



A S S E T   M A N A G E M E N T

## ESG HANDBOOK

*Responsible Investing at Montanaro*

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Certified



Corporation

## Welcome to Montanaro!

*This document is designed to tell you everything about our Ethical & ESG Philosophy & Process:  
why we think Ethics & ESG is important;  
why Ethics & ESG forms a natural part of our “Quality” approach;  
how we integrate Ethical & ESG analysis into our investment process;  
and why being Responsible Investors is integral to our role as long-term shareholders.*

**Certified**



**Corporation**

**This company meets the  
highest standards of social  
and environmental impact**

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## 1 - ABOUT MONTANARO

### A bit about us...

Montanaro was established in 1991. We have the largest and most experienced specialist team in Europe dedicated exclusively to researching and investing in Global quoted Small & MidCap companies. Our team of 34 is multi-lingual and multi-national (with no less than ten nationalities). This ensures that we have the benefit of local contacts and knowledge that is so essential to detailed and thorough research.

As of 31 December 2021, Montanaro's funds under management were approximately £4 billion. Our clients are mainly leading international financial institutions (insurance companies, pension funds, local authorities, endowments, family offices, universities, charities and fund of fund managers).

Many of these institutions sit at the centre of the sustainability revolution, requiring ESG considerations to be fully imbedded into the investment of their assets. We manage segregated mandates for a number of institutions which have specific ESG requirements.

We manage a total of 9 open-ended Funds, 2 closed-ended, listed Investment Trusts and several segregated mandates. Investors seeking exposure to Global Small & MidCap can choose from Montanaro's wide range of actively managed products:

- **Vehicle:** we manage open-end funds with a variety of share classes (Sterling, Euro, US Dollar, SEK, Accumulation/Distribution, Retail/Institutional shares), closed-end funds and segregated mandates;
- **Domicile:** we have a Dublin Fund range and a UK domiciled Fund range;
- **Geography:** we manage Global, Pan-European, Continental Europe (ex-UK) and UK only products;
- **Strategy:** we offer capital growth, income and global impact strategies;

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### Our investment approach

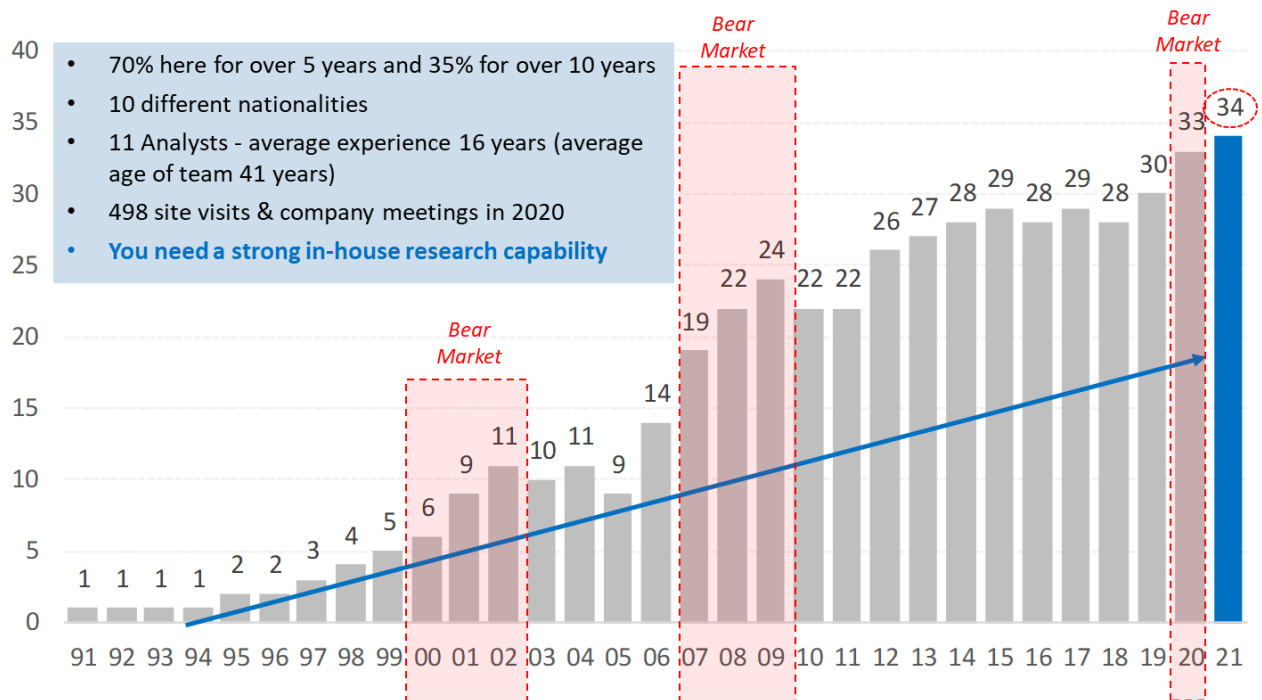
We are **"Quality Growth"** investors. We take a common sense approach to investing, identifying the highest quality companies with the best management teams that we can hold for the long term.

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 over the long term.

## Our team

<b>INVESTMENT Committee</b> Charles Montanaro (Chairman) Mark Rogers George Cooke + PMs		<b>Charles Montanaro</b> Chairman of the Board / PM	<b>SUSTAINABILITY Committee</b> Christian Albuissou (Chairman) Ed Heaven (Deputy Chairman) Cedric Durant des Aulnois Mark Rogers Nere Asumendi Kate Hewitt / Sarah Bridges	
<b>INVESTMENTS</b> <b>Mark Rogers</b> Head of Investments / PM		<b>CLIENT RELATIONS</b> <b>Tom Norman-Butler</b> Head of Business Development		<b>COMPLIANCE &amp; ADMINISTRATION</b> <b>Matthew Francis</b> Head of Compliance, Risk & Administration / Compliance Officer
<b>Ed Heaven</b> Head of Sustainable Investment	<b>George Cooke</b> Head of Fund Management / PM	<b>Chris Crier</b> UK IFAs (North)	<b>Christian Albuissou</b> France, Benelux, Spain, Scotland	<b>John Ensor</b> Client reporting / Admin. Manager
<b>Andrea Shen</b> Analyst / PM	<b>Alex Magni</b> Analyst / PM	<b>Adam Lomas</b> UK IFAs (South)	<b>Henrik Schmidt</b> Nordics	<b>Aaron Gomez</b> Trade Execution / Fund Administrator
<b>Guido Dacie-Lombardo</b> Analyst / PM	<b>Stefan Fischerfeier</b> Analyst / PM	<b>Grace Applegate</b> Marketing Assistant	<b>Harry Fitzgerald</b> UK Wealth Managers	<b>Dimitris Giakis</b> Fund Administrator
<b>Nere Asumendi</b> Senior Analyst	<b>Henrik Schmidt</b> Senior Analyst	<b>RISK</b> <b>Bill Jiang</b> Head of Investment Analytics		<b>Sarah Bridges</b> Compliance Manager
<b>Gaspar Arino</b> Senior Analyst	<b>Hal Miller</b> Analyst	<b>IT &amp; SYSTEMS</b> <b>Mark Petar</b> Head of Systems		<b>Lowri Brown</b> Office Manager / PA to the Chairman
<b>Yannis Gidopoulos</b> Analyst	<b>Kate Hewitt</b> ESG & Impact Specialist	<b>FINANCE</b> <b>Gillian Edwardes-Ker</b> Senior Finance Manager		<b>Karis Rose</b> Assistant to the Office Manager

The team has grown steadily over the years:



## 2 - OUR COMMITMENT TO ESG

### Being Responsible Investors

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 Responsible 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.

Research (see appendix) 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 certified UN PRI signatory and has been awarded the “Label ISR” (SRI label) by the French Ministry of Finance.

### Sustainability is part of our investment DNA

It forms an integral part of how we think, behave and invest. ESG was first included in our investment process over 15 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 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 engaging 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 Public Commitments

#### **Certified B Corporation:**

- Montanaro became a certified B Corporation in [June 2019](#)



#### **The UN Principles for Responsible Investment (PRI): 2009**



- An international network of investors working together to put six Principles for Responsible Investment into practice
- Principle 1: *"We will incorporate ESG issues into investment analysis"*

#### **The Stewardship Code (Tier 1 Rating): 2010**



- *"Investors in the company...play an important role in holding the board to account for the fulfilment of its responsibilities".*

#### **The Carbon Disclosure Project (CDP): 2015**



- *"CDP has incentivised...companies...to measure and disclose their environmental information".*

#### **Net Zero Asset Managers Initiative: 2021**

#### **Our Funds and Investment Process have been endorsed externally:**

##### **Better World Fund Awarded 5 Star Rating by 3D Investing**

- specialist UK ESG Ratings Company: over 200 Funds rated
- only 6 Equity Funds have been awarded a 5 Star Rating



##### **Better World Fund awarded leading SRI label**

- awarded by the Finance Ministry after extensive due diligence to recognise "best-in-class" SRI products in Europe
- only two Funds rated in the UK



#### **Montanaro are proud to have been recognised for our excellence in the field of ESG:**

- 2019: **Winner Best Impact Fund**, Investment Week Sustainable & ESG Investment Awards
- 2019: **Winner Best Impact Report**, Pensions for Purpose
- 2020: **Highly Commended Best Impact Fund**, Investment Week Sustainable & ESG Investment Awards

### 3 - ETHICAL & ESG POLICIES

Companies that we consider for investment must pass the criteria set out in the following policies. Each policy has a corresponding checklist which our Analysts complete during the research process. The Ethics and ESG criteria that we highlight below forms form an intrinsic part of Montanaro's assessment of a company's "Quality".

#### 1. ETHICAL POLICY – our Ethical Exclusions apply across the house

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Investors occupy a position of immense responsibility as they direct capital flows across economies. As such, investors should consider the ethical value (either good or bad) of a company's products, services, and wider operations. By doing this, investors can aid the development of economic systems that benefit all stakeholders.

While our primary fiduciary duty is to maximise investment returns for our clients, attractive returns and sound ethical considerations are not mutually exclusive. We strongly believe that it is possible to have the best of both worlds and "*do well by doing good*"<sup>1</sup>.

##### **Ethical Policy:**

Investors occupy a position of immense responsibility as they direct capital flows across economies. As such, investors should consider the ethical value (either good or bad) of a company's products, services and wider operations. By doing this, investors can aid the development of economic systems that benefit all stakeholders. On ethical grounds, we do not invest in the following areas of the economy. We exclude from investment any company which derives 10% or more revenue from these areas:

- Exploration & production fossil fuels;
- Tobacco producers & distributors;
- Alcohol producers & distributors;
- Controversial weapons;
- Gambling;
- Pornography;
- High Interest rate lending;
- Animal testing (unless it is required by law for healthcare related companies).

##### **The areas that we ban from our investment universe are explained below:**

##### **Exploration & production fossil fuels:**

**Coal:** We formally exclude coal extraction & production companies from our investment universe. In CO<sub>2</sub> terms, coal is the most polluting energy industry. Thermal coal remains an inefficient way to generate energy<sup>2</sup>. Companies that are heavily involved in these operations are "*unlikely to be able*

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<sup>1</sup> *The Market for Virtue: The Potential and Limits of Corporate Social Responsibility*, David Vogel, p.19

<sup>2</sup> <http://www.c2es.org/energy/source/coal>



*to assist with the transition to a low carbon economy<sup>3</sup>". A coal power station produces twice the carbon dioxide per unit of energy relative to a gas powered one<sup>4</sup>.*

**Oil:** We formally exclude oil exploration & production companies from our investment universe. We do not wish to direct capital towards companies developing new sites. In addition we make the following points:

- Tar Sands: we recognise that certain forms of oil production are worse than others. As a group of Canadian scientists have argued<sup>5</sup>, the recent proliferation of tar sands appears incompatible with climate protection initiatives.
- Oil Services: we will invest in certain oil service companies, particularly those whose products and services help to reduce the environmental impact of oil production.

**Gas:** We formally exclude gas exploration & production companies from our investment universe. However, it must be noted that gas can play a role in the energy mix transition. Replacing coal with gas can yield a substantial decrease in greenhouse gas emissions. The UK is a good example of this, where declining coal use in favour of a blend of gas, wind and solar has pushed UK carbon emissions to levels last seen in 1890. Nevertheless, we recognise that gas still has a net negative environmental impact, in part due to the high level of methane released<sup>6</sup>. The CO<sub>2</sub>E of gas based equivalents should be considered by investors.

#### **Tobacco:**

We do not invest in tobacco producers and distributors. This includes companies involved in the manufacture and distribution of vaping or e-cigarette products. Smoking causes the largest number of avoidable deaths in Europe on an annual basis<sup>7</sup>. Across the world, tobacco use kills 6 million people each year with nearly 80% of those deaths in low and middle-income countries. Tobacco use caused 100 million deaths worldwide during the 20th century. If current trends continue, it will kill 1 billion people in the 21st century<sup>8</sup>. We see no case for justifying investing in an industry that knowingly causes so much harm and distress to so many often disadvantaged people.

#### **Alcohol:**

We do not invest in alcohol producers and distributors. Across society, alcohol causes immense harm. In the European Union, alcohol-attributable disease, injury and violence costs the health, welfare, employment and criminal justice sectors some €125 billion a year<sup>9</sup>. The UK Department of Health<sup>10</sup> estimates that 10 million adults drink more than the recommended alcohol consumption limits. A cause of concern is that alcohol companies do not differentiate between responsible drinkers and those who misuse alcohol and show limited attempts at controlling underage drinking.

#### **Controversial Weapons:**

We do not invest in controversial weapons manufacturers. This includes weapons such as anti-personnel mines, cluster munitions, chemical & biological weapons and companies involved in the production, supply or storage of weapons grade nuclear fissile materials. We also do not invest in

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<sup>3</sup> <https://www.churchofengland.org/media/2235218/climate%20change%20policy%2030%2004%2015.pdf>

<sup>4</sup> <http://www.eiris.org/blog/fossil-fuels-logic-divestment/>

<sup>5</sup> <http://www.oilsandsmoratorium.org/>

<sup>6</sup> <http://www.sciencemag.org/news/2018/06/natural-gas-could-warm-planet-much-coal-short-term>

<sup>7</sup> [http://europa.eu/pol/pdf/flipbook/en/public\\_health\\_en.pdf](http://europa.eu/pol/pdf/flipbook/en/public_health_en.pdf)

<sup>8</sup> <http://www.tobaccoatlas.org>

<sup>9</sup> [http://ec.europa.eu/health/archive/ph\\_determinants/life\\_style/alcohol/documents/alcohol\\_europe\\_en.pdf](http://ec.europa.eu/health/archive/ph_determinants/life_style/alcohol/documents/alcohol_europe_en.pdf)

<sup>10</sup> <https://www.gov.uk/government/organisations/department-of-health>

companies that make or sell civilian handguns. Our ban on these is total and in line with our obligations under the United Nations Principles for Responsible Investment<sup>11</sup>. In the Better World Fund we go further and ban any investment in military companies.

#### **Gambling:**

We do not invest in gambling companies. All forms of gambling have the potential to lead to destructive addiction. Academic studies suggest that the social effect of gambling is worse for those from economically disadvantaged communities<sup>12</sup>. Gambling has been linked to increases in domestic abuse as well as alcohol and drug addiction.

#### **Adult Entertainment (pornography):**

We ban investment in companies that produce and distribute pornography (including magazines, newspapers, videos, films, websites and related software) as well as any companies involved in the staging of live sex shows or the ownership of sex shops. We use guidance from the Church of England to define pornography as *"the sexually explicit depiction of persons, in words or images, created with the primary, proximate aim, and reasonable hope, of eliciting significant sexual arousal on the part of the consumer"*<sup>13</sup>. Porn has been linked to social exploitation, particularly of vulnerable women, and has been negatively linked to behavioural and mental health conditions.

#### **High Interest Rate Lending:**

Pay-day lending companies are a contentious area for investors. On the one hand, they are deemed unethical, preying on the most vulnerable by charging exorbitant rates of interest. On the other, they are seen as a necessary part of the credit market, servicing customers who have been priced out of accessing loans by banks and credit card companies<sup>14</sup>. Despite the debate, in our view the scales fall in favour of a total exclusion of payday loan companies. We use the Church of England's definition of a pay-day lending which is as follows: *"Any company, whose main business activity or focus is the provision of home-collected credit ('doorstep lending'), unsecured short-term loans ('payday loans') or pawnbroker loans, directly or through owned-subsidaries...Typical indicators of potentially exploitative lending will be triple-digit, or close to triple-digit, Annual Percentage Rates (APRs); short loan term durations (less than 18 months);and no requirement for security"*<sup>15</sup>.

#### **Animal Testing:**

Montanaro does not invest in companies that use animal testing for purposes other than healthcare research. The only exception to this policy is when animal testing is required by law and alternative tests are not permissible. In such cases the company in question must have a clear animal testing policy, compliant with "The Three Rs":

1. **Replacement:** methods which avoid or replace the use of animals in research;
2. **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;
3. **Refinement:** use of methods that alleviate or minimise potential pain, suffering or distress, and enhance animal welfare for the animals used.

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<sup>11</sup> <http://www.unpri.org/>

<sup>12</sup> *Research on the Social Impacts of Gambling*, Scottish Executive, University of Glasgow pg. 42-63

<sup>13</sup> <https://www.churchofengland.org/media/1376293/pornography%20policy%20nov%202011.pdf>

<sup>14</sup> <http://www.adamsmith.org/blog/regulation-industry/wonga-post/>

<sup>15</sup> <https://www.churchofengland.org/sites/default/files/2017-11/High%20Interest%20Lending%20Policy.pdf>

## 2. ENVIRONMENTAL POLICY

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Our Environmental Policy helps us to identify the highest quality companies by guiding us towards truly sustainable investment opportunities. The areas that we focus on are influenced by and support the UN Global Compact.

Via our Environmental Checklist, we assess the risks and opportunities that our companies face from an environmental perspective. By analysing specific areas of environmental and social concern, our companies are encouraged to foster a long-term focus in their business. Our approach helps to drive more accurate risk analysis, helping us to invest companies well-placed to deliver sustainable returns in a changing world. Our Checklist allow us to score companies on their environmental profile and identify issues on which to engage.

We consider specific areas of environmental exposure in our analysis:

- Environmental intensity: how much carbon, water and waste is produced/consumed by our companies?
- Stranded asset risk: how exposed are our companies to unanticipated or premature write-downs of assets?
- Reporting: which companies are failing to report quality environmental data?
- Climate change: which of our companies have taken steps to materially reduce their carbon footprint?

We use MSCI, Bloomberg and company sourced data to measure the environmental intensity of our companies across carbon, water and waste. Where available, we record the carbon intensity of companies across Scopes 1, 2 and 3 on the basis of tonnes of carbon used per million US Dollars of sales generated. We do the same for water and waste. This allows us to compare the carbon intensity of companies across our Approved List.

We also monitor MSCI's Low Carbon Transition score. This combines Management assessments for the following issues: Carbon Emission for all companies; Product Carbon Footprint; Financing Environmental Impact; Opportunities in Clean Tech; and Opportunities in Renewable Energy where available. A score is given from 0-10. Higher scores indicate greater capacity to manage risk.

In addition to the above, we record MSCI's Low Carbon Transition score. Companies with higher Low Carbon Transition score are more aligned with the Low Carbon Transition compared to the companies with lower scores. A score is given from 0-10.

We also assess environmental management culture (in accordance with UN Global Compact Principles 7-9); supply chain management; and the extent to which a company's products/services are a positive influence on the environment. We also record whether a company's operations are certified by a national or global standard (e.g. ISO 14001).

Finally, we consider the quality of a company's environmental reporting and if they have a Net Zero Carbon target or other environmental targets in place. Companies are scored out of 10 for their environmental profile on our Environmental Checklist.

## 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’.”*<sup>16</sup>

**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.

**With this in mind, our stance can be summarised as follows:**

1. We ban investments in oil, coal, and gas exploration & production companies;
2. To halt and mitigate the effects of climate change, fossil fuels must be kept in the ground;
3. Despite the development of new technologies, the transition to a cleaner energy mix will take time;
4. For now, investing further down the energy value chain is permissible given fossil fuels are likely to be a feature of our world for many years to come;
5. Investment is needed in carbon capture and more efficient storage technologies;
6. All companies have a role to play in the energy transition: we support companies who take steps to reduce their own energy consumption and apply 100% renewable or Net Zero Energy targets, or Science Based Targeting.
7. In July 2018, our Better World Fund set an ambitious target that by 2025, at least 10% of companies within Fund by value will have achieved “Net Zero Carbon”. We have initiated this project in conjunction with asset owners and the UK Climate Impacts Programme at the University of Oxford.

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<sup>16</sup> From speech by Philip Lambert, CEO, Lambert Energy Advisory - *FT Energy Transition Strategies Summit, London, 14th June, 2018*

We have developed an Energy Transition Table (below) to illustrate how we view different areas of energy production. This enables us assess where an energy company sits within the energy matrix.

Energy Transition Table						
Energy Source	Stage 1	Stage 2	Stage 3	Stage 4	Stage 5	Consumers
Coal	Extraction & Transport	Power Station Investment	Electricity Generation	Grid Investment	Utilities & Wholesale	
Oil	E & P Exploration & Transport	Upstream Refining	Chemical Production	Engineering	Auto Industry Consumer products Industrial products	
Gas	E & P Exploration & Transport	Storage Technology	Power Station Investment	Electricity Generation	Utilities & Wholesale	
Nuclear	Fuel extraction	Power Station Investment	Electricity Generation & spent fuel storage	Utilities & Wholesale	Retail & Industrial	
Renewables	Land Availability	Production Engineering	Production Materials	Electricity Generation & Storage	Grid Access	
Quoted Companies	Multiple of operators from mining, oil & gas, chemical refining, chemical/electrical/mechanical engineering, utilities, auto, consumer					

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. While renewable energy has increased as part of Germany's energy mix, 40% of the country's electricity is generated from hard coal and lignite. 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<sup>17</sup>.

#### Renewables:

The World Energy Council notes that *"the rate of improvements towards cleaner energy is far slower than required to meet emissions targets"*. Solar and Wind currently account for just 8% of energy produced. Clearly 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

<sup>17</sup> <https://www.ucsusa.org/nuclear-power/cost-nuclear-power#.W2K2YLgna71>

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. Companies that have a publicly stated “Net Zero Energy” goal should be applauded. Such 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. With the carbon budget in mind, we encourage companies to sign up implement Science Based Targets. These can help investors to best contextualise a company’s energy usage.

**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. We also encourage our companies to consider joining the RE100 club, a network of companies committed to 100% renewable power.

**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<sup>18</sup>”*. We encourage companies to continue improving their levels of environmental reporting.

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## 2. SOCIAL POLICY

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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.

We use MSCI, Bloomberg and company sourced data to measure and record the following:

- % Employee Turnover;
- % Women in Workforce;
- % Women in Management;
- Gender Pay Gap Breakout;
- Company 5-year tax rate;
- Underlying tax rate;
- Estimated Tax Gap;
- Social tax rating.

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<sup>18</sup> <https://www.unglobalcompact.org/issues/environment/>



Additional areas that we focus on include: Human rights; Bribery & Corruption; Equal Opportunities; Labour Practices; Human Resources & Training; Supply chain management.

Companies are scored out of 10 for their social profile on our Social Checklist.

### **3. CORPORATE GOVERNANCE POLICY – Linking governance to financial fundamentals**

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We wish to align the interests of company management teams with the interests of long-term shareholders. Ensuring high standards of corporate governance forms an important part of this. Our logic here is simple: good corporate governance increases the quality of a business; the higher the quality of a business, the greater the sustainability of returns.

#### **Our Checklist considers:**

- Remuneration of the Executive Board;
- Capital Allocation Record;
- Board Independence;
- Board Ownership;
- Board Diversity.

#### **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.

We receive independent third party corporate governance reports and voting recommendations from Institutional Investor Services ISS ahead of meetings, however we use these 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”.



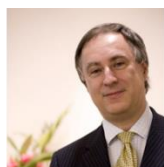
## 4 - Sustainability COMMITTEE

Our Sustainability Committee is made up of experienced members from across our business. Their primary responsibility is to ensure that Montanaro's ESG effort remains coordinated across the house. The Sustainability Committee meets officially on a quarterly basis. Meetings have a set agenda:

1. Review of previous minutes and action points
2. Review of engagement activity
3. ESG engagement with clients
4. Client reporting (ensuring that institutional client demands are managed appropriately)
5. Review of ESG within the Investment Process
6. ESG seminars / events attended / training required
7. Latest developments of ESG standards & guidelines and their implications
8. Long-term ESG objectives for Montanaro

In addition, the Sustainability Committee assesses and votes on the impact credentials of potential investments for The Better World Fund. A company cannot be invested in within the Better World Fund unless the Committee has approved it for impact.

### Our Sustainability Committee:



**Christian Albuisson**  
CHAIRMAN



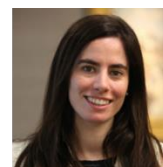
**Ed Heaven**  
HEAD OF SUSTAINABLE  
INVESTMENT



**Cedric Durant  
des Aulnois**  
CEO



**Mark Rogers**  
HEAD OF INVESTMENTS



**Nere Asumendi**  
SENIOR ANALYST



**Sarah Bridges**  
COMPLIANCE ANALYST

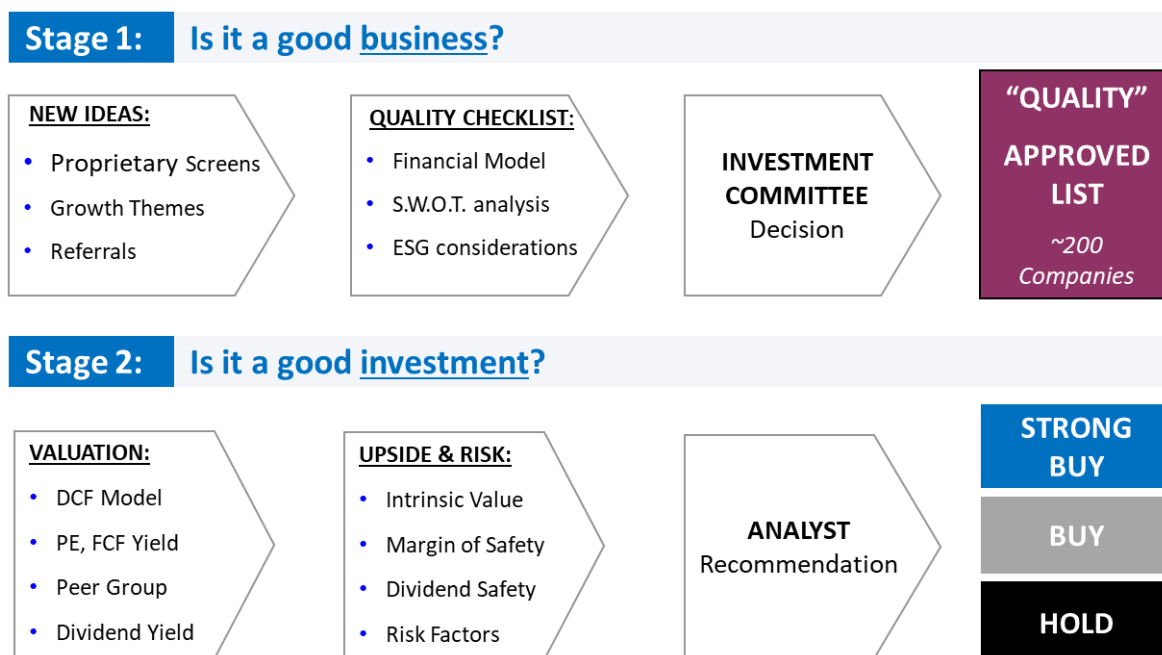
#### The Sustainability Committee:

- reviews, challenges and debates every impact report submitted by our Analysts;
- has rejected c.20% of companies on impact grounds.

**We do not invest in companies that fail on impact**

## 5 – ESG IN THE INVESTMENT PROCESS

The following investment process is applicable to all of our Funds, although the Better World Fund has an additional “impact” stage which is explained in the Impact section of this handbook.



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?**”. If the answer is “No” then we stop there.

Once an idea has been identified, the Analyst will spend several days analysing the business, its industry and articulating the investment case. The Analyst will complete Quality and ESG Checklists as well as a Financial Model. If the Analyst is confident that this is a good business that we should own for the next 10 plus years, they will present it to the six person Investment Committee which decides whether it should be added to our “Approved List”. Only companies that have been formally approved (there are c.200 currently) are available for investment.

The **second stage** of the process focuses on answering the question: “**Is it a good investment?**”.

Having established that a company meets Montanaro’s “Quality” criteria, the Analyst then conducts valuation work using a proprietary DCF model to work out the intrinsic value of the business.

Once this is completed, the Analyst will produce a Target Price for the share of equity. Alongside this, an official recommendation (STRONG BUY / BUY / HOLD) is placed on the stock, reflecting Analyst conviction. These are subject to change, based on company performance and market conditions.

Finally, we meet management typically twice a year and always visit the operations of our companies, wherever they are located in the world. These site visits helps us to “kick the tyres” by seeing the operations of the company with our own eyes and meeting other members of staff. Analysts prepare detailed questions in advance of meetings and site visits, which enables us to set

the agenda and get the most out of our time with the company. Site visits are labour intensive but add considerable value. These face-to-face meetings are excellent opportunities to raise any concerns we may have about ESG.

### How we use our ESG Checklists:

Scores for each ESG area weighted and then aggregated to produce a final ESG score out of 10. We weight the Corporate Governance section of our checklist higher than Environmental and Social as we believe management are ultimately responsible for a company's approach to ESG. The summary section of our ESG Checklist is shown below:

MONTANARO ETHICS & ESG CHECKLISTS			
SUMMARY			
	Score	% Weight	General Comment / Key Issues
ETHICS	Pass	/	The company has a very poor score on its Environmental Checklist. The company publishes very little data on its environmental footprint and does not publicly disclose its approach to environmental matters. We need to arrange an engagement with management to understand why disclosure in this area is so poor.
ENVIRONMENTAL (1 to 10)	2.0	30%	
SOCIAL (1 to 10)	6.0	30%	
CORPORATE GOVERNANCE (1 to 10)	6.0	40%	
ESG Score (1 to 10)	4.8	100%	
ESG Rating	REVIEW		
Engagement Required?	YES		

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 "Review" (as shown above) meaning that engagement is required if we wish to invest in the company.

Analysts continue to update the ESG Checklists 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 to understand how Analysts are scoring companies.

Our clients have long-term time horizons (five years plus) and our approach to ESG reflects this long-term commitment. As a result, we are happy to invest in a company with a weakness in its ESG profile so long as management express a willingness to engage with us and a desire to improve areas of weakness. These checklists have led to engagements that have resulted in better conviction in the investment case and also decisions to sell stocks, for example:

- **Increased conviction:** The Environmental reporting of a Swedish company we invested in was notably poor, with little detail given on Scope 1, 2 or 3 emissions. After engaging with the CEO of the company, we encouraged them to sign up to the Science Based Targets Initiative in support of the CDP Science Based Targets Campaign. The company has done this and delivered an improved Sustainability Report with a greater level of reported environmental data. This allowed our Analyst to increase the Environmental Checklist score and increased our confidence in the investment case.

- **Reduced conviction:** We spoke to a company listed in Hong Kong about their plans to transition to a less carbon intensive business model following the completion of the company's ESG Checklist. Management informed us that they are unlikely to set any environmentally linked targets for their business as there is little incentive from the Chinese government for them to do this. Coupled with some concerns about the ownership structure that were flagged by the Analyst in the Corporate Governance Checklist, we decided to sell our holding.

**Our ESG Checklists also help 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 Investments and Head of Sustainable Investment works with the 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 risk and the quality of our analysis. In recent years we have conducted engagement Deep Dives on:

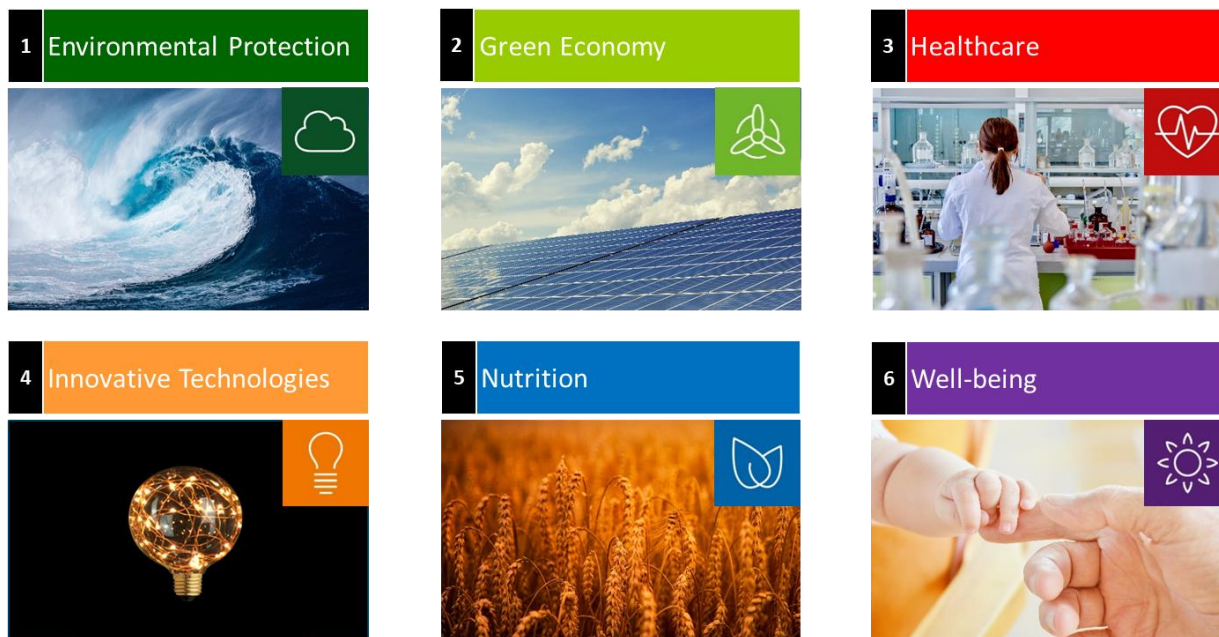
- **Nutrition:** our consumer Analysts wanted to better understand how food companies were responding to healthy eating trends and government regulation on unhealthy foods;
- **Supply Chain Management:** we noticed that the management of supply chains was frequently a low scoring area on our ESG Checklists. Analysts indicated that low supply chain visibility was one reason scores in this area were low. We engaged with a number of companies in order to better understand how companies were approaching supply chain management. This improved our analysis of this area, allowing us to identify best and worst supply chain management practice.

Our Deep Dive reports are available on Montanaro's website. A detailed explanation of our ESG Policies and Checklists is contained within our ESG Handbook, which is also available on our website.

## 6 – IMPACT INVESTING

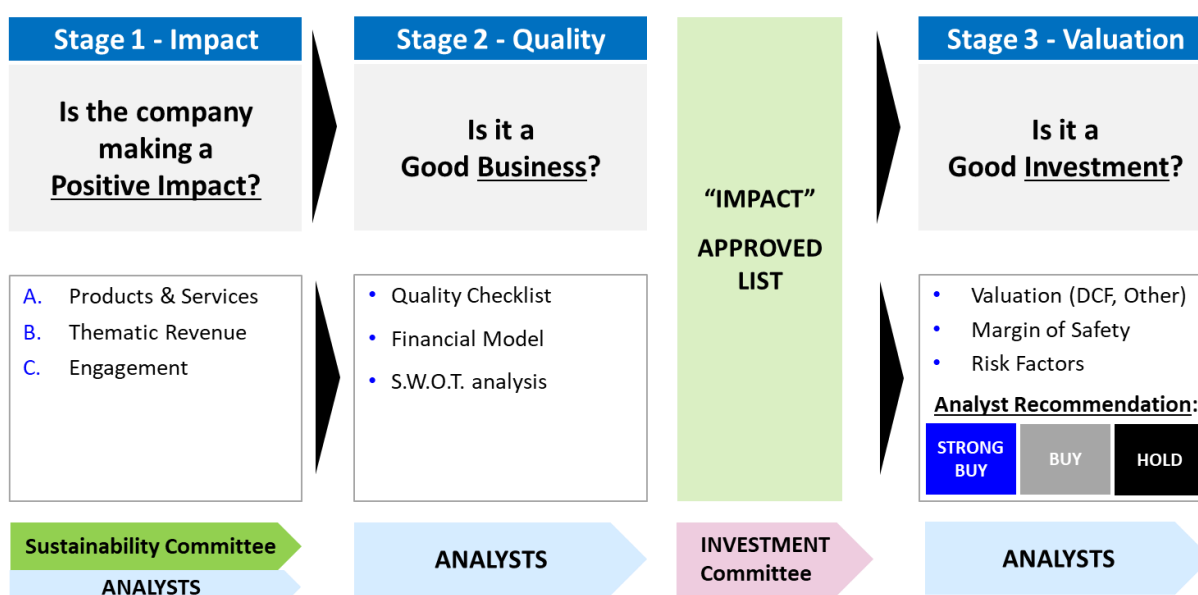
In April 2018, we launched the [Montanaro Better World Fund](#).

The Montanaro Better World Fund invests 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. Companies within the Fund are aligned to six themes:



### Impact Investment Process:

The investment process for the Better World Fund is largely the same as for our other Funds. We are interested in assessing the Quality of a company (Stage 2) and the valuation of the investment (Stage 3). However, "Stage 1" is unique to the Better World Fund and considers impact:



## Stage 1:

Analysts complete an “Impact Report” for every company that we consider for investment. The graphic below provides a summary of what we include in these reports.

A) Products / services	B) Thematic revenue	C) Engagement
<ul style="list-style-type: none"> <li>• What product / service does the company offer?</li> <li>• What problem does this help to solve?</li> <li>• Key Performance Indicator</li> <li>• Intentionality</li> <li>• Additionality</li> <li>• Affordability</li> <li>• Reporting</li> </ul>	<ul style="list-style-type: none"> <li>• Is at least 50% of revenue attributable to our themes?</li> <li>• UN SDG alignment</li> </ul> 	<ul style="list-style-type: none"> <li>• What is the engagement opportunity?</li> <li>• Are there any areas of concern / weakness?</li> <li>• Are management willing to engage?</li> <li>• What is the engagement timeline?</li> </ul>

### A) Products / services:

Analysts consider how the company’s products or services have the potential to deliver a positive impact by understanding the specific problem the company is helping to address. We attempt to identify key performance indicators to allow us to measure the impact of the company over time. We also seek to understand:

- Intentionality: are management operating the company with a purpose to deliver impact?
- Additionality: is the company providing a new product or service, or delivering an existing product in new ways, perhaps via a new technology that is better for the environment, or into a new geography?
- Affordability: are the products/services affordable to a large market, ideally including underserved people?
- Reporting: we consider the quality of company reports. Do they disclose the impact of their business in a form that recognises both the positive and negative impacts of their business?

### B) Thematic Revenue:

Analysts attribute company revenue against the Fund’s 6 themes, where appropriate. We will only invest in companies with revenue of alignment of at least 50%.

### C) Engagement:

Engagement offers a potential avenue for the delivery of impact. We believe that the Small & MidCap markets are particularly attractive for engagement as shareholders have a louder voice and we have access to the decision-makers. Management teams recognise Montanaro as long-term shareholders and we are known for our patient approach to engagement and our focus on making improvements that stand the test of time.



**ESG analysis & targets:**

Companies within the Better World Fund must also demonstrate high standards of ESG and pass our Ethics and ESG Checklists.

In addition, we have set out certain **ESG and Human Rights targets** that the strategy is aiming to achieve:

- **Environmental:** at least 10% 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.

**Reporting:**

We publish an annual **Impact Report** detailing the progress of the portfolio from both an investment return and impact perspective. The report, which is publicly available on our website, provides a detailed explanation of how the Better World Fund aims to achieve impact, with detail analysis of the Portfolio’s contribution to the impact objectives of the Fund:



We were delighted that our Impact Report won an award from **Pensions for Purpose in 2019 for Best ESG & Impact Report:**



## 7 – ENGAGEMENT

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.

### How we engage

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There are a number of channels open to us when we seek to engage with a company. These include:

- Direct engagement with the management and /or Board;
- Speaking to industry competitors;
- Speaking with industry representatives such as Trade Unions;
- Liaising with other shareholders;

### Engagement process

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Our engagement process can be summarised as follows:

1. Issue source: we can become aware of issues that require engagement through a number of sources. Our Ethical & ESG Checklists are a primary source as they force our Analysts to “score” a company on Ethical & ESG grounds. A low score in a particular area often suggests that engagement of some kind is needed. Company meetings and site visits also provide us with an opportunity to discover whether an issue exists that requires engagement. In addition to this we also monitor company newsflow, through the information provider Factiva as well as more mainstream news sources.
2. Deciding to engage: if an Analyst (or any other member of Montanaro’s staff) feels that engagement is needed with a company, the relevant Analyst will discuss the issue with the Sustainability Committee at an ad hoc meeting, or via email. They will agree on which of the Engagement Channels to pursue given the case details and the Analyst will then go ahead and engage.
3. Recording engagement: all engagement activity is recorded on Montanaro’s ESG Engagement Log. Any activity is deemed to be “ongoing” until formally closed. It is the responsibility of the Sustainability Committee to review this Log at each meeting to monitor progress and discuss priorities.
4. Monitoring engagement: once we have initiated engagement with a company the Analyst and Sustainability Committee – supported by other members of the Investment Team, such as the Head of Research – monitor the company’s response. This can go a number of ways:
  - The company responds promptly and assuages our concerns and/or provides material evidence to prove that they are going to solve the issue at hand.
  - The company responds promptly but we are not satisfied by their answer. We engage further. In some cases we may speak to competitors of the company to better understand the industry, or an industry body, such as a Trade Union or discuss the matter at a shareholders forum.



- The company does not respond, so our Analyst engages again with management. In some cases we may choose to escalate the matter to another member of the company's senior management team in an effort to garner a response.
  - The company does not respond and appears unlikely to do so, so we liaise with industry bodies or other shareholders in order to gain further support for our cause, or better understand the situation.
5. Reaching a conclusion: in an ideal world we wish to reach a positive conclusion on every matter of engagement. Our single aim when we engage with companies is to encourage an improvement in behaviour that leads to more sustainable business practices. We are realistic, however; engagement is often a complex business in itself. We do not place a deadline on engagement as in our experience, complex issues can take time to resolve. As long-term shareholders, our focus is on ensuring the improvement of a company's performance over a long time period. However, if our engagement subsequently leads us to doubt the longer term attraction of an investment, that investment will be reviewed and could be sold.

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## **Escalation**

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Our escalation strategy falls into two parts:

**Internal:** If an Analyst fails to get satisfactory answers to an engagement matter, then they will discuss the next steps with: the Head of Research; then the Sustainability Committee; then the Investment Committee (if for example the Analyst is recommending that the stock should be sold).

**External:** With the company, we may escalate matters up the corporate hierarchy. For example, if our first point of contact has been the Head of Investor Relations, then we may ask to speak to a member of the Executive Team (typically the CEO or CFO). If they prove unresponsive, then we will seek to speak with members of the Board (such as the Chair or Chair of the Remuneration Committee). In the world of SmallCap, many companies remain owned by the founder, or family members of the founder. We have experience of escalating matters with companies which have resulted in meetings with family shareholders who have not, or do not usually, meet with minority shareholders. In some instance we will also escalate matters more widely, either by speaking to industry bodies or other shareholders.

**8 – UK STEWARDSHIP CODE****Summary:****We have been awarded a Tier 1 rating for our UK Stewardship Code statement**

Montanaro Asset Management is an independent institutional investment manager with an exclusive focus on quoted UK and European Small & MidCap equities.

Our investment process is designed to ensure that we fulfil the responsibilities expected from an institution such as ours, including those set out in the UK Stewardship Code. With reference to the Code, we summarise our investment approach with the following statement:

*At all times we aim to be effective stewards of our clients' assets by seeking to promote good Corporate Governance and the long-term success of the companies in which we invest, for the benefit of all stakeholders.*

## Principle 1

### **Institutional Investors should publicly disclose their policy on how they will discharge their stewardship responsibilities**

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Montanaro discloses how we discharge our stewardship responsibilities in our “ESG Handbook”, a detailed document which sets out our approach to corporate governance and company engagement. This handbook includes a dedicated chapter titled “*Montanaro’s Approach to the UK Stewardship Code*”. This information is publically available on our website.

#### **How we discharge our stewardship responsibilities:**

Montanaro seeks to invest in the highest “Quality” companies on behalf of our long-term clients. We assess both qualitative and quantitative factors when we conduct company analysis in order to ascertain the Quality of an investment opportunity. The attributes that we analyse include:

1. **Measuring company performance:** As part of company analysis our Analysts are responsible for the completion of Montanaro’s four checklists: Quality, Ethical, Environmental & Social and Corporate Governance. Our Corporate Governance Checklist considers criteria set out in the UK Stewardship code: “*strategy, performance, risk, capital structure, corporate governance, culture and remuneration*”. With regards to this, Analysts consider:
  - Leadership: We believe that Boards should be independent. Where there is a majority of Executive or non-independent Non-Executive Directors - which is relatively common for founder / family-owned small companies – Analysts, supported by the Fund Managers, engage with the Chairman to understand the logic and discuss the succession plan.
  - Effectiveness & Accountability: Analysts monitor and judge the effectiveness of company management teams by detailing the experience and track record of the executive body in their company research. Management are held to account for the performance of the companies under their control in meetings, which our Analysts host at Montanaro. Fund Managers also attend these meetings. As we explain below, Voting and Engagement form an important part of accountability and responsibility for both sits primarily with our Analysts. They are supported in this by Montanaro’s Investment, Executive and Sustainability Committees.
  - Remuneration: Analysts record details of Executive remuneration (if publically available) including base salary and long-term incentive schemes (LTIPs). These are assessed against our internal guidelines (which are detailed in Montanaro’s ESG Handbook). Whilst we recognise that every company is different Analysts encourage competitive, but not extreme, salaries and LTIPs that are linked to long-term returns on capital employed. Analysts engage with companies where remuneration policies differ from our guidelines.
2. **Engaging with investee companies:** The responsibility for company engagement predominantly sits with our Analysts given it is they who have direct lines of communication with our investee companies. Engagement includes “normal” events such as management meetings which we host regularly at Montanaro. Both Analysts and Fund Managers attend these meetings. At these meetings Analysts ask questions relating to the general management of the business including questions relating to matters of Corporate Governance. Where relevant, Analysts also ask questions relating to matters that require more focused engagement. They are supported in this by Montanaro’s Sustainability Committee who may liaise with the company directly and

other relevant parties. The Sustainability Committee records and monitors all instances of engagement.

3. **Apply a clear and consistent approach to voting:** Voting is a vital part of our engagement with companies. Our Compliance Department receives independent third party corporate governance reports and voting recommendations from Institutional Investor Services (ISS) ahead of meetings, which they send to our Investment Team. These are used for advice only. Our Analysts systematically review all resolutions ahead of shareholder meetings and we voice our concerns where required. Via dialogue with Investment and Sustainability Committees, our Analysts aim to discuss any issues with management prior to voting against or abstaining. We apply the same voting decisions across all portfolios, unless a segregated client has specified that a particular voting policy be applied in their client agreement. The Compliance Department keeps a record of our voting rationale.

## Principle 2

### **Institutional Investors should have a robust policy on managing conflicts of interest in relation to stewardship which should be publically disclosed**

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Montanaro recognises that it is our duty, as an institutional investor, to act in the interests of our clients. Equally, we understand that in the course of our business, conflicts of interest may arise from time to time.

Due to this – and in line with our commitment to the UK Stewardship Code – we maintain a Conflicts of Interest Policy which is available on our website. The high level aim of the policy is to ensure that Montanaro remains conscious of our responsibility to always act in the best interests of our clients and to be aware of any potential conflicts that may arise.

#### **This policy is supported by:**

- Our simple business model: We are a “long only” manager of quoted UK and European Small & MidCap equities. As a result, we believe that our business model is as transparent as is possible for an institutional asset manager.
- Our Personal Account Dealing Policy: This prohibits employees and connected persons from dealing in any security that falls into Montanaro’s investment universe for their own account.
- A ban on dealing in investments for Montanaro’s own account. We only invest on behalf of our clients.
- An annual review of our Conflicts of Interest Policy by our Compliance Officer.

#### **Examples of where conflicts may occur include:**

1. **Where the company being voted on is a client of MAM**: In this situation, a record of the potential conflict will be logged against the upcoming Annual General Meeting in our internal log. This ensures that the potential conflict and its resolution is monitored by Montanaro’s Compliance Team. The Analyst covering the company then recommends how to vote to the Investment Team. Prior to the actual vote being processed, the Analyst’s recommendation would be reviewed by the Sustainability Committee and the Compliance Officer, to ensure that the decision reflects the best interests of the clients holding the stock.
2. **Where the MAM employee making the voting decision (or a person connected to them) is a director of, significant shareholder of or has a position of influence at the company being voted on**: Employees sign an annual declaration notifying MAM of any outside business interests. If a Montanaro Analyst had a connection to an investee company, responsibility for researching that company (and for making voting decisions) would be assigned to another Analyst by the Head of Research.
3. **Where MAM or an affiliate is a shareholder of the company being voted on**: MAM does not deal for its own account, with the exception of holdings in its own funds. MAM has a simple business structure and does not have any affiliates.
4. **Where there is a conflict of interest between one client and another**: Given Montanaro purely

invests in European Small & MidCap equities on a long-only basis, we do not take contrarian positions in company shares. Our clients all benefit when the shares in our investee companies appreciate and vice versa. In terms of voting, decisions are made by the Analyst responsible for the respective company – following dialogue with the wider investment team – and applied across all accounts where we possess the right to vote. If a conflict arises between one client and another, both clients would be notified of the conflict by the relevant Client Relationship Manager and asked to approve any relevant voting decision made on their behalf. Voting decisions are applied across all portfolios where we have authority to vote, unless the client has formally specified that a different policy should be applied.

5. **Where the director of a company being voted on is also a director of MAM:** All MAM employees and directors are required to declare outside business interests. In this situation, a record of the potential conflict will be logged against the upcoming Annual General Meeting in our internal log. The Analyst covering the company would make their recommendations on how to vote as usual, and prior to the votes being processed would refer their recommendations to the Sustainability Committee and the Compliance Officer, who will ensure that the decision reflects the best interests of the client.

**In addition to the above, Montanaro mitigates against the likelihood of certain conflicts by:**

- Conducting thorough due diligence on all clients before take on, including an assessment of whether any conflicts of interest are likely to occur. This is reviewed annually.
- Requiring all employees and directors to disclose their outside business interests and directorships when they join the company. This is reviewed annually.

**Principle 3****Institutional Investors should monitor their investee companies**

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Guidance relating to the UK Stewardship Code states that “*effective monitoring is an essential component of stewardship*”. To ensure that we fulfil this responsibility, we have built one of the largest in-house SmallCap research teams in Europe so that we can effectively monitor our investee companies to the highest of standards. Our team is responsible for the analysis and monitoring of:

- The performance of companies: Analysts are responsible for monitoring companies on a daily basis via Montanaro’s four checklists, financial modelling and internal investment meetings. Results announcements are studied closely and we read all of our companies’ Annual Reports. Additionally, we spend a great deal of time meeting with management teams and attending company site visits to ensure that we get to understand the culture of a business. This work is supported by monthly, quarterly and annual attribution analysis, provided by Montanaro’s Risk & Compliance Team. We keep abreast of wider industry and sector based trends that may impact the value of a company via weekly newsflow monitoring. We use the information provider Factiva to assist us with this.
- The executive team: As per our Corporate Governance Policy, we place emphasis on the performance of a company’s management team and Board. We seek to understand how management are remunerated and whether pay policies work for the benefit of long-term shareholders and other stakeholders. We encourage Boards to have a majority of Non-Executive, fully independent Directors. By doing this, we encourage companies to adhere to the spirit of the UK Stewardship Code.
- Potential issues that may require engagement: Where possible, we aim to identifying potential issues before they fully develop. We aim to allow investee companies time to improve their behaviour and address areas of concern.

**The monitoring of investee companies is further supported by:**

- Montanaro’s Sustainability Committee: The purpose of the Sustainability Committee is to ensure that Montanaro’s ESG effort remains coordinated across the organisation. As part of this, the Sustainability Committee meets formerly on a quarterly basis. Its responsibilities include the review of Checklists, company meeting notes and Montanaro’s Engagement Log. The Committee liaises with the investment team regarding issues that may affect an investee company – for example they have recently requested that the Consumer Analyst completes a project on Nutrition to ensure that we fully understand how investee companies are exposed to changing diets and new food regulation. To ensure that there is buy-in across the organisation, the Committee is formed of members from the Investment, Business Development and Compliance teams.
- Montanaro’s Executive Committee: In turn, Montanaro’s Executive Committee – comprised of the Chairman, Chief Executive Officer, Compliance Officer and Head of Research – meets on a quarterly basis to review the full operations of Montanaro’s business operations. This includes a review of internal company research, performance data and the work of the ESG Committee.

**Regarding Insider Information:**

- Montanaro would generally prefer not to be made an insider: however in some situations it is unavoidable. In these cases, we follow the guidance contained in Montanaro's Insider Dealing Policy. The Compliance Officer is notified and the stock in question is put on a banned list and blocked from trading in our Investment Management System until the relevant information is made public.

For more information on the monitoring of our investee companies, please contact Ed Heaven, who is a member of our Sustainability Committee at [ehaven@montanaro.co.uk](mailto:ehaven@montanaro.co.uk)



#### Principle 4

### **Institutional Investors should establish clear guidelines on when and how they will escalate their activities as a method of protecting and enhancing shareholder value**

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Montanaro is open to engaging with every single company in which we invest. We believe that institutional asset managers are well placed to improve companies' long-term performance through engagement. In our opinion, this forms a fundamental part of good stewardship.

We will engage on a variety of issues. In line with our ESG Policies, these include, but are not limited to:

- **Ethics:** We do not invest in companies involved in the production or supply of indiscriminate weapons; tobacco producers and manufacturers; gambling companies; companies that produce and distribute pornography; alcohol producers; high interest rate lending companies. We may engage with companies if we are concerned that they have exposure to these areas. We also engage with companies concerning other areas of ethical interest.
- **Environmental & Social:** Guided by the UN Global Compact, we engage with companies on issues surrounding Humans Rights, Labour Practices, Bribery & Corruption, Environmental Impact, Climate Change and Supply Chain Management.
- **Corporate Governance:** We will engage with companies on a range of corporate governance factors, for example Remuneration, Capital Allocation Record and Board Independence.

Montanaro has developed an Engagement Policy to ensure that our approach to company engagement is consistent. This is set out below:

#### **1. Deciding to engage**

If an Analyst (or any other member of Montanaro's staff) feels that engagement is needed with a company, the relevant Analyst will discuss the issue with the Sustainability Committee at an ad hoc meeting, or via email. They will agree on a course of action given the case details and the Analyst will then go ahead and engage. There are a number of channels open to us when we seek to engage with a company, including:

- Direct engagement with the management and /or Board
- Speaking to industry competitors
- Speaking with industry representatives such as Trade Unions
- Liaising with other shareholders

#### **2. Recording engagement**

All engagement activity is recorded on Montanaro's ESG Engagement Log. Any activity is deemed to be "ongoing" until formally closed. It is the responsibility of the Sustainability Committee to review this Log at each meeting to monitor progress and discuss priorities.

#### **3. Monitoring engagement**

Once we have initiated engagement with a company the Analyst and Sustainability Committee – supported by other members of the Investment Team, such as the Head of Research – monitor the company's response. This can go a number of ways:

- The company responds promptly and assuages our concerns and/or provides material evidence to prove that they are going to solve the issue at hand.
- The company responds promptly but we are not satisfied by their answer. We engage further. In some cases we may speak to competitors of the company to better understand the industry, or an industry body, such as a Trade Union or discuss the matter at a shareholders forum.
- The company does not respond, so our Analyst engages again with management. In some cases we may choose to escalate the matter to another member of the company's senior management team in an effort to garner a response.
- The company does not respond and appears unlikely to do so, so we liaise with industry bodies or other shareholders in order to gain further support for our cause, or better understand the situation.

#### **4. Reaching a conclusion**

In an ideal world we wish to reach a positive conclusion on every matter of engagement. Our single aim when we engage with companies is to encourage an improvement in behaviour that leads to more sustainable business practices. We are realistic, however; engagement is often a complex business in itself. We do not place a deadline on engagement as in our experience, complex issues can take time to resolve. As long-term shareholders, our focus is on ensuring the improvement of a company's performance over a long time period. However, if our engagement subsequently leads us to doubt the longer term attraction of an investment, that investment will be reviewed and could be sold.

We have good relationships with our investee companies and they tend to be open to our engagement requests. Indeed, many of our companies reach out to us for guidance, notably in respect of executive remuneration. For instance, we are regularly approached by Remuneration Committees to discuss the structure of Long-term Incentive Plans (LTIPs) for the Executive.

**Principle 5****Institutional Investors should be willing to act collectively with other investors where appropriate**

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We are willing to act collectively with other investors in situations where we believe it will be productive. This may occur when:

- Our initial engagement has failed to produce a desirable outcome.
- We are approached by other shareholders regarding a specific issue that threatens to negatively impact the value of our investment.

Each situation is considered on a case by case basis. We wish to avoid being deemed to be acting in concert with others. In practice, however, we find that most collective engagements:

- Are focused on sectors in which we don't invest due to our Quality bias.
- Involve LargeCap companies which are not part of our investment universe.

**Principle 6****Institutional Investors should have a clear policy on voting and disclosure of voting activity**

- We seek to exercise all of our voting rights.
- We make our own voting decisions.
- We do not chose to automatically support the Board of an investee company.
- We have and will abstain or vote against resolutions.
- We publish Voting Activity Summary Reports on our website

**We exercise our voting rights**

Voting is a vital part of our engagement with companies. This is why we vote at all Annual General Meetings for the holdings within our Funds. We also do this for segregated portfolios where we have authority to do so. We do not engage in stock lending in Montanaro Funds (although our segregated clients may have their own policies on this).

**We make our own voting decisions**

We receive independent third party corporate governance reports and voting recommendations from Institutional Investor Services (ISS) ahead of meetings, however we use these 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.

We apply the same voting decisions across all portfolios, unless a segregated client has specified that a particular voting policy be applied in their client agreement. We keep a record of our voting rationale.

**We publish Voting Activity Summary Reports on our website**

We use ISS to process our proxy voting. All voting activity is recorded in our Proxy Voting Log.

The Sustainability Committee reviews voting activity for the quarter at each meeting. Voting Activity Summaries are produced quarterly and published on our website. These include the total number of proposals we voted on and a breakdown of how we voted on different subjects such as approving Remuneration policies, electing Directors, and approving capital increases.

**Principle 7****Institutional Investors should report periodically on their stewardship and voting activities**

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Montanaro maintains clear records of our stewardship activities. We recognise that transparency is an important feature of effective stewardship and unless a disclosure may involve confidential or price sensitive information, we share the details of our stewardship with clients as follows:

- **Company Research:** Our Analysts are responsible for writing and maintaining up-to-date Investment Case Presentations, Company Research Notes (including summaries of company meetings and site visits) and Checklists on all of the companies in which we invest. Details of these are shared with clients at meetings and on request. This helps our clients to understand why we have invested in a company on their behalf, and how we monitor companies during the holding period.
- **Performance:** Performance data is reported to our clients on a monthly, quarterly and annual basis for all of our Funds, Investment Trusts and segregated mandates. This includes monthly factsheets which detail performance numbers versus respective benchmark indices, attribution analysis, stock specific comments and an economic outlook. For certain clients, we also include summaries of recent “buys” and “sells” as well as an overview of engagement activity.
- **Engagement:** We record all engagement activity in our Engagement Log. Summary details of engagement cases are provided to clients as requested and in certain circumstances we have provided clients with detailed “ESG Case Studies”. We quantify our engagement activity each year across the full ESG spectrum and publish this information on Montanaro’s website.
- **Engagement reporting:** Certain clients receive quarterly engagement reports on companies in which their assets are invested. Additionally, we compile a Quarterly ESG Presentation which contains both qualitative and quantitative information on our stewardship activities. Our Sustainability Committee meetings are minuted and are also available to clients on request. We also provide a summary of engagement cases to the UN PRI on an annual basis.
- **Voting:** Each year we publish a summary of our voting statistics on our website. This includes the number of proposals where we voted either in favour, against or abstained. A more detailed breakdown of how we voted on specific issues and our rationale for doing so is provided to clients on a case by case basis. Proxy Voting Activity Summaries are produced each quarter and are available on Montanaro’s website. As well as reporting to clients, we report annual voting statistics to the UN in line with our responsibilities under the Principles for Responsible Investment.
- **Montanaro’s ESG Handbook:** The handbook explains our approach to investment and how we see ESG – and good stewardship – as an intrinsic part of our “Quality” investment approach. The handbook summarises our investment process and our three ESG policies. Details of engagement and voting activity are also recorded in the handbook. Montanaro’s ESG Handbook is updated at least annually and is available on our website.

## 9 – BECOMING A B CORPORATION

Certified B Corporations® (B Corps™) are defined as for-profit companies that use the power of business to build a more inclusive and sustainable economy. As of June 2019, there are 2,800 B Corps in 130 industries and 60 countries around the world. Just 198 of these are based in the UK.

- They meet the highest verified standards of social and environmental performance, transparency and accountability.
- 
- Certified B Corporations amend their governance so that, by law, they can make decisions and implement practices that consider not just shareholder value, but the impact on all stakeholders - employees, customers, society, and the environment.
- 
- B Corp Certification is a highly selective status. Companies must document their positive impact to qualify and undergo verification every three years to maintain their Certification.
- 
- Certified B Corporations range from multinational corporations [Natura] to wholly owned subsidiaries [Seventh Generation] to small businesses [Harvest Market] serving local communities.
- 
- It is one of the only certifications that is not for a product or service but for the whole business behind the product or service.
- 
- B Corporation Certification helps consumers identify companies with a mission and helps investors to select investments that align with their values.

### **Becoming a B Corp was a natural step in Montanaro's Responsible Investment journey.**

The Certification process uses credible, comprehensive, transparent and independent standards of social and environmental performance. The B Corp assessment process measures a company's performance in five categories:

- 1. Governance;**
- 2. Workers;**
- 3. Customers;**
- 4. Community;**
- 5. the Environment.**

The assessment is marked out of 200 and the pass mark to become a B Corp is 80. The median score for businesses who complete the impact assessment is 50.9.

Montanaro's 2019 B Corp score was 81.8. Our report can be viewed in full at:  
<https://bcorporation.net/directory/montanaro-asset-management>

## 10 – EXECUTIVE REMUNERATION

Executive Remuneration is one of the most contentious area of Corporate Governance. This is largely because it is so difficult to come up with a “*one size fits all*” framework with which to appraise executive pay. No company is the same and every business model is different. Executive Remuneration is therefore more of an art than a science. What is appropriate for one company may not work for another.

For more information on our approach to Executive Remuneration, please request a copy of our separate publication: *Executive Remuneration: Montanaro’s Principles*.

## 11 – SUSTAINABILITY AT MONTANARO

### ENCOURAGING SUSTAINABLE BEHAVIOUR

We aim to practise what we preach. We encourage our colleagues to live as sustainably as possible, both during their time at Montanaro and in the world beyond.

### OUR HOME: 53 THREADNEEDLE STREET

We are based in a beautiful building a few doors down from the “Old Lady of Threadneedle Street”, the Bank of England. The bank has been here since 1744 and our building is not much younger. So we:

- Turn off lights and computers when they are not needed;
- Source stationary from Wild Hearts supporting the impact work of the Wild Hearts Foundation;
- Reduced plastic use: no plastic cups and no plastic covers on presentations;
- Support a bee-hive on our roof.

### RECYCLING

In 2018 our recycling programme achieved:

- 1,930 kg of waste recycled;
- 2,710 kg of CO<sub>2</sub> saved (equivalent to 23 trees).

### CARBON OFFSETTING

We offset over 28 tonnes of CO<sub>2</sub> in 2018 via ClimateCare, which helped to finance a range of impact projects including:

- The provision of safe water to 4 million people in Kenya;
- The delivery of energy efficient cookstoves to households in Ghana.

### CHARITY & COMMUNITY

In 2018, Montanaro’s charity work included:

- Ongoing support to Tribal Survival, a UK registered charity which aims to promote the well-being of indigenous people across the world.
- Staff volunteered over 100 hours of their time to work for local London charities.

### HEALTHY EATING

We provide two baskets of fruit each week in the office from the company Fruitful Office. This helps to fund sustainable farming in Africa:

- We planted 101 fruit trees in 2018 for local communities in Malawi.

### MINDFULNESS

A healthy body and a healthy mind go hand-in-hand. This is one reason why we host a weekly Yoga class, run by our multi-talented Head of Research, Mark Rogers.



## APPENDIX

## WHAT DOES RESEARCH SAY ABOUT ESG?

Appraising investment opportunities consistently from an ESG perspective can prove problematic. The reason for this is because, as Professors Elroy Dimson, Paul Marsh and Mike Staunton acknowledge<sup>19</sup>, it can be hard to find a definition of an “unethical” company that is universally acceptable.

For instance, Medtronic, a medical devices company, is a constituent of the FTSE4Good Index but has a tax-inversion scheme that has been deemed unethical by certain stakeholders. The US supermarket, Walmart, scores highly on certain ESG metrics, but was divested by the Norwegian Sovereign Wealth Fund due to unacceptable labour practices.

Yet, when things go wrong, ESG failings are often highly visible. In recent years we have witnessed the unethical behaviour of the banking sector which contributed to the Global Financial Crisis; the environmental failings of BP after the Macondo oil disaster; and Tokyo Electric Power Company’s social neglect, in the wake of Japan’s Tsunami disaster. In all cases, shareholders and their fellow stakeholders suffered.

While ethical failings can appear obvious in hindsight, a problem for proponents of ESG investing is that there is no simple “forward-looking” way of evaluating ESG risk. Yet such difficulties should not preclude ESG from forming part of an investment process. In fact, there is academic support for such an approach:

- It is becoming increasingly difficult for investment decision-makers to dismiss ESG, given investors *“readily quantify business goodwill and other equivalently nebulous intangibles”*<sup>20</sup>.
- Responsible investing *“recognises that the generation of long-term sustainable returns is dependent on stable, well-functioning and well-governed social, environmental and economic systems”*<sup>21</sup>.
- Considering ESG issues helps to protect all stakeholders, as *“shareholders...can exercise considerable influence over the management of companies”*<sup>22</sup>.
- Sustainability policies are a means of *“pre-emptive insurance for adverse ESG events”*<sup>23</sup>.
- Worthwhile ESG policies require *“knowledge of the subject matter and criteria used to measure it”*<sup>24</sup>.

We would suggest that there is no definitive proof that ESG increases shareholder returns. We would argue, however, that correctly integrated into an investment process, considering ESG makes

<sup>19</sup> Credit Suisse Global Investment Returns Yearbook 2015, *Responsible investing: does it pay to be bad?* Elroy Dimson, Paul Marsh and Mike Staunton, London Business School, pg. 20

<sup>20</sup> ibid

<sup>21</sup> <http://unpri.org/wp-content/uploads/1.WhatIsResponsibleInvestment.pdf>

<sup>22</sup> <http://ec.europa.eu/environment/archives/finserv/fisum.pdf>

<sup>23</sup> [http://www.smithschool.ox.ac.uk/library/reports/SSEE\\_Arabesque\\_Paper\\_16Sept14.pdf](http://www.smithschool.ox.ac.uk/library/reports/SSEE_Arabesque_Paper_16Sept14.pdf)

<sup>24</sup> <http://www2.deloitte.com/content/dam/Deloitte/us/Documents/risk/us-aers-sustainability-reporting-landscape.pdf>

positive investment returns more likely, rather than less. With this in mind, we would agree with the following statements:

- ESG *“considerations often have a role to play in the proper analysis of investment value<sup>25</sup>”*.
- *“Socially and environmentally responsible policies...[minimise] risks by anticipating and preventing crises that can affect reputation and cause dramatic drops in share prices<sup>26</sup>”*.
- *“Stock price performance is positively influenced by good sustainability practices<sup>27</sup>”*
- *“Sound sustainability standards lower the cost of capital of companies<sup>28</sup>”*
- *“Solid ESG practices result in better operational performance<sup>29</sup>”*
- *“Corporate engagement can pay, whether the focus is on environmental and social issues or on corporate governance<sup>30</sup>”*.

In addition to the above, it is worth highlighting certain findings from a comprehensive report by Deutsche Bank, *Sustainable Investing, Establishing Long-Term Value and Performance, 2012<sup>31</sup>*. The report clearly demonstrates that there is academic support for considering ESG factors in investment decisions. Indeed, as the renowned economist Michael Jensen states, *“it is obvious that we cannot maximise the long-term market value of an organisation if we ignore or mistreat any important constituency<sup>32</sup>”*.

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<sup>25</sup>Credit Suisse Global Investment Returns Yearbook 2015, *Responsible investing: does it pay to be bad?* Elroy Dimson, Paul Marsh and Mike Staunton, London Business School, pg. 20

<sup>26</sup> *The Commission Green Paper on promoting a European framework for Corporate Social Responsibility COM (2001) 366 final (18/07/2001).*

<sup>27</sup> [http://www.smithschool.ox.ac.uk/library/reports/SSEE\\_Arabesque\\_Paper\\_16Sept14.pdf](http://www.smithschool.ox.ac.uk/library/reports/SSEE_Arabesque_Paper_16Sept14.pdf)

<sup>28</sup> Ibid

<sup>29</sup> Ibid

<sup>30</sup> [http://www.oekom-research.com/homepage/english/oekom\\_CR\\_Review\\_2013\\_en.pdf](http://www.oekom-research.com/homepage/english/oekom_CR_Review_2013_en.pdf)

<sup>31</sup> [https://institutional.deutscheawm.com/content/\\_media/Sustainable\\_Investing\\_2012.pdf](https://institutional.deutscheawm.com/content/_media/Sustainable_Investing_2012.pdf)

<sup>32</sup> As cited in *Drivers of Long-Term Business Value: Stakeholders, stats and strategy*, Koehler & Henspenide, Deloitte, 2012

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**The Deutsche Bank report** analyses the findings of “over 100 studies...[including] 56 research papers, as well as 2 literature reviews and 4 meta studies”:

- “100% of the academic studies agree that companies with high ratings for CSR and ESG factors have a lower cost of capital in terms of debt (loans and bonds) and equity. In effect, the market recognises that these companies are lower risk than other companies and rewards them accordingly”.
- “89% of the studies we examined show that companies with high ratings for ESG factors exhibit market-based outperformance, while 85% of the studies show these types of company’s exhibit accounting-based outperformance”.
- “The single most important of these factors, and the most looked at by academics to date, is Governance (G), with 20 studies focusing in on this component of ESG (relative to 10 studies focusing on E and 8 studies on S). In other words, any company that thinks it does not need to bother with improving its systems of corporate governance is, in effect, thumbing its nose at the market and hurting its own performance all at the same time”.
- “Strong corporate commitment to ESG (or E, S or G) is positively correlated to a lower cost of capital. Again, this finding is evident in all the studies we analysed”.

## GLOSSARY

Key terms used in the Field of Sustainable Investing<sup>33</sup>:

Concept	Definition	Source
<b>Ethical Investment</b>	Investment philosophy guided by moral values, ethical codes or religious beliefs. Investment decisions include non-economic criteria. This practice has traditionally been associated with negative (or exclusionary) screening.	Mercer, 2007
<b>Values-Driven Screening</b>	Values-based (also referred to as negative or exclusionary) screening is defined as an investment approach that excludes some companies or sectors from the investment universe based on criteria relating to their policies, actions products or services. Investments that do not meet the minimum standards of the screen are not included in the investment portfolio. Criteria may include environmental, social, corporate governance or ethical issues. For example, specific industries or sectors such as weapons manufacturers, or specific companies considered to be poor environmental, social or governance (ESG) executors.	Mercer, 2007
<b>Socially Responsible Investment (SRI)</b>	SRI, as it first emerged, was very similar to ethical investing in that it allowed a level of trade-off between corporate social and financial performance when making investment decisions, and predominantly utilized exclusionary screening. However, modern SRI represents an investment process that seeks to achieve social and environmental objectives alongside financial objectives, utilizing both values-driven, and risk and return screening.	DBCCA analysis 2012; Mercer, 2007
<b>Sustainability</b>	Sustainability or sustainable development refers to the concept of meeting present needs without compromising the ability of future generations to meet their needs. It encompasses social welfare, protection of the environment, efficient use of natural resources and economic well-being.	Brundtland Report, 1987; Mercer, 2007
<b>Risk &amp; Return Screening</b>	Risk and return (or positive) screening is defined as an investment approach that includes non-traditional criteria relating to the policies, actions, products or services of securities issuers. Portfolios are tilted towards stocks that rate well on the nominated criteria, which can include ESG or ethical issues.	Mercer, 2007
<b>Corporate Governance</b>	Procedures and/or processes according to which an organization is directed and controlled. Corporate Governance structure specifies the distribution of rights and responsibilities among the different participants in the organization – such as the board, managers, shareholders and other stakeholders – and lays down the rules and procedures for decision making. National and international best practice standards exist.	OECD, as cited in Mercer, 2007
<b>Universal Owner</b>	A large asset owner who, as a consequence of its size, owns a slice of the whole economy and market through its portfolios. Universal owners adapt their actions with the intent of improving long-term performance by benefiting the whole economy and market in a logical but ambitious extension of sustainable investing. They justify these actions on financial grounds.	Towers Watson, 2011
<b>Environmental, Social and Corporate Governance (ESG)</b>	The term that has emerged globally to describe the environmental, social and corporate governance issues that investors are considering in the context of corporate behavior. No definitive list of ESG issues exists, but they typically display one or more of the following characteristics: (i) issues that have traditionally been considered non-financial or not material; (ii) a medium or long-term time horizon; (iii) qualitative objectives that are not readily quantifiable in monetary terms; (iv) externalities not well captured by market mechanisms; (v) a changing regulatory or policy framework; (vi) patterns arising throughout a company's supply chain; and (vii) a public-concern focus.	Mercer, 2007
<b>Best-in-Class Approach</b>	Investment approach that focuses on companies that have historically performed better than their peers within a particular industry or sector on measures of environmental, social and corporate governance issues. This typically involves positive or negative screening or portfolio tilting.	Mercer, 2007
<b>Responsible Investment</b>	The integration of ESG considerations into investment management processes and ownership practices in the belief that these factors can have an impact on financial performance, in particular over the medium to longer-term. Responsible Investing (RI) can be practiced across all asset classes.	Mercer, 2007; DBCCA analysis

<sup>33</sup> [https://institutional.deutscheawm.com/content/media/Sustainable\\_Investing\\_2012.pdf](https://institutional.deutscheawm.com/content/media/Sustainable_Investing_2012.pdf)

Key terms related to Corporate Social Responsibility and Shareholder Engagement<sup>34</sup>:

Concept Name	Definition	Source
<b>Corporate Social Responsibility</b>	Approach to business which takes into account economic, social, environmental and ethical impacts for a variety of reasons, including mitigating risk, decreasing costs, and improving brand image and competitiveness. This approach is sometimes implemented by means of a comprehensive set of policies and procedures integrated throughout a company, encompassing a wide range of practices, including: corporate governance, employee relations, supply chain relationships, customer relationships, environmental management, philanthropy and community involvement.	Mercer, 2007
<b>Stakeholder</b>	Individuals or organizations with an interest in the actions and impacts of an organization. They may be customers, suppliers, shareholders, employees, communities, members of special interest groups, non-governmental organizations, or regulators.	Mercer, 2007
<b>Active Ownership</b>	The voting of company shares and/or the engaging of corporate managers and boards of directors in dialogue on ESG issues as well as on business strategy issues. Increasingly pursued in an effort to reduce risk and enhance shareholder value. Can also be referred to as "Shareholder Activism".	Mercer, 2007
<b>Shareholder Engagement</b>	The practice of monitoring corporate behavior and seeking changes where appropriate through dialogue with companies or through the use of share ownership rights, such as filing shareholder resolutions. Shareholder engagement is often employed in attempts to improve a company's ESG performance.	Mercer, 2007
<b>Proxy Voting</b>	The delegation of voting rights from entitled voters who do not attend shareholders' meetings to delegates who vote on their behalf. Proxy voting allows shareholders to exercise their right to vote without committing the time involved in actually attending meetings. Proxy voting policies can include specific guidance on ESG and ethical decisions.	Mercer, 2007
<b>Corporate Social Performance</b>	A business organization's configuration of principles of social responsibility, processes of social responsiveness, and policies, programs, and observable outcomes as they relate to the firm's societal relationships.	Wood, 1991:693 <sup>23</sup>
<b>Corporate Financial Performance</b>	A term widely used within academia to refer to the financial or economic performance of a company. In general, academic studies have tended to focus on either financial accounting measures (for example, Return on Assets or Return on Equity) or economic measures (usually a company's stock performance) to measure, rank and compare the CFP of different companies.	DBCCA analysis 2012
<b>Corporate Citizenship</b>	A term used to describe a company's role in, or responsibilities towards society. For this reason it is sometimes used interchangeably with corporate social responsibility, although this concept is extended by some to refer to the political activities – and perhaps even rights – of a company.	DBCCA analysis 2012
<b>Integrated Reporting</b>	A growing practice of corporate reporting that demonstrates the linkage between an organization's financial performance in relation to environmental, social, and governance (ESG) factors that underlie the organization's core activities. By "integrating" financial and non-financial data, Integrated Reporting can help businesses take more sustainable decisions and enable investors and other stakeholders to transparently understand an organizations true performance.	DBCCA analysis 2012
<b>Triple Bottom Line</b>	A holistic approach to measuring a company's performance on environmental, social and economic issues. The triple bottom line focuses companies not just on the economic value they add, but also on the environmental and social value they add or destroy. This concept is frequently utilized in CSR or sustainability reporting.	Mercer, 2007; DBCCA analysis 2012

<sup>34</sup> [https://institutional.deutscheawm.com/content/media/Sustainable\\_Investing\\_2012.pdf](https://institutional.deutscheawm.com/content/media/Sustainable_Investing_2012.pdf)



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[END]