

The Stewardship Code

Montanaro Asset Management has been a signatory of the UK Stewardship Code since its publication in 2010. The following explains how we comply with the seven principles underlying the Stewardship Code, as defined in the most recent version published by the Financial Reporting Council in September 2012.

Summary:

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.

The application of Montanaro's stewardship responsibilities are contained within the "Montanaro ESG Handbook", which is available under the Ethical & ESG Investing section of our website (www.montanaro.co.uk).

Principle 1

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

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 ESG 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 ESG Committee who may liaise with the company directly and other relevant parties. The ESG 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 ESG 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

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 ESG 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 ESG 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

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 ESG Committee:** The purpose of the ESG Committee is to ensure that Montanaro’s ESG effort remains coordinated across the organisation. As part of this, the ESG 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 ESG Committee at eheaven@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

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 ESG 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 ESG 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 ESG 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

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 ESG 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.

The most recent report can be found here:

<http://www.montanaro.co.uk/media/75593/voting-summary-2015.pdf>

Principle 7

Institutional Investors should report periodically on their stewardship and voting activities

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 ESG 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.

For further information on the above, or to request a copy of our ESG Handbook, please contact Ed Heaven at: eheaven@montanaro.co.uk

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