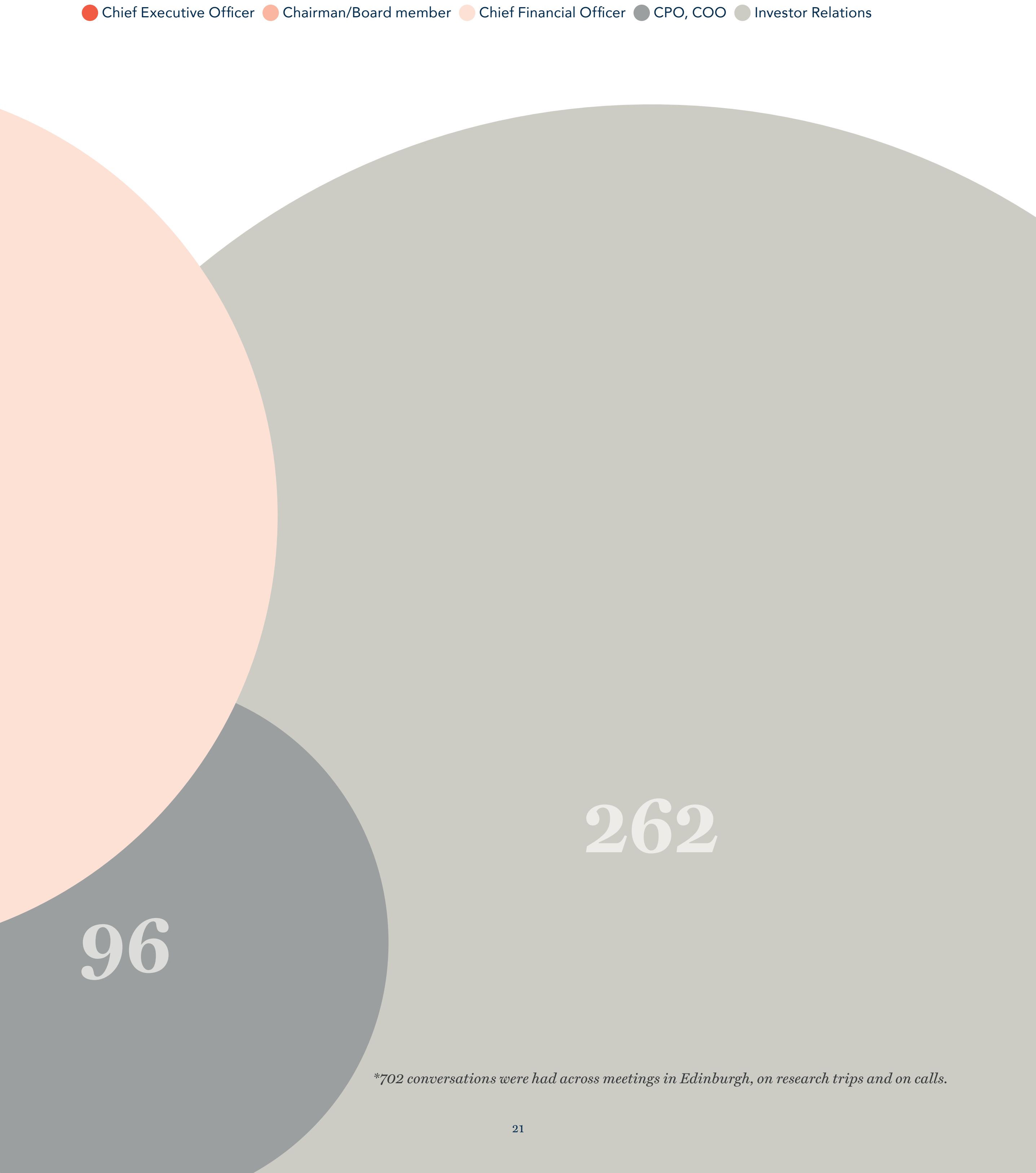
As events unfolded it transpired that this new arrangement was one that benefited both management and stakeholders. The announcement of the proposed spin-off brought interested bidders to the table and four months later the business was sold to Coca-Cola for £3.9bn in cash, a higher price than we had anticipated.

Our approach to engagement is almost always direct and almost always done without fanfare. In this case our approach worked.

COMPANY MEETINGS*

702 conversations (1 July 2018 – 30 June 2019)





**702 conversations were had across meetings in Edinburgh, on research trips and on calls.*

ENGAGEMENT

Engagement with companies is something in which we place great value. It is a critical part of our company research.

Before making any investment, we must be convinced of the merits of the company in question. That demands robust research. It also benefits from dialogue with management.

We must listen to management, probe and then reach our own judgement. Engagement, to us, is not just accepting well-rehearsed corporate messages but quizzing management to understand the particular strengths and vulnerabilities of a business, and the basis for its long-term strategy.

As long-term investors, engagement is also about developing effective lines of communication as we monitor and assess a holding and as we also proactively reach out to raise concerns or encourage change. We look to collaborate with management to the benefit of all and never hesitate to put our views forward on strategic steps, capital allocation, governance or standards.

CALENDAR OF ENGAGEMENT

Over the 12 months from 1 July 2018, the team conducted 702 conversations in Edinburgh and around the world with companies held within portfolios, or their competitors, as well as potential investment ideas. 275 of those meetings included specific or detailed discussion on an ESG matter.

The extracts below, taken directly from the Research team's internal meeting notes, hopefully give a flavour of the range of topics discussed.

Q2 2019

Alphabet
E S G

We met with the chief financial officer of Google's parent company, Alphabet. During our meeting, we spent considerable time discussing the reputational and operational challenges facing the company. These include shareholder misgivings around governance, and employee discontent about conditions and treatment, as well high-profile concerns around privacy and unsavoury online content. To some extent, the company's position at the forefront of a rapidly evolving industry makes some of these challenges unavoidable. However, management could do much more to address the concerns of stakeholders; a view we expressed during our meeting.

We will continue to engage with Alphabet and will use our access to senior management to encourage improvement. For now, the company, its culture and its attitude towards stakeholders remains under close scrutiny.

EOG Resources

E S G

We enjoyed a timely and insightful meeting with the CEO and chief IT officer of Houston-based oil & gas company EOG Resources. This meeting was an opportunity for management to update us on medium-term priorities in the context of the outlook for global oil supply and demand, as well as the company's sustainability agenda.

EOG's disclosure has improved significantly in the last two years and its second sustainability report should include new scientific-based targets for reducing methane intensity. By 2020, these targets will be linked to executive compensation. Work is also ongoing to provide scenario analysis for the long-term sustainability and value of EOG's business in line with the Paris climate agreement framework. This is all encouraging progress.

SM Investments

E S G

Evidencing ESG considerations might not yet be as established among emerging market companies as they are with many of their developed market counterparts; however, change is underway. Potential investment candidate SM Investment, the Philippines conglomerate, is an excellent case in point. It was the first company in the Philippines to be certified by the Global Reporting Initiative and it is a signatory to the UN Global Compact. The Sy family, which is a majority shareholder, is a genuine advocate of ESG and believes ESG principles very often make sound business sense.

Our meeting was also an opportunity to quiz the company on a recent merger and what it meant for minority shareholders. The rationale given was reassuring and highlighted the family's commitment to aligning its interests with stakeholders.

Q1 2019

Ambev

E S G

This was a very useful meeting with this Latin American brewer, which, despite a tough few years, is an exceptionally well run and efficient company. Ambev sports amongst the highest returns in the global brewing industry, in our view, and this leadership extends to its sustainability credentials. More than R$1 billion has been invested in sustainability projects in Brazil in the last five years, addressing eight of the United Nations Sustainable Development Goals.

By the nature of its business, water usage is substantial but numerous initiatives are underway to improve the sustainability of this vital input. The water used to produce one litre of beer has declined from over three litres to around 2.2. All water that doesn't end up in the beer is recycled. Almost 100% of glass used is also recycled, while through the Smart Barley programme – a global project to digitally connect farmers with the company and map best practices – cereal productivity and quality should increase.

EssilorLuxottica

E S **G**

EssilorLuxottica is the product of a 2018 merger between the French lens maker Essilor and the Italian eyewear group Luxottica. At a meeting in March, we raised a number of concerns around the cultural differences between the two companies. Those differences appeared central to the fact that integration plans were not yet agreed and that the search for a new CEO for the combined group was expected to take almost two years. Only days later, a number of press reports published clear details of governance conflicts between the two businesses.

Following our meeting, we concluded that over the longer term, the combined group may well be a powerful player in the strong growth market of corrective eyewear. However, we also agreed that management's current behaviour was of material concern. From our perspective, the risk that cultural and management misalignment might have a negative operational impact on the company overall could not be ignored.

Shin-Etsu

E S **G**

This proved a highly encouraging meeting with Japan's largest chemical company. It was rewarding to hear the company acknowledge the importance of a 2015 meeting between Walter Scott and Shin-Etsu's Chairman in the introduction of a more progressive dividend policy. This was strong confirmation that the Shin-Etsu board has been listening to our views, expressed both in writing and in numerous meetings over time, concerning its balance sheet and capital return policy.

Q4 2018

3M

E S G

There are very few businesses that don't have an ESG narrative to share. In a meeting with the chief financial officer of 3M, it was made clear that its customers aren't just talking about wanting sustainable products anymore, they're now demanding them. And 3M, is only too happy to oblige! In EVs (electric vehicles), 3M provides myriad products and solutions that go into the design and creation of an electric vehicle. For instance, there is a significant and growing number of cameras in EVs. 3M offers solutions to hide the cameras. It also develops vital components in EV batteries and produces sealants that bind plastic car parts together. By 2030 more than half the cost of building a car will come from electronic components, and 3M has a broad range of solutions for both component makers themselves, and for the assemblers.

Colgate-Palmolive

E **S** **G**

We enjoyed a wide-ranging discussion with a number of Colgate-Palmolive's senior managers. Among other subjects, the conversation touched on director skills and qualifications, sustainability, preferred shares and priorities for use of cash. Colgate has a well-structured board in terms of gender, independence and a good mix of tenure. Furthermore, all members of the audit committee are financial experts. The company's 2018 proxy statement also provided more disclosure around the qualities sought in board members and the rationale for each quality. The listed qualities are business operations, industry, regulatory and public service, information technologies, international, corporate governance and diversity.

We also discussed Colgate's stated sustainability commitments and progress with its 2015-2020 plan. The aims of this plan range from reaching 1.3 billion children with the company's 'Bright Smiles, Bright Futures' programme, to partnering with local and global organisations to bring clean water to under-served parts of the globe. Colgate has been awarded an "A" score for both water and climate by the CDP and it is committed to 100% recyclables (reusable, compostable) in all categories, and 25% recycled content for plastics by 2025.

Disney

E S G

During a conference call with a member of Disney's investor relations team, one of the main topics of discussion was the recently announced revised executive remuneration package. We had voted against the 'say on pay' resolution at the 2018 AGM. The company had proposed a one-off grant for its CEO. In our view, the quantum of the award was too large, the performance-based conditions were not testing enough and there was little alignment with the interests of shareholders.

The revised plan, acknowledged and discussed on this call, addressed these concerns, to a degree. Just as importantly, the revised plan provided positive evidence that shareholder feedback had meaningfully registered with the Board and that the experience will inform future pay awards.

Q3 2018

CSL

E S G

A call with the chair of the remuneration committee and the company secretary of this global biotherapy company gave us the opportunity to discuss the remuneration framework introduced in the prior year. Shareholders had requested more simplicity, and changes were needed to make the remuneration workable. A much stronger alignment with shareholder interests has now been achieved, with remuneration more closely linked to strategy and performance.

Evidencing the new arrangements in action, even though 2018 saw CSL post some great results, there had been no increase in basic salaries. This is down to a move orienting remuneration more towards long-term awards. Annual bonus targets remain the same (net profit after tax) but cash flow from operations has been used as a short-term incentive metric for the first time. The latter now plays a bigger role given this metric is important for the company; it sets CSL apart and leads to a higher investment capability compared to peers.

Nichols

E S G

As a soft drink supplier, primarily through its Vimto brand, Nichols is at the forefront of the debate around plastics. Following its half year results, we discussed this and other environmental issues with the company's chief financial officer (CFO).

Vimto's packaging is 100% recyclable so the issue is what the consumer then does with that packaging. To what extent soft drink distributors can change, or be responsible for, consumer behaviour, is a challenging question. Overall, 75% of packaging that is taken home is recycled, but recycling of 'on-the-go' product categories is lower at 43%. Consumers tend to be less diligent with their recycling when out and about.

The CFO stressed that the company would continue to work with its industry peers to enhance labelling and education on the recyclability of its products so that there is no misconception as to what can and what can't be recycled. This will hopefully nudge consumer behaviour. The BFCA (the industry association that Nichols and most UK beverage companies are part of) will work with the UK government on a plastics consultation starting in the autumn. On the agenda will be a proposed industry-wide deposit return scheme, which would potentially take a reverse vending machine approach.

Occidental

E S G

Having had a lengthy call a month previously, this meeting gave us the opportunity to discuss the carbon capture business in more detail among other ESG matters. Occidental is the world leader in carbon capture and storage through its sizeable enhanced oil recovery (EOR) business. This involves pumping CO_2 into maturing oil fields to increase resource recovery while sequestering enormous amounts of CO_2 in the process.

Occidental's EOR is roughly a quarter of group production, making Occidental by far the largest EOR business in the world. The key input for EOR is carbon dioxide, after which the CO_2 stays in the ground. Currently the majority of CO_2 used in the process does not come from anthropogenic sources, so while CO_2 sequestration isn't helping very much in the battle against climate change today, in time it most definitely will.

Several pilots are underway that are exploring ways to economically capture CO_2 from big emitters, such as ethanol or coal plants. Ethanol plants in particular could be a major source of anthropogenic CO_2 given the extremely high CO_2 content of the emitted residual gas. Further, the FUTURE Act is a federal incentive programme that offers CO_2 emitters an incentive of $35/tonne of CO_2 to implement carbon capture technology. The industry is still nascent but is growing rapidly and Occidental is very confident that ongoing improvements will help create a significant source of CO_2 for the company. This will ensure it has a plentiful and cheap supply for its profitable EOR business.

The company estimates that it has one billion barrels of oil resource that could be produced through EOR processes, assuming it has the necessary CO_2 in place. The volume of CO_2 sequestered underground in the EOR process is such that Occidental would be an enormous net positive contributor to greenhouse gas emissions. To put this in perspective, Occidental currently sequesters the equivalent CO_2 of 200,000 internal combustion engine vehicles.

PROXY VOTING

Responsibility for proxy voting rests with the Research team rather than a separate corporate governance team, demonstrating that it is a duty which we take very seriously. We will, on the majority of occasions, vote in line with management proposals. However, the team will vote against management if a proposal is not considered to be in the best interests of clients.

Through engagement ahead of an AGM we will often ask for clarification and where we have concerns we will raise them, thereby offering management the opportunity to state their case.

Where we do decide to vote against management we will typically ensure that the reason for the vote, and the underlying point of contention or concern is communicated directly to the company.

"Through engagement ahead of an AGM we will often ask for clarification and where we have concerns we will raise them, thereby offering management the opportunity to state their case."

Q2 2019

147

NO. OF MEETINGS

130

TOTAL VOTED AGMS

8

TOTAL VOTED SPECIAL MEETINGS

8

TOTAL MIX MEETINGS

1

TOTAL VOTED COURT MEETINGS

BASED ON ALL / VOTED MEETINGS	NO. OF VOTES	AS A % OF TOTAL PROPOSALS VOTED ON
Total all / voted proposals	1851	100
Total votes against Management Recommendation (MR)	113	6.1
Total votes against ISS recommendation	201	10.9
Total proposals voted 'For'	1685 (of which 5 were against MR)	91 (of which 0.3 were against MR)
Total proposals voted 'Abstain'	30 (25 against MR)	1.6
Total proposals voted 'Against'	134 (of which 81 were against MR)	7.2 (of which 4.4 were against MR)
Total proposals voted 'Withhold'	2 (of which 2 were against MR)	0.1

RATIONALE FOR VOTES AGAINST MANAGEMENT RECOMMENDATION	NO. OF VOTES
Political donations	6
Due to potential dilution >10%	57
Non-disclosure of individual board member's remuneration	4
Vague / Poorly-defined proposal	8
"Ad hoc" items	7
Bundled resolutions	8
Corporate governance issue	7
Compensation and stock option plans – not reasonable or excessive dilution	5
Excessive non-audit fees	1
Failure to address shareholders' concerns on the company's capital policy	1
Proposed dividend too low	2
Shareholder proposal – independent Board Chairman	2
Shareholder proposal – Eliminate Above-Market Earnings in Executive Retirement Plans	1
Shareholder proposal – Submit Severance Agreement (Change-in-Control) to Shareholder Vote	1
Shareholder proposal – one vote per share	1
Tender offer – not in best interest of long-term shareholders	1
Vague / Poorly-defined proposal and Bundled Resolution	1

Q1 2019

35

NO. OF MEETINGS

30

TOTAL VOTED AGMS

3

TOTAL VOTED SPECIAL MEETINGS

2

TOTAL VOTED COURT MEETINGS

BASED ON ALL / VOTED MEETINGS	NO. OF VOTES	AS A % OF TOTAL PROPOSALS VOTED ON
Total all / voted proposals	451	100
Total votes against Management Recommendation (MR)	25	5.5
Total votes against ISS recommendation	49	10.9
Total proposals voted 'For'	425 (of which 5 were against MR)	94.2 (of which 1.1 were against MR)
Total proposals voted 'Abstain'	9 (8 against MR)	2.0
Total proposals voted 'Against'	17 (of which 12 were against MR)	3.8 (of which 2.7 were against MR)
Total proposals voted 'Withhold'	0	0.0

RATIONALE FOR VOTES AGAINST MANAGEMENT RECOMMENDATION	NO. OF VOTES
Political donations	2
Due to potential dilution >10%	9
Non-disclosure of individual board member's remuneration	1
Vague / Poorly-defined proposal	1
"Ad hoc" items	4
Additional independence	5
Bundled resolutions	2
Corporate governance issue – Board term > 1 year	1

Q4 2018

23

NO. OF MEETINGS

18

TOTAL VOTED AGMS

4

TOTAL VOTED SPECIAL MEETINGS

1

TOTAL VOTED MIX MEETINGS

BASED ON ALL / VOTED MEETINGS	NO. OF VOTES	AS A % OF TOTAL PROPOSALS VOTED ON
Total all / voted proposals	225	100
Total votes against Management Recommendation (MR)	11	4.9
Total votes against ISS recommendation	29	12.9
Total proposals voted 'For'	210 (of which 1 was against MR)	93.3 (of which 0.4 were against MR)
Total proposals voted 'Abstain'	0	0.0
Total proposals voted 'Against'	15 (of which 10 were against MR)	6.7 (of which 4.4 were against MR)
Total proposals voted 'Withhold'	0	0.0

RATIONALE FOR VOTES AGAINST MANAGEMENT RECOMMENDATION	NO. OF VOTES
Political donations	1
Due to potential dilution >10%	8
Non-disclosure of individual board member's remuneration	1
Shareholder proposal – deduct impact of stock buybacks from executive pay	1

Q3 2018

24

NO. OF MEETINGS

18

TOTAL VOTED AGMS

6

TOTAL VOTED SPECIAL MEETINGS

0

TOTAL VOTED MIX MEETINGS

BASED ON ALL / VOTED MEETINGS	NO. OF VOTES	AS A % OF TOTAL PROPOSALS VOTED ON
Total all / voted proposals	270	100
Total votes against Management Recommendation (MR)	29	10.7
Total proposals voted 'For'	236	87.4
Total proposals voted 'Abstain'	3	1.1
Total proposals voted 'Against'	31 (of which 26 were against MR)	11.5 (of which 9.6 were against MR)
Total proposals voted 'Withhold'	0	0.0

RATIONALE FOR VOTES AGAINST MANAGEMENT RECOMMENDATION	NO. OF VOTES
Bundled resolutions	3
Due to potential dilution >10%	19
Non-disclosure of individual board member's remuneration	2
Poison pills	1
Political donations	4

COLLABORATION

We recognise the role that all investment firms have to play in raising standards, and encouraging greater transparency and reporting. Where appropriate, we participate in discussions and regularly provide input to industry initiatives.

From industry bodies pushing for higher standards, independent organisations seeking to raise awareness and prompt change in very particular areas and groups of investors seeking to share best practice, the number of groups that we could sign up to is ever increasing.

We are now members or signatories to a number of select groups that we believe best-represent the industry in pushing for meaningful change or where we feel the educational element will complement our own research in a material way.

Other groups are regularly assessed and we attend events and consider the work of many organisations where for now we have decided against a more formal association.

"We recognise the role that all investment firms have to play in raising standards, and encouraging greater transparency and reporting."

—We became a PRI signatory in 2017. Our 2019 rating is A+, A, B.

—Our commitment to the UK Stewardship Code dates back to 2010. That commitment has been consistently rated Tier 1 by the UK Financial Reporting Council (FRC), owner of the Code.

—We made public our commitment to the Japanese Stewardship Code on its launch in 2014.

—We are a member of the CDP (formerly, Carbon Disclosure Project).

—We are a longstanding member of the UK Investment Association, and more recently have been much more actively involved in a number of initiatives that we deem important for the industry.

—We are a member of Climate Action 100+ and engage with companies and other investors to pursue change in this ever-more critical area.

WE EXPECT NO LESS OF OURSELVES

"We have always sought to recruit individuals with varied backgrounds, personalities and academic interests, all united by a passion for what we do."

We expect the companies in which we invest on behalf of our clients to strive towards sound ESG practices. And we expect no less of ourselves.

We are proud of our track record in retaining, and motivating, staff. We believe our culture is distinct, and that its strength has been key to the firm's success. We have always sought to recruit individuals with varied backgrounds, personalities and academic interests, all united by a passion for what we do.

Operationally our offices, built in the early and mid-1800s offer both benefit and challenge. However, where we can, we strive to ensure efficiency and sustainability. In 2019, we switched to 100% green energy, draught proofed windows and installed more energy-efficient boilers.

Similarly, we continually look for ways to both cut back on the need for recycling and to recycle as much as we can efficiently. In the first half of 2019, we recycled 75% of our total waste.

In considering the community in which we all work and live, we have supported a range of philanthropic causes across education, health, historical architecture and local communities.

Oversight of our ESG-related actions today, as well as responsibility for the encouragement and direction of ongoing improvement falls to an ESG Group. Senior colleagues from Research, Investment Operations, Client Service, Client Operations and Communications form that Group reflecting the importance of its work and the need to address these issues across the firm's activities.

It goes without saying that there is always more we can do. In that respect, we are on the same journey as many of the companies in which we invest. And like them, we are committed to exploring new and innovative ways to meet the high ESG standards we set ourselves.

75%

—WASTE RECYCLED IN FIRST HALF OF 2019—

FURTHER READING

THE REPORTS LISTED BELOW ARE AVAILABLE ON REQUEST FROM CLIENTSERVICE@WALTERSCOTT.COM

Quarterly ESG Commentaries

Research Papers

Responsible Investing: An Integrated Investment Approach (2018)

Research Journal articles

Journal 8
A Healthy Balance – The healthcare industry is changing fast, amid rising demand and rapid advances in treatment. Co-Head of Research, Alex Torrens, and Investment Managers Tom Miedema and Maxim Skorniakov consider the economic, social and technological issues faced by the industry.

Shake Up Your Make-Up – The challenges in building a diverse workforce and how best to overcome them.

Opening Minds To Diversity Of Thought – Sean Brocklebank, Senior Teaching Fellow at The University of Edinburgh makes the case for cognitive diversity within teams.

Forced Labour – The effect of forced labour on supply chains worldwide. Interview with Rosey Hurst, founder of Impactt.

Not Paying By The Rules – Working for low or no pay is widely associated with far-off climes, yet it is increasingly common in developed markets.

THE FOLLOWING POLICIES ARE AVAILABLE ON REQUEST

ESG Policy

Engagement Policy

Proxy Voting Policy

Conflicts of Interest Policy

In addition, Walter Scott's response to the UK Stewardship Code and Japan's Stewardship Code is available on our website: walterscott.com

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Donald Provan
Green And Silver Shoal

Walter Scott has been supporting emerging Scottish talent since 1988. In the same way that we believe that different perspectives within the team generate the best investment ideas, so we believe that our art collection should incorporate a wide range of work from an eclectic group of contemporary artists.

Our commitment to the art community is also reflected in our established partnerships with – and sponsorship of prizes at – the Royal Scottish Academy, the Royal Glasgow Institute of The Fine Arts and the Royal Scottish Society of Painters in Watercolour.

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