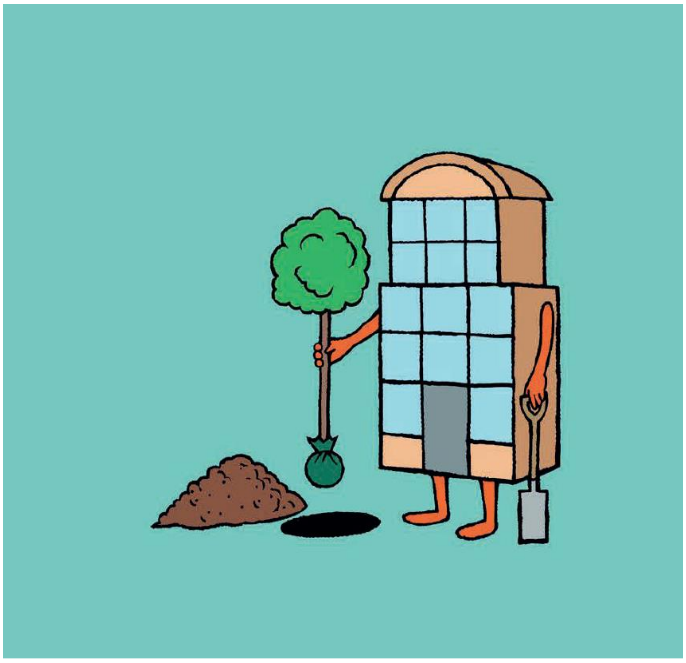
ESG HANDBOOK

Sustainable Investing at
Montanaro Asset Management

2024



MONTANARO

Certified B Corporation

Introduction

Our “ESG Handbook” is now in its 10th year. We first published it in 2014 because we had just been through a major update of our Ethical and Environmental, Social and Governance (ESG) policies. These policies define how we integrate ethical and ESG criteria into our investment process. At the time, this led to the rebuilding of our ESG Checklist, a template that is used by our Analysts to appraise the ethical and ESG credentials of companies within our investment universe.

Since 2014, ESG and sustainable investing has moved firmly into the mainstream. Impact investing – a term many investors in public markets were unfamiliar with just a few years ago – has come to the fore. Some investors are advocates of this shift; others are firmly against the emphasis placed on sustainable investing.

Despite the fundamental shift in the market, this Handbook aims to deliver on its original aim: to explain how we apply ethics and ESG considerations to investing in Small & Midcap quoted equities. We also explain our approach to impact investing.

Our approach has continued to evolve. In 2023, we again redeveloped our ESG Checklist in response to the better availability of ESG data in the Small & Midcap space. We continue to conduct engagement with our companies to improve their sustainability reporting, believing that this can lead to more complete investment cases.

One of the reasons we place such importance on conducting our own ESG research is because it allows us to draw conclusions that we believe the market may be missing. For example, there are instances where a company is scored poorly for ESG by a major third-party research provider, but scores well on our internal ESG Checklist. While other investors may shun the stock because it could negatively affect the overall ESG rating of a fund, we are willing to invest if we think the flagged weakness is either incorrect or can be addressed through proactive engagement.

Our approach, like that of our investors and the wider market, will continue to evolve. As we improve and adapt, so we will update this Handbook.

Our aim with this document is to tell you everything about our approach to Sustainable Investing:

- Who we are and how we invest
- Why we think our Ethical framework remains relevant today
- How we integrate ESG into our Quality Growth investment process
- Our approach to Impact Investing
- Why being Sustainable Investors is integral to our role as long-term shareholders

We hope that you find it informative.

Ed Heaven - Head of Sustainable Investments

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About Montanaro

Montanaro Asset Management ("MAM" or "Montanaro") is an asset management company that specialises exclusively in the management of long-only Global, European, and UK Small & MidCap equity portfolios.

History & ownership

MAM was founded in 1991 by Charles Montanaro to provide an institutional approach to investing in Small & MidCap quoted equities. MAM remains true to this Smaller Companies heritage and have expanded our geographic remit over the last 30 years. During the 1990s, MAM invested exclusively in UK equities; in the 2000s we began investing in companies listed in Continental Europe; and in 2018 we launched our first Global fund.

We introduced our first ethical exclusions in the 1990s; ESG was fully integrated into our investment process from 2005 (when we were awarded a mandate by the Church of England); and in 2018 we launched our first Global Positive Impact Fund, the Montanaro Better World Fund ("BWF"). In 2019, we won our first Impact mandate from a large Nordic Public Pension Fund. This was followed by the launch of a UK domiciled version of BWF in 2020. Our ethical framework and ESG analysis are applied to 100% of our assets.

B Corporation

In 2019, MAM placed sustainability at its core by becoming a certified B Corporation[1]. This was achieved by meeting verified standards of social and environmental performance, transparency and accountability. In 2020, we amended our Articles of Association to place a legal obligation on the Board to consider the impact of Montanaro's business on its stakeholders. This formalised our business approach as one of "Stakeholder Capitalism" - moving beyond a "shareholder primacy" model to consider the impact of our organisation on all stakeholders, including people and planet. MAM recertified as a "B Corp" in 2022.

Certified B Corporation — This company meets the highest standards of social and environmental impact

Our investment approach

At MAM, all portfolios are managed according to the same "Quality Growth" investment philosophy.

We are stock pickers at heart: we construct portfolios purely on a bottom-up basis. We aim to identify the highest quality companies with the best management teams that we can hold for the long term. We believe that you "get what you pay for in life": it is worth paying more for a well-managed, financially sound business that operates in a growth industry and enjoys a sustainable competitive advantage. Businesses with such quality characteristics are able to "beat the fade" and maintain a high Return on Capital (ROC) over the long term.

A "Montanaro" company has the following characteristics:

- A business model we can understand;
- Profitable growth;

[1] A summary of our B Corporation score is available here: https://www.bcorporation.net/en-us/find-a-b-corp/company/montanaro-asset-management/

- Focused business operating in growth markets;
- Market leader;
- High returns on capital with strong balance sheet / cashflow;
- Outstanding management;
- Exemplary standards of ESG and a willingness to engage.

We take a conservative approach. We never lose sight of our primary goal which is to make money for our clients through sound investment decisions based on our own rigorous, fundamental analysis. We also believe that it is right to align our interests with those of our investors – we all invest in our Investment Trusts and Funds alongside our clients.

Sustainable investing

A sustainable focus is central to how we invest. We believe that the best and most sustainable investment returns come from the highest quality businesses, run by the very best management teams. ESG forms part of our definition of a company's Quality and ESG is fully integrated into our investment process. For a company to be deemed "Quality", it must meet the standards set out in our Ethical and ESG Policies, which we explain below. We do not invest in companies that fail to meet our ESG standards or those that are unwilling to engage with us on areas of weakness. We believe this approach is well understood by our investee companies, providing us with good access to management when we need to engage, an approach endorsed by our clients.

We aim to achieve "best in class" status for our approach to sustainable investing and ESG:

- As a certified B Corporation, sustainability is embedded in MAM's Articles of Association;
- ESG & Stewardship is a standard item at all MAM Board meetings;
- Our Sustainability Committee is tasked with overseeing all aspects of Montanaro's sustainable approach;
- An internal Net Zero Carbon Steering Group to guide us towards our net zero targets at the company and portfolio level;
- ESG and Impact Analysis is fully integrated into our Investment Team;
- We utilise proprietary ESG screens and checklists to assist our Analysts as they conduct due diligence on companies;
- We utilise ESG data and services from MSCI, Bloomberg and Impact Cubed.

Our commitment to sustainable investing

ESG analysis is fully integrated into the investment process for all Montanaro Portfolios. Analysts at Montanaro are responsible for conducting fundamental research alongside ESG analysis. This helps us to build as complete a case as possible for the "Quality" of an investment.

To us, being Sustainable Investors means considering anything that may influence the long-term financial performance of our investments. Oversight is provided by our Sustainability Committee who formulate our ethical and ESG policies and ensure their consistent implementation across the house. ESG forms part of Analyst appraisals and is directly tied to remuneration.

Research supports our view that there is a positive correlation between how well a company manages issues in relation to ESG and what we are ultimately concerned with: the long-term return for our clients. We believe that this approach will help to foster a more sustainable form of capitalism.

We have a long-term investment horizon

We are genuine long-term investors, an increasing rarity these days. We still hold investments made in our first Fund launched in 1993, more than twenty years ago.

We are a truly Sustainable Business

We encourage our colleagues to live sustainably at Montanaro and in the world beyond. In recent years we have launched a number of sustainability initiatives: we have policies to reduce energy use and waste; we offset our carbon footprint; and we are active in the community via charitable work and donations.

Our sustainable focus became embedded within the legal framework of our company when we became a certified "B Corporation" in 2019. Montanaro is also a PRI signatory since 2009 and has been awarded the "Label ISR" (SRI label) by the French Ministry of Finance for our Better World Fund. We have been signatories to the UK Stewardship Code since its inception in 2010.

Sustainability is part of our investment DNA

Sustainability forms an integral part of how we think, behave and invest. ESG was first included in our investment process almost 20 years ago and today is firmly integrated within our approach. Every Analyst at Montanaro is responsible for conducting ESG and impact analysis on the companies under their coverage. The result is that our investment decision makers "do" sustainability analysis.

We conduct fundamental company analysis

At Montanaro, all research is conducted in-house. This has allowed us to integrate ESG into our investment process. We recognise that this is resource and time consuming, especially in SmallCap where managers cannot rely on external ESG research. It is one reason why we have arguably the largest team of SmallCap Analysts in Europe. It is also why our Analysts are capable of not just assessing a company's finances but also the more qualitative aspects of a business.

We seek to engage with our investee companies

As fiduciaries of our clients' assets, we take our shareholder responsibilities seriously. Through regular interaction with management teams, we seek to promote high standards of ethics, an awareness of environmental and social issues and transparent corporate governance practices. We have an active policy of proxy voting and a track record of seeking to improve companies through engagement rather than exclusion.

We take a stance on ethical issues
There are some companies that we will not consider investing in. Typically, this is where they are involved in operations that we deem ethically detrimental to wider society. Our stance in these areas forms part of our commitment to our fellow stakeholders and helps to foster a longer-term perspective in the asset management industry.

Our industry commitments include:

- **2009**: Principles for Responsible Investment (PRI)
- **2010:** FRC Stewardship Code
- **2015:** Carbon Disclosure Project (CDP)
- **2017:** LGPS Code of Transparency
- **2019:** B Corporation Certification
- **2019:** Farm Animal Investment Risk & Return (FAIRR)
- **2020:** Net Zero Asset Managers Initiative
- **2021:** Glasgow Finance Alliance for Net Zero
- **2022:** Tobacco Free Portfolios Finance Pledge
- **2022:** Living Wage Accreditation
- **2022:** UK Sustainable Investment and Finance Association (UKSIF)
- **2023:** Task Force for Nature Related Financial Disclosures (TNFD)
- **2023:** Investor Coalition on Food Policy
- **2023:** ShareAction - Long-term Investors in People's Health (LIPH)
- **2023:** ShareAction - Workforce Disclosure Initiative (WDI)

We have won a number of awards for our approach in recent years:

2019	Winner of **"Best Impact Fund"** Award (Investment Week) Winner of **"Best Impact Report"** Award (Pensions for Purpose)
2020	Highly Commended "**Best Impact Fund**" Award (Investment Week)
2021	Winner of "**Best Impact Equity Fund**" Award (Investment Week)
2022	Highly Commended for "**Best Impact Fund**" Award (Investment Week) Winner of "**Best Equity Global Small & MidCap Fund**" 3 years (Lipper)
2023	Winner of "**ESG Company of the Year**" Award (Financial Times) Winner of "**Best ESG Investment Fund: Impact**" Award (ESG Investing) Winner of "**Best Sustainable UK Equity Fund**" Award (Investment Week) Highly Commended for "Best **Biodiversity Report**" (Pensions for Purpose)
2024	Winner of "**Best ESG Global Equity Fund**" Award (MainStreet Partners)

Note: not all ratings are current - all awards were given either to MAM or MAM Funds domiciled in Ireland (Irish UCITS V OEIC).

Sustainable investment policies

Companies that we consider for investment must pass the criteria set out in the following policies. These policies are used to construct our ESG Checklist which our Analysts complete during the research process. ESG forms an intrinsic part of Montanaro's assessment of a company's "Quality".

Ethical Policy – our Ethical Exclusions apply across our entire product range

On ethical grounds, we do not invest in companies that are involved in any of the controversial activities listed below (MAM's "Banned List").

Specifically, we:

- do not invest in companies with any production revenue exposed to these activities;
- have a 10% revenue limit to companies that distribute products or services on the Banned List;
- have a 20% revenue limit to companies that provide services to areas of the economy included in our Banned List.

ETHICS

Exclusions:
- Fossil fuels
- Weapons
- Tobacco
- Alcohol
- Gambling
- Pornography
- High interest rate lending
- Animal testing (ex-Healthcare & Regulatory)

As an example:
- **we would not** invest in an oil and gas producer as this would breach the 0% production revenue threshold.
- **we could** invest in a company distributing energy, such as a power company operating an energy grid, so long as less than 10% of energy came from fossil fuels.
- **we could** invest in a company providing IT services to the oil and gas sector, so long as revenue to such companies was less than 20% of total company revenue.

Fossil Fuels
- Exclusion of companies involved in the exploration and production of coal, oil and gas.
- Ban encompasses both onshore and offshore extraction.
- We also ban investment in fossil fuel refinement companies.

Tobacco
- Exclusion of companies involved in the production of tobacco products.

- Ban encompasses traditional products (e.g. cigarettes) and vaping, heated tobacco products and e-cigarette products.

Alcohol
- Exclusion of companies involved in the production of alcohol products.

Gambling
- Exclusion of companies that own or operate gambling facilities of any kind (e.g. casinos, racetracks, lottery operations, online gambling, spread betting).
- Companies that provide key products or services fundamental to gambling operations, including (but not restricted to) products manufactured exclusively for gambling or gambling technology are fully excluded.

Pornography
- Exclusion of companies that produce pornography.
- Ban encompasses magazines, newspapers, videos, films, websites and related software, as well as companies involved in the staging of live sex shows or the ownership of sex shops.
- Companies that provide key products or services fundamental to pornography operations, for example IT maintenance or software design.

High Interest Rate Lending
- Exclusion of any business whose activity is the provision of home-collected credit ("doorstep lending"), unsecured short-term loans ("payday loans") or pawnbroker loans, directly or through owned-subsidiaries.
- Common indicators of exploitative lending are close to triple-digit Annual Percentage Rates; short loan term durations (less than 18 months); and no requirement for security.

Weapons
- Controversial/indiscriminate weapons exclusions: of companies involved in the production or supply of indiscriminate weaponry (defined as nuclear weapons, anti-personnel mines, cluster munitions, chemical weapons or biological weapons), with no turnover threshold to be applied.
- Any company involved in the production, processing, supply or storage of weapons-grade nuclear fissile materials, with no turnover threshold to be applied.
- Any company involved in the provision of parts or services for anti-personnel mines, cluster munitions, chemical weapons or biological weapons, with no turnover threshold to be applied.
- Conventional weapons exclusion: We ban investment in manufacturers of conventional weaponry and any company deriving more than 10% of its turnover from any strategic military sales including conventional military platforms, whole military systems or strategic military parts or services.
- Non-military firearms exclusion: Any company deriving more than 10% of its turnover from the production or sale of non-military firearms or ammunition, excepting companies specialising exclusively in products specifically designed for hunting or sporting purposes.
- Note: Under this policy Montanaro is permitted to invest in companies whose products are used to ensure the safety of military personnel (e.g. protective equipment such as helmets), although such companies must not have exposure to the areas banned above.

Animal Testing
- Exclusion of companies that conduct (either themselves or via outsourcing) animal testing.
- We allow animal testing for the purposes of regulated healthcare research and regulatory

requirements.

- Where animal testing is conducted it must be required by regulation and we expect companies to have a clear animal testing policy compliant with “The Three Rs”:
  - Replacement: methods which avoid or replace the use of animals in research;
  - Reduction: use of methods that enable researchers to obtain comparable levels of information from fewer animals, or to obtain more information from the same number of animals;
  - Refinement: use of methods that alleviate or minimise potential pain, suffering or distress, and enhance animal welfare for the animals used.

Environmental Policy

Our Environmental Policy helps us to select the highest quality companies by identifying the environmental factors we need to consider from an opportunity, strengths, weaknesses and risks perspective. The areas that we focus on are influenced by and support the UN Global Compact.

Via an internally designed ESG Checklist, we assess and score companies out of 10 based on their environmental profile. Our approach helps to drive more accurate risk analysis, helping us to invest in those businesses capable and willing to manage their environmental footprint in a changing world. We engage with companies on environmental issues to better understand their approach to environmental issues; improve areas of weakness; and encourage improved levels of data disclosure and reporting.

We assess the data of a company's Environmental Profile, comparing this against a global benchmark, our Approved List (companies that we can invest in across our portfolios) and a relevant peer group. Indicators considered include:

ENVIRONMENTAL

Climate targets
- Net Zero (interim and final) & SBTi

Carbon Emissions
- Absolute, intensity and trajectory for Scope 1 & 2
- Absolute Scope 3
- Use of renewable energy
- Carbon intensity of supply chain

Water
- Policy
- Intensity

Waste
- Policy
- Waste intensity of operations (including toxic emissions and packaging waste)

Biodiversity
- Policy
- Exposure to operations with highly fragile ecosystems & with land or ecosystem disturbance

Climate Change: Our views on the "Energy Transition"

Climate change is possibly the greatest challenge facing humanity. To ensure that climate change is kept within a manageable range, a shift in how we produce and consume energy is required. Different views exist on how this can be achieved and the role that investors can play.

There are those who believe that investors should divest from fossil fuel industries. The divest movement – which has been seen before in relation to sectors including tobacco and political movements such as apartheid South Africa – seeks to remove investor support for companies involved in the production and supply of fossil fuels. The aim of this is to drastically reduce, or halt, the amount of fossil fuels extracted from the earth. The scientific argument in favour of this is that between two-thirds and four-fifths of fossil fuel reserves need to remain in the ground in order to limit global warming to a rise of 2°C compared to pre-industrial temperatures (these reserves are often referred to as being "stranded"). There is far more carbon lurking within existing fossil fuel reserves than can be safely burnt.

At the other end of the spectrum are those who believe that investors should continue to invest in fossil fuel related companies. The benefits fossil fuel production have brought to the world are often cited in support of this view: cheaper and more available energy has helped lift millions of people out of poverty, supporting globalisation and the raising of living standards. Turning off capital flows to fossil fuel industries could place this at risk given the Replacement Energy System – e.g. renewables – remains in its infancy. According to research by the energy consultant Lambert Energy Advisory, *"out of the 280 million barrels of oil equivalent energy (BOE) produced to keep…6 billion customers happy, only 7 million BOE will be 'new renewables'."*

Investors stepping into this debate must tread with care. Our aim is to support the shift to a cleaner energy mix as quickly as possible.

As well as our exclusions of exploration and production fossil fuels we also consider:

Nuclear:
High profile incidents such as Chernobyl and Fukushima have negatively impacted the public perception of nuclear power. Some countries, such as Germany, have stepped away from nuclear power altogether. The nuclear debate is one that we will continue to monitor. The energy produced is cleaner than fossil fuel energy, but clearly there are other challenges: if something goes wrong the consequences are potentially catastrophic, while the issue of radioactive waste disposal is yet to be settled. Another point to consider, particularly from an investment perspective, is the high cost of nuclear power plants, which makes a decent return on invested capital challenging.

Renewables:
The World Energy Council notes that *"the rate of improvements towards cleaner energy is far slower than required to meet emissions targets"*. Renewable energy must take up a greater share of the global energy mix if climate change is to be stopped or reversed. A steady transition is needed, however, so that the most sustainable and efficient technologies emerge. These must not rely on unsustainable subsidies and investors should carefully consider the investment risks of "concept" ideas that have yet to deliver a financial return. New technologies must be cleaner than fossil-based alternatives across their value chain, not just when they reach the consumer.

In addition to the above, we wish to encourage all of our investee companies to consider their energy consumption and what they can do to reduce their own carbon footprint. This is the focus of our multi-year "Project: Net Zero Carbon" engagement. Net zero targets can help the energy transition, allowing the "Carbon Budget" (the estimated amount of carbon we can use without breaching the 2°C limit) to be used by areas of the economy where it is most essential. We encourage companies to implement Science Based Targets and to get such targets externally verified.

We also engage with companies to better understand and influence the steps they take in relation to their carbon emissions. We want to encourage our companies to aid the transition to a lower-carbon economy, hence in 2015, we became signatories of the Carbon Disclosure Project.

The focus on a business's environmental impact is only likely to increase over time: three of the ten UN Global Compact Principles are dedicated to the environment. These state that companies should *"support a precautionary approach to environmental challenges…promote greater environmental responsibility…and encourage the development…of environmentally friendly technology"*. We encourage companies to continue improving their levels of environmental reporting.

Social Policy

Our Social Policy allows us to analyse specific social factors, leading to more accurate risk analysis of investment opportunities. The areas that we focus on are influenced by and support the UN Global Compact.

We engage with companies on social issues – by doing so, we believe that we can help to encourage management teams to contribute to a more sustainable world, which will ultimately lead to better investment returns. Companies are scored out of 10 for their social profile on our ESG Checklist. We use MSCI, Bloomberg and company-sourced data to measure and record data relevant to a company's social profile.

We assess the data of a company's Social Profile, comparing this against a global benchmark, our Approved List (companies that we can invest in across our portfolios) and a relevant peer group. The factors we consider include:

SOCIAL
Diversity • Women in workforce & management • Diversity and discrimination controversies • Gender pay gap reporting Labour practices • Health and Safety (policy, injury rate, annual fatalities) • Management of supply chain • Controversies (human rights and supply chain labour) • Annual employee turnover Policies • Human Rights, Child Labour, Diversity, Equal Opportunity, Bribery and Anti-corruption, Business Ethics, Consumer Data Protection Tax gap

Corporate Governance Policy

We wish to align the interests of company management teams with the interests of long-term shareholders. Our Corporate Governance Policy helps us to identify companies with high standards of governance, while highlighting companies with areas of risk or weakness.

Our logic here is simple: good corporate governance increases the quality of a business – and the higher the quality of a business, the greater the sustainability of investment returns. Via our ESG Checklist, we assess and score companies out of 10 on their governance profile.

We engage with companies on governance issues and work with management teams to foster a responsible and long-term approach to the running of their companies. We assess the data of a company's Governance Profile, comparing this against a global benchmark, our Approved List and a relevant peer group. Indicators considered include:

GOVERNANCE

Board composition

- Chair (independence, whether combined with CEO)
- CEO gender (not scored)
- Board (independence, % women, average tenure of independent directors, significant votes against)

Insider ownership

- CEO equity (changes, multiple of salary)
- Remuneration
- CEO (total pay USD & whether in extreme range, non-equity bonus paid, CEO-to-employee ratio)
- Pay (link to sustainability, say on pay policy, significant votes against)

Committees

- Remuneration (including % independent directors)
- Audit (including % independent directors, financial expert present, tenure of auditor)
- Nomination

Ethics

- Business ethics
- Controversies

We engage with companies on governance issues and work with management teams to foster a responsible and long-term approach to the running of their companies.

Remuneration:
We consider the level of executive compensation, including base salary, bonuses and long-term incentives. In particular, we are interested in the structure of remuneration packages and the role of the Remuneration Committee. The right kinds of incentives can ensure that management are focused on what matters most for shareholders: creating sustainable shareholder value. As long-term investors, we want the interests of management to be aligned with ours. We expect management teams to behave ethically and responsibly in relation to pay, taking into account the impact excessive executive pay can have on other stakeholders.

Capital Allocation Record:
When we model a company's financials, we also analyse the capital allocation record of the management

team. This tells us whether management have been deploying capital efficiently and effectively, thereby enhancing the long-term value of the business. To ascertain this, we analyse Return on Capital Employed (ROCE) relative to the cost of capital. Shareholder value is created when economic ROCE is sustained at a level above the cost of capital. We are specifically interested in what management are directing their capital towards. We consider the level of reinvestment in the business; the acquisition track record; the dividend policy; share buyback programs and the level of cash relative to debt.

Board Independence, Ownership & Diversity:
Companies should aim to have the right governance structure in place. In general, we look for Boards to have a majority of Non-Executive, fully independent Directors. We recognise, however, that this may not always be possible or warranted in the case of small companies. An executive founder, or a family, may retain a material interest in the business and a significant presence on the Board. Therefore, we consider the suitability of Boards on a case-by-case basis, taking into account Director tenure, skills and reputation. We expect companies to disclose sufficient biographical information about Directors to enable investors to make a reasonable assessment of the value they add to the company. We want to see our investee companies achieve Board independence over time.

Voting:
Voting is a vital part of our engagement with companies which is why we vote at all AGMs (where possible). We receive independent third-party corporate governance reports and voting recommendations from Institutional Investor Services (ISS) ahead of meetings. These are used for advice only. Our Analysts systematically review all resolutions ahead of shareholder meetings and we voice our concerns where required. We aim to discuss any issues with management prior to voting against or abstaining. As such, we consider ourselves as “active” shareholders rather than “activists”.

ESG Checklist

Analysts complete the ESG Checklist for companies as part of fundamental research. The ESG Checklist draws on 80 data points, sourced from MSCI, Bloomberg and directly from company reports. Analysts also score companies based on their own research and informed opinion. This results in a “MAM ESG Score”. Companies with scores of less than 5 require engagement as a material point of weakness has been identified. An example summary of our ESG Checklist is show below:

SCORE SUMMARY		
ETHICS		PASS
ENVIRONMENTAL	*weight 30%*	7.1
SOCIAL	*weight 30%*	6.3
GOVERNANCE	*weight 40%*	6.9
MAM ESG RATING		6.8
RESULT:		PASS
MSCI RATING		AAA
MAM UNIVERSE SCREEN ESG RATING		AAA
RAW MAM ESG DATA SCORE (EQUAL WEIGHTING)		6.8

Sustainability in the investment process

ESG analysis is fully integrated into the Montanaro investment process. This analysis is conducted by our Investment Team meaning that our decision makers "do" ESG.

The following investment process is applicable to all Montanaro Funds. The BWF has an additional impact stage, which is explained in the "Impact" section of this handbook.

Thanks to the improving availability of ESG data, we have developed an "ESG Screen" that allows us to rank the Small & MidCap investment universe based on certain ESG criteria at both a Global and a European level.

The screen utilises 10 ESG data inputs. These 10 criteria are weighted according to their importance to produce a "MAM ESG Screen Rating" from AAA (best) to D (worst). All data points come from MSCI or Bloomberg.

The ESG factors we consider in the screen are:

		ESG factors									
		Ethics	Environmental			Social		Governance		General	
Location of risk	ESG Screen Rating	Permissible sector	Carbon Intensity 1+2	Water Intensity (vs. sales)	Waste Intensity (vs. sales)	Anti-Bribery Ethics Policy (Y/N)	% Women in Workforce	% Women on Board	% Independ. Directors	MSCI Weighted Average Score	ESG Disclosure Score

These factors are explained below:

Location of risk (country exclusions):

<u>We screen out Chinese and Russian businesses on ethical grounds</u>. We use the Bloomberg "Country or Territory of Risk" field to identify these stocks:

1. <u>Holding Companies</u>: a holding company with the majority of its revenue generating operations being derived from subsidiaries or other equity investments in China/Russia.
2. <u>The following factors may also be considered</u>: Location of Management / Country of Domicile / Country or Territory of Listing / Primary Security Composite Exchange Code / Sales / Revenue / Country or Territory of Largest Revenue / Reporting Currency / Currency Override.
3. <u>China specific: Red Chip Companies</u>: a company that does most of its business in China but is listed on the Hong Kong Stock Exchange ("H" Shares and Red Chip issuers).

Permissible sector:
We screen out companies on ethical grounds and also to avoid investing in carbon intensive businesses, in support of our environmental objectives.

Using ICB Level 4 sub-sectors we screen companies involved in the following areas:

- Aluminium
- Brewers
- Casinos & Gambling
- Cement
- Chemicals and Synthetic Fibres
- Chemicals: Diversified
- Coal
- Copper
- Defence
- Diamonds and Gemstones
- Distillers & Vintners
- Diversified Materials
- Forestry
- General Mining
- Iron & Steel
- Iron and Steel
- Metal fabricating
- Metal Fabricating
- Multi-utilities
- Nonferrous Metals
- Oil Equipment and Services
- Oil Refining and Marketing
- Oil: Crude Producers
- Paper
- Plastics
- Platinum and Precious Metals
- Soft drinks
- Sugar
- Textile Products
- Tobacco

Any company that does not comply with the country/sector exclusions listed above will be automatically rated "D".

ESG Factors:
We capture data across the following ESG factors to help us calculate the MAM ESG Screen Rating. The weightings applied to these factors are also shown below:

	Environmental			Social		Governance		General	
ESG Factor:	Carbon Intensity 1+2	Water Intensity (vs. sales)	Waste Intensity (vs. sales)	Anti-Bribery Ethics Policy (Y/N)	% Women in Workforce	% Women on Board	% Independ. Directors	MSCI Weighted Average Score	Bloomberg ESG Disclosure Score
Weighting	10.0%	5.0%	5.0%	7.5%	7.5%	7.5%	7.5%	25.0%	25.0%

Definitions:
- MSCI Weighted Average Score: this score indicates how well the index constituents manage their most material ESG risks relative to sector peers based on MSCI's analysis. Scores range from 10 (best) to 0 (worst).
- Bloomberg ESG Disclosure Score: a score based on the extent of a company's ESG disclosure. The score ranges from 0 for companies that do not disclose any of the ESG data included in the score, to 100 for those that disclose every data point.

The results of the screen are as follows[2]:

Global Screen:

There are over 11,000 stocks in the Global Small & Midcap investment universe (companies with market capitalisations of between $100 million to $60 billion). When we apply the above ESG Screen to this universe, the number of stocks across the various categories are as follows. (Please note that "NR" stands for "No Rating", where data availability remains poor):

ESG Screen Rating	Number of stocks	%
AAA	1179	10%
AA	1176	10%
A	1364	12%
B	945	8%
C	2336	20%
D	2351	20%
NR	2374	20%
Total	11725	

European Screen:

There are over 3,000 stocks in the European Small & Midcap investment universe (companies with market capitalisations of between €50 million to €60 billion). When we apply the above ESG Screen to this universe, the number of stocks across the various categories are as follows:

ESG Screen Rating	Number of stocks	%
AAA	341	10%
AA	337	10%
A	459	14%
B	66	2%
C	675	20%
D	678	20%
NR	830	25%
Total	3386	

A result, at both the Global and European level is that ~20% of companies fall into the "D" category. Typically, D rated companies are excluded from further analysis[3].

<u>Exceptions:</u>

In exceptional circumstances, we may consider that continuing to analyse and invest in a "D" rated company is warranted. For a "D" rated company to be considered for investment it must pass through three internal hurdles[4]. This is also the case for "non-rated" stocks, which may be of a high ESG quality, but may suffer from poor levels of public data disclosure. As the below steps indicate, it is always the

[2] As of March 2024
[3] The exclusion of 20% of the Global and European investment universe on ESG grounds is aligned with the requirements of the French "Label ISR", Pillar 2.1.1.
[4] This exception is in line with the requirements of the Label ISR requirements under pillar 2.1.2

case that 90% of a Fund's holdings will have been rated.

The three internal hurdles are:

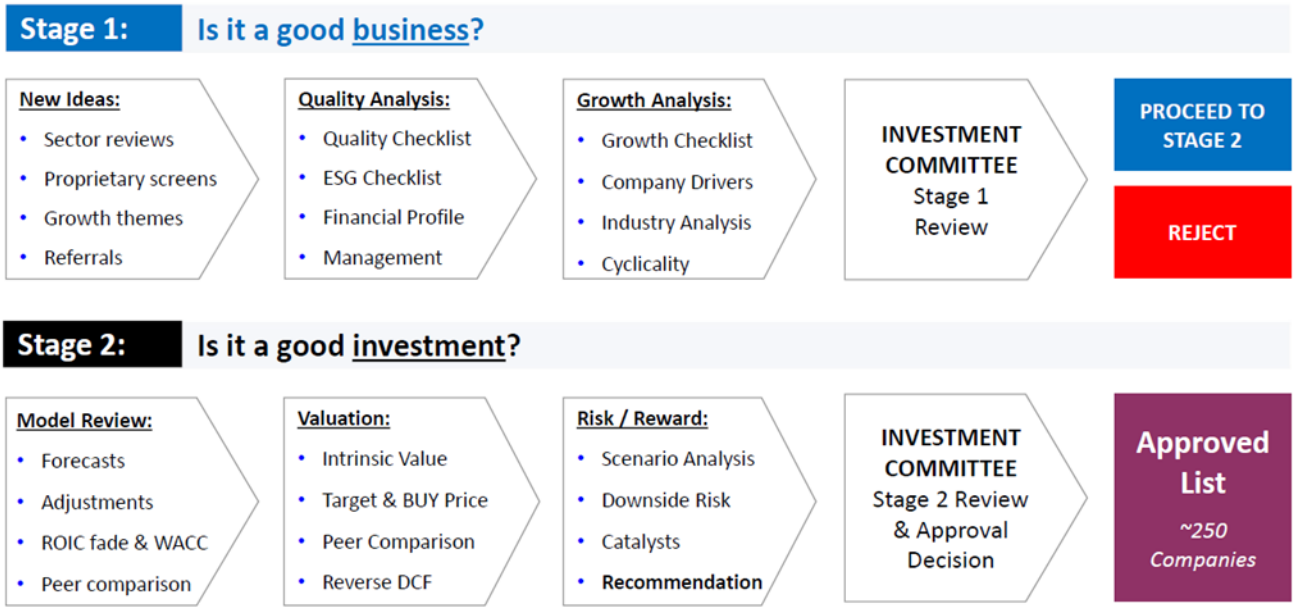
- ✓ The company must score at least 5 out of 10 on Montanaro's internal ESG Checklist.
- ✓ The company must be approved by Montanaro's Sustainability Committee.
- ✓ "D" rated stocks cannot together account for more than 10% of a Fund's AUM.

The outputs from the screen are reviewed by the Compliance department on a quarterly basis.

Once this screening process is complete, Analysts then begin the fundamental parts of Montanaro's Investment process.

ESG in the "fundamental" investment process:

Our investment process has two distinct stages.



The first stage focuses on identifying High Quality companies. In essence, we aim to answer the question: "Is it a good business?". ESG forms part of our definition of a company's "Quality". We do not believe it is possible for a company to be deemed Quality if it is exposed to material ESG risks, or management do not pay due attention to material ESG factors.

Using our bespoke ESG Checklist, Analysts appraise the ESG profile of our companies.

Conclusions from our ESG analysis are presented to the Investment Committee who discuss any issues with the Analyst. The Committee will decide to continue with, or discard, a new idea based on the Analyst's findings. Companies with a total ESG score of below 5 are flagged on the Checklist under "ENGAGE" meaning that engagement is required if we wish to invest in the company.

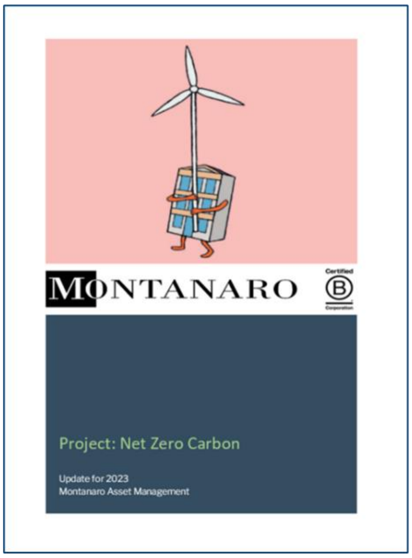
ESG Checklist scores are reviewed by the Investment Team on an ongoing basis and scores are recorded in the Montanaro holdings file, of which monthly records are kept indefinitely.

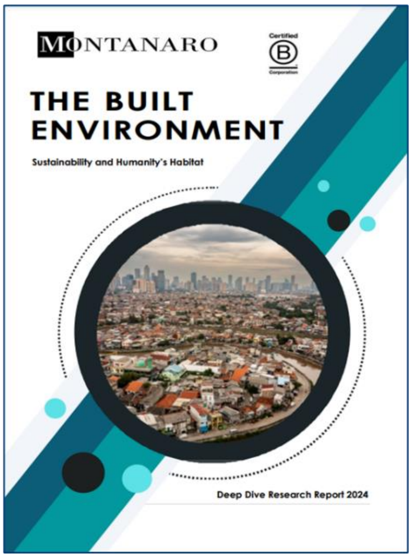
We subscribe to MSCI's ESG Ratings for companies in the MSCI World SMidCap Index. The purpose of this is to allow a comparison of our internal ESG score to a "market proxy" and understand any points of difference. We encourage our companies to complete MSCI's annual questionnaire so that their ESG profile can be understood by a wide range of stakeholders.

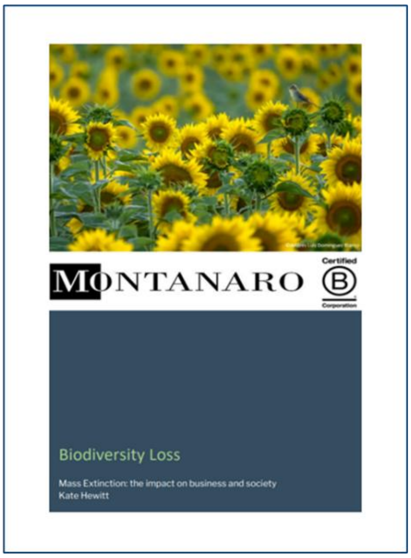
Analysts continue to update the ESG Checklist throughout the holding period as new information comes to light, for example after a set of results; the AGM; or an engagement. The Sustainability Committee monitors the ESG scores of companies on our Approved List at quarterly meetings. We aggregate company ESG scores across each of our investment portfolios to produce a total ESG Fund Score.

Our ESG Checklist helps us to set ESG priorities. In particular, they allow us to identify risks common to many of our companies. When we identify such risks, our Head of Sustainable Investments works with the Investment Team to explore the issue in greater detail via an engagement "Deep Dive".

The purpose of these Deep Dives is to engage with companies from across our Approved List and improve our understanding of a particular subject. In recent years we have conducted engagement Deep Dives on a number of topics including Supply Chain Management; Net Zero Carbon; biodiversity; and The Built Environment. Our Deep Dives can be read on our website.







Impact investing

In 2018, we launched the Montanaro Better World Fund (BWF) to invest globally in Small & MidCap companies whose products or services make a positive impact by helping to solve some of the world's greatest challenges in support of the UN Sustainable Development Goals (UN SDGs).

The investment process for the BWF is largely the same as for our other Funds in terms of the financial fundamentals and our analysis of ESG factors. In addition, however, we consider the impact of a company's products and services and their revenue alignment to six impact themes:

Our impact assessment process – **which we call Impact360°** – ensures that we target impact consistently across specific areas of the economy.

Impact360° encompasses:

- Impact screening
- Initial company research
- Completion of Montanaro Impact Profile
- Completion of Montanaro ESG Checklist
- Approval / rejection by Impact Team
- Portfolio inclusion
- Impact measurement
- Ongoing monitoring
- Engagement
- Voting

These steps create a full circle "Better World" approach to achieving impactful and sustainable change.

The foundation of Impact360° is the Fund's "Theory of Change". This describes the cause-and-effect relationship between the desired impact of an investment and the realistic expectation that this impact can be achieved. In simple terms, it involves identifying a problem (the "cause") and finding a company that can deliver a solution (the impact, or "effect").

In 2021, our Impact Team developed an "Impact Score", further developing our approach to impact investing and allowing us to better assess the spectrum of impact across the portfolio. A company must have an impact score of at least 25 (out of 50) in order to pass our Impact Criteria. This impact score was refined in 2024 to acknowledge the development of best practice and the introduction of sustainable regulation in Europe and the UK.

Annual Impact Report:

Every year, we publish an award-winning annual Impact Report detailing the progress of BWF from both an investment return and impact perspective. This is available on our website.

ESG targets

In addition to the SFDR classification of our Dublin domiciled fund range (Article 8/9) certain MAM Funds have ESG targets. These targets influence the focus of our engagement activity and are a requirement of the "Label ISR":

Montanaro Better World Fund:

- **Environmental**: at least 20% of the companies within the Fund by value to have achieved "Net Zero Carbon" by 2030
- **Social**: at least 30% of Women on Boards across the Fund by 2025
- **Governance**: at least 75% of Independent Directors across the Fund by 2025
- **Human Rights**: at least 70% of companies within the Fund reporting an Anti-Bribery Policy by 2025

Montanaro European Smaller Companies Fund:

- **Environmental**: at least a 20% reduction in carbon intensity (Scope 1 & 2) by 2025
- **Social**: at least 40% of Women on Boards across the Fund by 2025
- **Governance**: at least 70% of Independent Directors across the Fund by 2025
- **Human Rights**: at least 70% of companies within the Fund reporting an Anti-Bribery Policy by 2025

Sustainability Committee

Our Sustainability Committee is made up of experienced members from across our business. The Sustainability Committee meets formerly at least four times a year.

The Sustainability Committee is chaired by Ed Heaven, Head of Sustainable Investments, who sits on the Board of the UK Sustainable Investment & Finance Association (UKSIF). The Sustainability Committee is responsible for the following matters:

1. **Establishing MAM's Ethical, ESG and Sustainable policies:**
- Ensuring the integration of MAM's Ethical, ESG and Sustainable policies in MAM's investment process.
- Ensuring compliance of MAM's portfolios with MAM's policies and procedures.

2. **Monitoring of sustainable regulatory developments:**
- Ensuring compliance with regulations at MAM and product level.
- Monitoring of best practices in the industry.

3. **Monitoring Voting and Engagement activities**:
- Reviewing and monitoring Engagement and Voting activities to ensure alignment with relevant policies.

4. **Risk Management**:
- Identifying and managing risks related to ESG and sustainable investment practices.
- Working together with the Risk Team on ESG risk reporting.

5. **Tracking Climate Change targets**:
- Ensuring that MAM remains on track to meet its corporate and investment climate change targets and commitments.

6. **Corporate stewardship responsibilities**:
- Overseeing MAM's corporate stewardship responsibilities, including B Corporation certification, PRI membership, UK Stewardship Code signatory status and other relevant certifications and memberships.

7. **Assessment of third-party ESG and Impact service providers**:
- Monitoring of MAM's third-party ESG and Impact service providers.

8. **Charitable Programme review**:
- Reviewing and overseeing MAM's Charitable Programme to ensure alignment with MAM's values and objectives.

9. **Stakeholder Communication**:
- Ensuring effective communication with stakeholders regarding MAM's sustainable investment strategies and outcomes, including the review of MAM's ESG Handbook and online Sustainability Library.

10. **Training and Education**:
- Ensuring that Committee members and relevant staff are adequately trained and informed about ESG and sustainable investment practices.

The Sustainability Committee reports to the Executive Committee of MAM.

In 2021, we formed an internal "Net Zero Steering Group"[5] to oversee and guide our transition pathway. Responsibilities include working with environmental consultant Green Element to measure MAM's carbon footprint; the setting of interim targets; and the appraisal of different mechanisms in the market (such as carbon offset options) that may support us on our transition pathway.

The Steering Group also has responsibility for MAM's commitments under the Net Zero Asset Managers (NZAM) initiative and the work that took place to prepare our methodology for submission in 2022. In order to keep accountable in the lowering of our financed emissions, we have set climate targets and publish an annual report on our progress: "Project: Net Zero Carbon". Our latest and fourth annual report can be found on our website. Details of our action on climate is explained later in this handbook.

[5] The Net Zero Steering Group is sub-set of our Sustainability Committee

Engagement & Voting

As responsible shareholders we believe that it is our duty to engage with our investee companies where necessary. In our experience, active engagement can help to foster positive long-term change in the way businesses are run and potentially lead to better investment returns and improved societal and environmental outcomes.

Engagement forms a key part of our long-term approach, allowing us to identify and manage risks within our portfolios, fulfil our stewardship responsibilities and consider other stakeholders (a duty of all B Corps). Engagement is used as a tool to better understand a company's impact, leading to better investment decisions. Engagement is typically initiated and conducted by our Analysts as they hold the closest relationships with company management. Support is provided by the Head of Sustainable Investments and our ESG & Impact Specialists, who may lead certain cases, such as those involving multiple stakeholders, collaborative engagements, or those that affect a number of companies within a portfolio. Our internal Sustainability Committee reviews engagement activity at quarterly meetings.

Voting is a vital part of our how we exercise our stewardship responsibilities. It is a key shareholder responsibility, which is why we vote at all AGMs (where possible).

We receive independent third-party corporate governance reports and voting recommendations from Institutional Investor Services (ISS) ahead of meetings. These are used for advice only. Our Analysts systematically review all resolutions ahead of shareholder meetings and we voice our concerns where required. We aim to discuss any issues with management prior to voting against or abstaining. As such, we consider ourselves as "active" shareholders rather than "activists".

Our voting policy is applied consistently across all our Funds and Investment Trusts. Our policy is applied to segregated portfolios where we have authority to vote on our clients' behalf. If we do not have authority to vote for segregated mandates, we still share our view with our clients. We do not engage in stock lending in any of our Funds (although our segregated clients may have their own policies on this).

Our **Engagement** and **Voting** policies can be read in full on our website.

Climate change

Montanaro recognises climate change as a global crisis. We believe that every business has a responsibility to play its role in addressing this crisis.

We have targets in place for our operations and our investment portfolios. These are explained briefly below and in more detail in our "Project: 2030" report and our annual "Project: Net Zero Carbon" report.

Operational emissions:

In March 2023, we announced two new carbon targets for our business:

- **Our full Scope 1 emissions**: the emissions that we make directly, for example running our boilers and our computers.
- **Our full Scope 2 emissions**: the electricity or energy we buy for heating and cooling our single office on Threadneedle Street in London.
- **Our upstream Scope 3 emissions**: our *upstream* emissions include business travel, hotel stays, our suppliers (such as our IT suppliers). We are not including our *downstream* financed emissions i.e. the emissions associated with our investment portfolios. We explain later in this note why we have taken this approach.

Becoming **carbon negative** and **removing from the atmosphere our historical emissions** is focused on our operations. We define the following under the umbrella of "*Montanaro's Operational Emissions*":

Our aim is to reduce our operational carbon emissions, measured in absolute terms, by at least 50% by 2030, from a baseline year of 2019.

For those emissions that are harder to remove entirely – and in order to go beyond net zero – we, in 2023, entered into a three-year partnership agreement with **Klimate**, a Danish Carbon Removal Platform. Klimate provides access to high-quality, innovative, and verifiable carbon removal solutions aligned with science. Klimate's core purpose is to scale and accelerate the development of carbon removal methods and technologies needed to achieve the targets laid out in the Paris Agreement.

Portfolio emissions:

We have had the following targets in place across our Portfolios since joining the NZAM initiative in 2019:

- To see a **50% reduction in portfolio emissions by 2030**, relative to 2019 base levels.
- That **50% of the designated AUM will have implemented a Science Based Target by 2030, increasing to 100% of AUM by 2040**.
- To have achieved **Net Zero Carbon by 2050** across our in scope portfolios.

Since 2019, a major engagement effort has been in place as we have sought to use our influence as shareholders to facilitate change among our companies. We have called this "Project: Net Zero Carbon". Its purpose has been to encourage companies to take measures to reduce their carbon footprint by setting net zero targets; implementing strategies to deliver on these targets; and adopting both approved and verified SBTs.

Our ESG Library

Deep Dive Engagement reports:

- **Deep Dive #11**: Project Net Zero Carbon 2023
- **Deep Dive #10**: The Built Environment
- **Deep Dive #9**: Waitaki Hydropower Scheme
- **Deep Dive#8**: Project Net Zero Carbon 2022
- **Deep Dive #7**: Biodiversity Loss
- **Deep Dive #6**: Data Centres
- **Deep Dive #5**: Project Net Zero Carbon 2021
- **Deep Dive #4**: Plastic Fantastic
- **Deep Dive #3**: Project Net Zero Carbon 2020
- **Deep Dive #2**: The Biomass Debate
- **Deep Dive #1:** Supply Chain Investigation

UK Stewardship Code:

- UK Stewardship Code 2022
-

Climate Change:

- Climate Change Policy
- Carbon Targets: Methodology

UN PRI reports:

- 2023 – Assessment Report
- 2023 – Transparency Report
- 2021
- 2020
- 2019
- 2018
- 2017

Voting:

- Voting policy
- Proxy Voting Summary 2023
- Proxy Voting Summary 2022
- Proxy Voting Summary 2021
- Proxy Voting Summary 2020
- Proxy Voting Summary 2019
- Proxy Voting Summary 2018

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