Smith & Williamson

Stewardship & Responsible Investing Annual Report

Introduction

2020 will be remembered for the many different things that stemmed from the COVID-19 pandemic, but one of the most impactful will be that ESG investing and stewardship is now indisputably mainstream. A second major change was to see social issues – human capital management, employee wellbeing, communities, supply chains - jump in importance, alongside climate change.

The monetary and fiscal response to the pandemic was unprecedented in both its speed and size. There is a desire to use this spend to 'build back better' with a huge focus on the infrastructure required to accelerate progress towards the net zero carbon targets set by the Paris Accord. To this has been added a wide range of commitments by government leaders, plus a tsunami of green legislation and regulations specifically designed to incentivise markets and companies to do the bulk of the heavy investment lifting.

The UK hosts the postponed COP26 summit in Glasgow this November and holds the presidency of the G7 for 2021 and it is clear that they will be seeking a significant ratcheting up of carbon reduction activity across the world, with a focus on green finance.

The UK's Climate Change Committee (CCC), the statutory body set up to advise the government on climate change and to report to parliament on the country's progress, produced its 6th Carbon Budget in early December. To meet the UK government's commitment of net zero by 2050, the target date to reduce emissions by 80% moves from 2050 to 2035 (a 63% reduction from 2019 levels). 'Low-carbon markets and supply chains must scale up so that almost all new purchases and investments are in zero-carbon solutions by 2030 or soon after'. The CCC report states that future reductions in carbon emissions must come from transport, industry, buildings and agriculture plus the phasing out of gas power stations. They acknowledge the very real policy challenges, including setting incentives for specific sectors, removing barriers to change, supporting a just transition, retraining etc. The scale of the challenge, the amount and speed of investment is huge, but so are the opportunities and the savings in terms of lower energy costs.

As signatories to the UN-supported PRI (Principles of Responsible Investment) and the UK Stewardship code Smith & Williamson is incorporating these Environmental Social and Governance (ESG) factors alongside traditional financial metrics when picking stocks and funds. We believe this information helps us make better investment decisions and build more resilient long-term portfolios for our clients. As part of this we vote the direct shareholdings on your behalf and engage with the management teams of companies in which we invest to make sure their interests and yours are properly aligned.

We are at the forefront of the UK wealth industry in this regard and are ambitious to remain as one of the leaders. I hope this annual Stewardship Report gives you a strong sense of the deep thought, activity and commitment of Smith & Williamson to the long-term interests of our clients and our other stakeholders.

Chris Woodhouse
CEO, Tilney Smith & Williamson

Contents

Our year in ESG

This past year, Smith & Williamson's responsible investment team has achieved a number of milestones, with important collaborative efforts in key areas, plus recognition from responsible investing organisations.

UK Stewardship Code

We are committed long term responsible investors and good stewards of our clients' assets. Being voluntary signatories to the UK Stewardship Code helps demonstrates this. Having previously received a Tier 1 Status we are now working towards our first report in line with the significantly revised and more demanding Stewardship Code 2020.

UN supported Principles for Responsible Investment (PRI)

These six principles are the foundation of our Responsible Investment response. Smith & Williamson were happy to note that we were awarded an A rating from the PRI in 2020. Our full PRI reports can be found on our website reflecting our commitment to transparency.

Proxy Voting & Engagement

As part of our commitment to both the UK Stewardship Code and the UN PRI we voted on over 700 company meetings and actively engaged with over 100 companies in 2020. Due to Covid-19 we saw an extended proxy voting season as AGMs were moved to virtual events. We managed to streamline our processes and report as normal. Our full voting record can be found later in this report. We have also worked hard to ensure we remain SRD II compliant for both discretionary and non-discretionary clients.

Collaborative Engagement

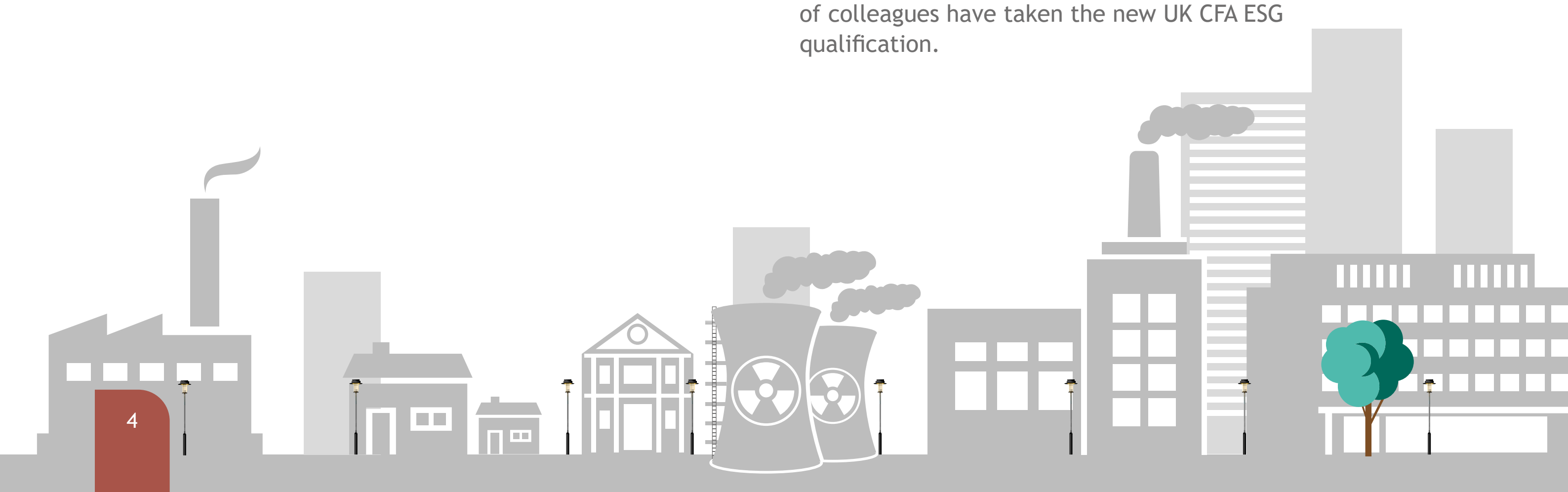
Working with other investors on key engagements makes a huge difference to our effectiveness. Through our membership of the UK Investor Forum we have taken part in most of the major UK collective engagements in 2020, which we look forward to reporting on when they have been concluded. We became members of Climate Action 100+ at the start of 2020, and are part of a working group engaging with one of the world's 100 largest greenhouse gas (GHG) emitters. This UN-supported engagement group has been hugely important in encouraging disclosure of GHG emissions and commitments to reach net zero. We are also in the process of joining Find it Fix it Prevent it, a UK based collaborative engagement focusing on Modern Slavery, especially in supply chains.

Empowering Investment Teams

Every team now has their own login to MSCI ESG Manager, our third-party screening provider and ESG portfolio reporting tool. Additionally, every team has access to the Glass Lewis database of voting recommendations and can provide clients with personalised voting records on demand.

ESG integration into the investment process

We don't separate out the roles of investment manager and analyst and we don't separate out the role of financial analyst and ESG analyst, so the investment process is fully integrated. The pace of change is rapid, updating process, documentation, assurance etc is continuous so maintaining and updating skill sets remains an ongoing challenge. Our teams have shown enormous enthusiasm and dedication throughout the year. Ongoing training programs are extensive. Significant numbers of colleagues have taken the new UK CFA ESG qualification.



Public Policy/Regulatory update – what to expect

There are several new sustainable finance regulations in the pipeline, for both our UK and EU offices. The most recent has been Level One of the Sustainable Finance Disclosure Regulations (SFDR), which was implemented on 10 March 2021. This requires us to disclose on how we integrate sustainability risks and factors into our investment process, as well as disclosing at an entity level how we assess the 'Principal Adverse Impacts' of the investments we make on the environment and society. We were fortunate as a firm that given our ongoing efforts in responsible investment, these new regulations have not changed the way we do things, only the way we disclose them.

However there are more regulations that we are preparing for, including the Level Two of the SFDR, the UK specific version of SFDR, the European Securities and Markets Authority's (ESMA) amendments to the Markets in Financial Instruments Directive II (MiFID II) and the new EU Sustainable Finance Taxonomy! These regulations aim to provide a common framework for assessing sustainable investments, preventing greenwashing and providing better transparency as well as more choices to clients. We have a dedicated team of front office managers, responsible investment experts and regulation experts who are working to ensure that we are not only well-prepared for this incoming regulation, but that we can exceed expectations while continuing to offer first class solutions to our clients.

Policies Update

Responsible investment policy

Our responsible investment policy outlines our commitment to generating superior risk adjusted returns for our clients, by investing in companies that will create long-term value for all stakeholders. As part of this we recognise how environmental, social and corporate governance (ESG) factors and voting and engagement activity can influence the prospects and financial performance of our investments and play a key part in our responsibility to society, stakeholders and our clients.

Stewardship code

Smith & Williamson are committed long term responsible investors and good stewards of our clients' assets. As such we are signatories to the UK Stewardship Code, for which we were awarded Tier 1 status. We have recently submitted our first report for the new Stewardship Code 2020 rules.

Proxy voting

As part of our commitment to both the UK Stewardship Code and the UN PRI, our proxy voting activity policy is regularly updated and builds on the Glass Lewis policy. The materiality threshold we apply to proxy voting was expanded over the previous year to include all AIM stocks and our voting policy covers this.

SRD II & engagement

Smith & Williamson is happy to announce that its offering to clients to meet the new EU requirements to non-discretionary clients went live in September.

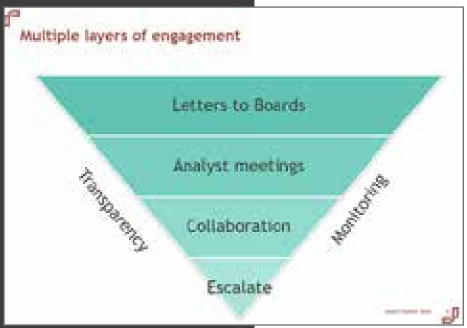
UN PRI

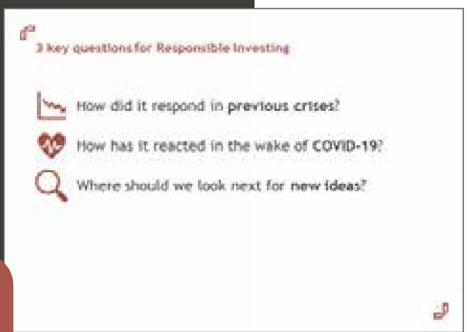
Smith & Williamson believes in being fully transparent in our UN PRI reporting and full transparency reports can be found on our website.

Sustainable Disclosure Policy

We recently published our Sustainable Disclosure Policy in line with the EU SFDR. This policy will be applied across the business, but is only a regulatory requirement for our Irish office and Irish listed funds. The policy describes how we incorporate sustainability risks and factors into the investment process and commits Smith & Williamson to reporting on the Principal Adverse Impacts of the investments we make on the environment and society.

Highlights from our Events





London Charity Conference

Due to the COVID-19 pandemic the Smith & Williamson (S&W) London Charity Conference was held as a virtual event. One of the webinars focused on Stewardship and Engagement; Responsible investment is more than just ESG. While Environmental, Social and Governance (ESG) screening is often at the forefront of discussions about responsible investment, stewardship and engagement is an essential and often overlooked part of the process. Our webinar discussed how our fiduciary duty to investors is incorporated as part of our commitment to the UK Stewardship Code and to the UN supported PRI. The topics included:

- What is stewardship
- The Stewardship Code
- Proxy voting
- Engagement
- Our record and case studies

Responsible Conference

We held our inaugural Responsible Investment Conference in December which was widely attended. These will become regular events through the calendar.

Topics covered included:

- How to make a difference with your investments. Understanding how you can invest sustainably and ensure your money is being put to good use.
- How can the UN Sustainable Development Goals (SDG) be used in investment? How can we use the UN SDGs in an investment context? Looking at ways we can use the goals to understand the world's greatest societal challenges, analyse the impact of different assets, and measure progress on positive ESG outcomes in portfolios.
- Climate change: Investing for the Future - Understanding the potential impacts of climate change on society, alongside public equity and debt markets, while also looking at the risks and opportunities created and understanding carbon as an emerging asset class.
- Navigating the Green Maze - What to look for when selecting sustainable funds for your portfolio.

Charity Trustee Training Webinar

At a recent Trustee Training webinar 'Responsible Investing after COVID-19', we discussed the outlook for Responsible Investing after COVID-19, covering:

- How have ESG metrics influenced performance in previous crises vs the current crisis?
- Why have companies with high ESG scores continued to outperform?
- Where should we be looking next – what are the key themes coming out of this crisis and where should responsible investors be looking now?

Webinar with Broadridge:
SRD II A case Study

We recently spoke at a webinar organised by Broadridge talking about our journey towards becoming SRD II compliant to an audience of wealth management firms

Introduction

Our starting position

The drivers were client demand first, and legislation second.

- Smith & Williamson became signatories to the UN supported PRI & UK Stewardship Code in 2018 because this has become non-negotiable for a number of our clients.

We have a duty to vote, but also to engage actively, to develop our own voting policy (not just use the policy of a proxy voting advisor) and to make public our voting & engagement records.

We do this with quarterly updates and an annual stewardship report. We also have to make sure that everything we do is documented and auditable.

Our requirements

At Smith & Williamson we hold around 5,000 securities in 34,000 client segregated portfolios in both the UK and Ireland. Voting had to cover both UK and Global equities, investment trusts & all AIM stocks.

Our solution had to work for our book of mainly discretionary portfolios, but also, we had to develop a solution for the non-discretionary accounts. We had to have the flexibility to opt out of individual stocks and/or whole portfolios.

We needed to appoint a like-minded proxy voting advisor that could cover everything we needed, including being able to generate detailed individual and collective voting records for reporting.

We needed to develop our own internal policy and procedures and, finally, we had to be able to provide access to our investment teams.

Our solution had to be efficient and reliable - cost effective - so outsourcing was always going to be important.

Our Solution

Working Group
Operations Team to handle IT and Administration, legal/contracts.

SRIG Team - to handle voting mechanism, options & operation also internal, external communication. We have a team of two who manage this whole area full time.

Proxy voting advisor plus a host of enthusiastic investment managers who help make the voting decisions

- Needed to be able to cope with a wealth manager with thousands of accounts rather than a big institutional manager with only a few accounts
- Able to work with Broadridge who manage the digital voting system
- A firm whose philosophy & voting policy was aligned to our own
- Global coverage - over 50% of our holdings are non-UK, but also coverage of AIM stocks and Investment Trusts
- Individual client reports as well as aggregated reports
- Good user interface and widespread access to data
- We chose Glass Lewis - it has taken time to optimise its systems to cope with the number of separate accounts but it is working really well now

Voting
With over 10,000 resolutions a year, we need to focus resources on the resolutions that matter. We vote with our analysts unless the proxy voting manager says there is a problem - that gives us 200-250 resolutions a year.

There are lots of grey areas, hence the need for our own policy. We always have three people sign off on each resolution and we involve the analyst's advice.

We are careful to keep a full audit trail - not least because we can and have voted against clients from other parts of the business.

We try to make decisions within 48 hours of each AGM statement received and write to the company so they have an opportunity to provide clarification and we can change our vote if they make a good case.

Reporting / Communications
We use the Glass Lewis reports for our engagement with individual companies so they have to be accessible to the analyst team. Also, if a client wants to know their own voting record, that can be run by their investment manager on an ad hoc basis and we have to have the group data to publicly disclose our voting records as part of our obligations to the PRI and UK Stewardship Code.

Voting & engagement record

Engagement with companies to improve environmental, social and governance performance of investee companies is a vital part of our responsible investment process.

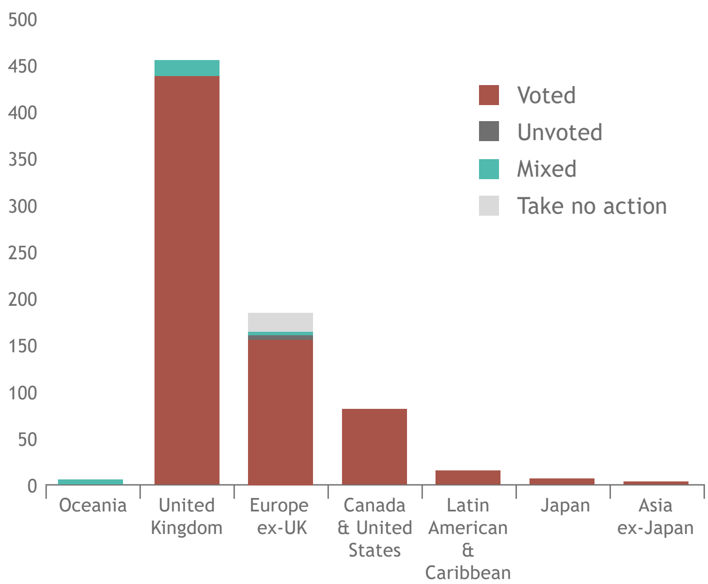
Voting & engagement in 2020

10,496 resolutions

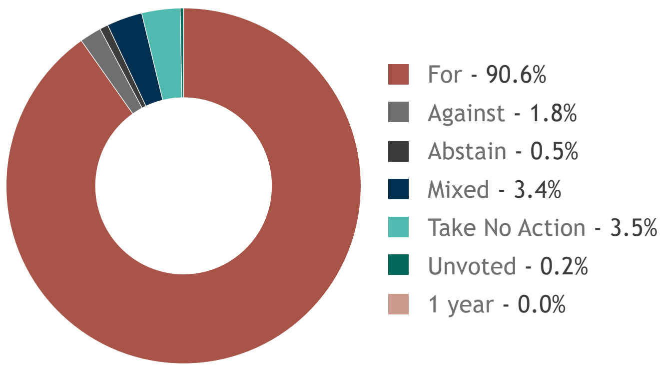
500 company meetings

644 AGMs

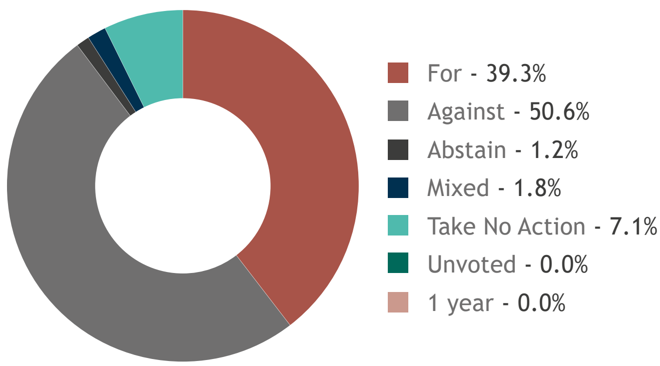
Meetings by region and vote status



Management proposals - votes cast



Shareholders proposals - votes cast



Voting in action

Pearson Plc - We decided to vote against the remuneration policy of the newly appointed CEO. We recognise that some discretion may be required to attract and motivate a new CEO, but we had reservations over the aggregate size, vagueness and non-demanding performance conditions used to decide the final payout.

Ceres Power Holdings Plc - We abstained from voting for the appointment of the auditor and the authority to set fees. While we note that the Company has a track record of disclosing the fees paid to its auditor, it did not for the most recently completed fiscal year. As such, we were unable to assess the remuneration paid to the auditor in the past fiscal year.

Victoria Plc - Our proxy voting service provider had concerns over the general authority to make market repurchases of shares and advised to vote against this resolution. We noted that the terms of the proposed repurchase exceeded the conventional limit. However, we assessed that in the unlikely event that the company did repurchase shares up to the maximum permitted, it would be likely to be generally beneficial to other shareholders. As such, we decided to vote in line with the board.

Exxon - We backed a shareholder proposal requesting additional disclosure on climate change-related risks. There have been concerns over the rising risks of accidental chemical releases from petrochemical facilities in the Gulf Coast of the United States due to extreme weather events, which have become more frequent and severe as a result of climate change. This proposal was meant to enable investors to better understand the public health risks associated with these facilities.

Johnson & Johnson - We voted in favour of a shareholder proposal asking for a comprehensive report on the company's response to the opioid epidemic. Opioid abuse is a public health crisis in the US. The company had offered to pay $4 billion to settle over 2,000 lawsuits by state and local governments claiming that the company's marketing of opioid drugs, as well as its sale of opioid active ingredients to other drug makers, contributed to the opioid crisis. The aim of this proposal was to allow shareholders to better understand how the company is managing and mitigating risks associated with its role in the crisis.

Glass Lewis (GL) is our proxy voting service provider. We have developed our own voting policy, but we rely heavily on Glass Lewis to provide voting research and to keep us abreast of the legislative changes in all the different jurisdictions where we vote. Both policies focus on transparency and communications; corporate culture; strategy; financial disciplines, structure and management; stakeholders, environmental and social issues; and governance.

The polices are influenced by best practice in each country, taking into account local guidelines and governance codes. We have great respect for the Glass Lewis policy, and where we differ tends to be in the detail rather than the broad principle. In particular we are able to make use of the detailed understanding our sector analysts have of our investments which can allow a more nuanced and less rule-based approach. In most cases, we vote with management, after all a key criterion of our investment process is that the investment has an executive team that we respect. Where we vote against management, the Stewardship & Responsible Investment Group (SRIG) assesses the vote and passes it to the relevant direct/ collective analyst where necessary for advice. The SRIG includes amongst others, Head of Charities, Head of Investment Risk and responsible investment (RI) specialists.

The chart shows that in the majority of cases we have voted in line with management. Most of our votes against management have been either board structure or compensation related. On nearly 100 occasions our view differed from that of GL, mainly on board related issues. Our in-house sector specialists conduct in-depth research by holding over 500 meetings with companies' management each year. We believe that our specialist knowledge can put us in a superior position, especially when it comes to AIM, investment trusts and UK stocks and therefore we are better placed to make decisions.

Votes vs management

Proposal Category Type	For Management	Against Management	Take no action	Unvoted	Mixed	N/A	Total
Audit/Financial	1792	23	55	4	72	0	1946
Board Related	4119	95	186	7	134	4	4545
Capital Management	1774	27	22	4	78	0	1905
Changes to Company Statuses	478	12	18	1	21	0	530
Compensation	1036	61	57	1	41	0	1196
M&A	34	2	0	0	0	0	36
Meeting Administration	37	3	25	0	0	0	65
Other	98	3	1	0	3	0	105
SHP: Compensation	18	2	0	0	0	0	20
SHP: Environment	10	4	6	0	2	1	23
SHP: Governance	30	40	6	0	1	0	77
SHP: Social	26	22	0	0	0	0	48
Totals	9452	294	376	17	5	352	10496

Our in-house voting policy can be found on our website https://smithandwilliamson.com/en/stewardship-responsible-investment/

Due to COVID-19, we saw a real change in how the proxy voting season took place. Many AGMs were postponed, resulting in an unusually high number of meetings in the second half of the year. This resulted in the proxy season lasting longer than in previous years. We also noted that many AGMs were held virtually. In these occurrences, we closely monitored proxy statement disclosures and engaged with companies not providing shareholders the same participation rights as the ones they would have had at an in-person meeting.

As we worked from home for most of the year, we modified our voting process to enable us to continue voting in these circumstances. For this, we worked closely with Broadridge, the intermediary we use for our proxy voting, and Glass Lewis. This ensured that we avoided any disruptions in our voting.

This was not only a year of adaptation but also a year of further integration of our responsible investment strategy. We started to vote systematically on all AIM companies. We also rolled out Glass Lewis access to our analysts and thus to their investment teams. They are now able to see company research and proposal data for all companies where we have a qualifying ballot.

Finally, we went live with our SRDII voting process (the EU's revised Shareholder Rights Directive) on 1 September 2020 for non-discretionary clients, all on time. We have been compliant with SRD II for discretionary clients since late 2018. SRDII took effect in the UK on 10 June 2019. Firms that provide investment management services to certain types of institutional investors are required to publish a shareholder engagement policy explaining how they engage with companies in which they invest, and annual information about how the policy has been implemented. Our in-house engagement policy can be found on our website.

Case Study - Voting & engagement

Who?

BlackRock North American Income Trust (referred to BlackRock below)

The backgound

The UK 2018 Corporate Governance code recommends the board appoint one of the independent non-executive directors to be the senior independent director (SID). As this code does not consider the Company's chair as independent, the SID has the role of acting as an intermediary for other non-executive directors and shareholders when necessary; to lead the non-executive directors in the oversight of the Chairman and to ensure there is a clear division of responsibility between the Chairman and Chief Executive.

Contrary to this UK best practice, BlackRock had not appointed a SID.

Our engagement

We wrote to the Chairman of BlackRock, Simon Miller, to inform him of our intention to vote against the re-election of Andrew Irvine at the AGM on 20 March 2020. As Chair of the nominations committee, our view was that Mr Irvine was responsible for ensuring the appointment of a SID. We outlined to the Chairman our opinion that an independent senior director is better able to oversee the executives of the Company and set a pro-shareholder agenda without management conflicts. This, in turn, leads to a more proactive and effective board of directors. In this case the Chairman was an affiliated director.

The response

Following on from our letter to the chairman of Blackrock, we received a call from him. Mr Miller asked us to reconsider our vote. He explained that the board as it stands is very competent and they had felt that investors were happy, so did not see the need to go through the expense of hiring a SID. He added that if we felt very strongly about this, they would investigate hiring a SID following the meeting and make an announcement to this effect, with the provision that we change our vote ahead of the meeting. We felt that his explanation was satisfactory and after some discussion, we decided to change our vote.

We then received a letter from BlackRock, on the day of the AGM, informing us that further to our letter to Simon Miller, and subsequent discussions, the board had appointed Ms Alice Ryder, one of its non-executive Directors, as a SID on 20 March 2020. It made a public announcement to this effect.

Who?

Jupiter US Smaller Companies (referred to as Jupiter)

The backgound

Due to COVID-19, many companies held virtual annual general meetings. Jupiter proposed the adoption of new articles to permit future general meetings to be held as a physical or electronic meeting, or a combination of both.

Our engagement

We wrote to the Chairman of Jupiter, Gordon Grender, to inform him of our intention to vote against the adoption of new articles at the AGM on 22 December 2020.

We recognised the current context of the COVID-19 pandemic. However, we expressed our concerns about the potential for future general meetings to be held on a wholly virtual basis even when COVID-19 should not be an issue anymore. We wanted the company to provide a convincing rationale for the use of hybrid/virtual meetings or provide assurances that shareholder participation would not be affected by the format of these meetings.

The response

In response to our letter to the chairman of Jupiter, we received a call from him. Mr Grender explained to us that the proxy wording was imperfectly drafted and told us that it was the board's intention to return to "in person" meetings as soon as it possibly could. He mentioned that he would make clear the board's intention at the AGM.

This reassured us. However, as the resolution was not formally re-drafted, we did not change our vote and voted against the resolution.

Who?

Airbus

The backgound

It is customary for companies in the Netherlands to submit the actions of executive and non-executive directors during the year for shareholder approval. The discharge from liabilities is binding for all shareholders and can hinder legal claims against board members. Moreover, it protects board members against claims for damages from the company.

Airbus came under fire when it submitted the actions of executive and non-executive directors during the year for shareholder approval, as it does annually. This is because on 28 January 2020, Airbus announced that it had agreed a settlement with French, British and US authorities for €3.6bn (£3bn) following investigations into allegations of bribery and corruption started in 2016. It is the largest global bribery settlement to date.

On another topic, Dutch legislation, in line with local corporate governance recommendations, contained a transitional clause regarding gender diversity. The clause expired on January 1, 2020. In February 2020, it was announced that a bill proposing a hard gender quota would be submitted in the following months. Under the new rules, if proposed nominees do not lower the gap towards compliance, appointments will be annulled.

Airbus had not yet met this requirement, with the proportion of the female representation on the board of Directors at 25% at its 2020 AGM, below the one-third target.

Our engagement

We wrote to the Chairman of Airbus, Denis Ranque, to inform him of our intention to abstain from voting for the re-election of Lord Paul Drayson and vote against the ratification of the executive and non-executive director's acts at the AGM on 16 April March 2020.

We expressed our concerns that the Company failed to bring its board into compliance with the Dutch law requirement on gender diversity, despite being given seven years to comply. Airbus did not disclose any convincing explanation or plan to address the gap in board gender diversity. We noted that the chair of the nomination committee was not held for re-election. As a result, we voiced our concern through the re-election of Lord Paul Drayson, a member of the remuneration & nomination committee since 2017.

We also shared our concerns that ratifying the actions of executive and non-executive directors would not allow for proper oversight and accountability on previous allegations of illegal activities including bribery.

The response

Thorsten Fischer, the Head of Investor Relations, and Auriane de Soultrait, the Head of Governance and Stakeholder Relations called us to discuss these concerns.

During this meeting, the management team explained the rationale behind asking shareholders to ratify the actions of executive and non-executive directors, which is customary in the Netherlands. Their management confirmed that the previous management team at Airbus were duly punished for their misconduct and there had since been a complete overhaul of the board. They also explained what they had done to make sure this could not happen again, and so shareholders would be better protected in the future. They have issued a new code of conduct with practical guidance and have delivered training to all employees.

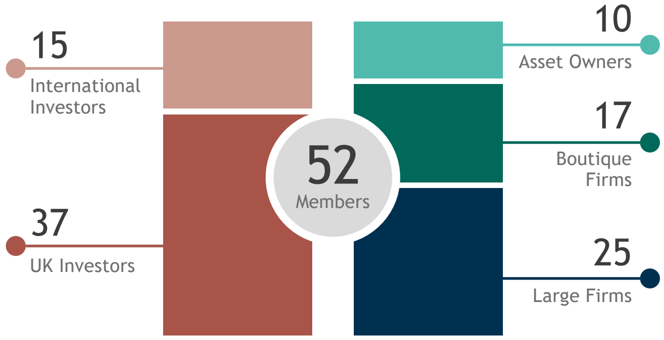
Finally, we discussed the lack of diversity on the board at Airbus. The company explained that it has attempted to increase representation at the board level, but it remains difficult. They have strict selection criteria, requiring expertise in the areas of finance, business and aircraft. They had found a female representative for the board with these skills, but she had taken a job elsewhere. This is an area where they are actively looking to improve.

The group's explanations were reasonable and addressed each of our concerns. We were encouraged by the way they had engaged with us and with other minority shareholders but did not amend our vote.

Collaborative Engagement

We are members of the Investor Forum, a community interest company set up by institutional investors in UK equities. The Forum helps investors to work collectively to escalate material issues with the boards of UK listed companies.

Membership



-£20tn in Global AUM

-£695bn Invested in UK Equities

-33% FTSE All-Share Market Cap

Source: The Investor Forum

Barclays collaborative engagement with Investor Forum

Company BARCLAYS PLC	Oversight (by the Board)					Execution (by the Management team)		
	Strategy	Leadership & Succession	Capital Allocation	Corporate Governance	Corporate Action	Operational Performance	Management Information	Reporting & Communication
	✓	✓						
Phase 1:								
Timeframe: Mar 19 - Jan 20	Size: FTSE100		Number in Engagement: 18			Combined Shareholding: 18%		
Phase 2:								
Timeframe: Jan 20 - Dec 20	Size: FTSE100		Number in Engagement: 22			Combined Shareholding: 26%		

Source: The Investor Forum

The background

This engagement was broken down into two phases: the first was to emphasise the long-term investor priorities. The second phase looked at conveying the importance of climate concerns and how they were a material issue for the business. We wanted the business to set clear climate ambitions and to engage with ShareAction (a registered charity that promotes Responsible Investment by campaigning to improve corporate behaviour on ESG issues).

Our engagement

This engagement involved the largest number of participants in any engagement to date. The Investor Forum wrote to the board to express member views and then engaged extensively with the Chair in a series of constructive conversations. The Investor Forum worked extensively with Barclays, ShareAction and investors to encourage ambitious climate commitments and to avoid a proxy battle.

The response

Following the engagement, Barclays outlined landmark climate ambitions ahead of the 2020 AGM and gave a commitment to providing greater granularity on its climate strategy before the end of 2020. At the AGM, two climate related resolutions were raised and while they did not go as far as ShareAction’s resolution, the group committed to “transitioning” its energy exposure. The board’s recommended resolution received almost complete support while the shareholder resolution received 23.9% support of the votes cast. Following on from this in November 2020, the bank reported on actions taken since the AGM. It has issued new targets for 2024 and has also committed to further action and enhanced reporting.

Climate Action 100 Update

Climate Action 100 is the world's largest investor engagement initiative on climate change. It focuses on 160 companies with significant greenhouse gas (GHG) emissions. These companies are critical to the net-zero emissions transition and to meeting the objectives of the Paris Agreement.

We are currently in a working group engaging with Walmart on areas such as

- Strengthening its reporting under the TCFD rules (Taskforce for climate related financial disclosures)
- Transparency surrounding its industry associations and climate lobbying
- Project Gigaton (which relates to its GHG emissions)
- Climate scenario analysis

Walmart has recently announced a new target to achieve net zero GHG emissions by 2040 (scope 1 and 2). As part of this the company will protect, manage or restore 50 million acres of land and 1 million square miles of ocean by 2030. Our engagement is ongoing, and we will report again in the future.

Focus companies by sector

- 39 Oil and gas companies
- 23 Mining and metals companies
- 31 Utilities companies
- 26 Industrials companies
- 26 Transportation companies
- 14 Consumer products companies

Climate action 100+ at a glance

- 545 Signatory investors
- $52 TRILLION Signatory assets under management
- Investor signatories in 32 MARKETS
- 160 Focus companies in **32** markets
- Companies engaged by the initiative are responsible for an estimated 80%+ of global industrial emissions
- Total market cap for all focus companies is $8.4 TRILLION

Source: Climate Action 100

Find it Fix it Prevent it update

Find It, Fix It, Prevent It is an investor led, multi-stakeholder project designed to harness the power of the investment community to increase the effectiveness of corporate actions against modern slavery. The initiative was launched by CCLA and Rathbones and now has over 100 investment firms and asset owners as signatories. CCLA provides secretarial services and hosts the website, while the core research is provided by the University of Nottingham.

The initial focus was 15 UK-listed companies within the ‘hospitality sector’, but this is being extended to other vulnerable sectors - the building materials sector is targeted next. Companies will be allocated to investors on a ‘lead and support basis’ and members of the project will meet regularly to share progress and best practice. We are in the process of signing up to take part in this collaborative engagement going forward and look forward to giving more details in our next report.

What is COP 26?

And why is it important for investors to take note?

(Originally published March 2021)

What is COP?

COP stands for Conference of the Parties, and refers to the decision-making body of the United Nations Framework Convention on Climate Change (UNFCCC)

It was at COP21 in Paris that the Paris Agreement was adopted, the agreement being a legally binding international treaty on climate change.

The Paris Agreement

The goal of the Paris Agreement is to limit global warming to well below 2, preferably to 1.5 degrees Celsius, compared to pre-industrial levels.

More bureaucratic and complicated shorthand…

COP, which is the supreme body of the Convention, shall serve as the meeting of the Parties to the Paris Agreement.

All States that are Parties to the Paris Agreement are represented at COP. Other States may participate as observers.

The meeting of the Parties to the Paris Agreement is referred to as the CMA. The CMA oversees the implementation of the Paris Agreement and takes decisions to promote its effective implementation.

The Agreement works on a 5-year cycle of increasingly ambitious climate action carried out by all signatory countries. It came into force on 4 November 2016.

In 2023, and every five years thereafter, the CMA undertakes a 'Global Stocktake', a temperature check on the implementation of the Paris Agreement and an assessment of collective progress towards limiting global warming.

And COP26?

This will be the 26th annual session of the Conference of the Parties to the Convention (COP26). It is going to be hosted by the UK in Glasgow, from 1 to 12 November 2021, after having been delayed by a year due to the COVID-19 pandemic.

At the summit, delegates including heads of state, climate experts and negotiators will come together to agree coordinated action to tackle climate change. Parties are expected to put forward their revised Nationally Determined Contributions (NDCs), which contain details of climate change mitigation and adaptation actions in addition to those outlined in the 'intended nationally determined contributions' which were submitted ahead of COP21 in Paris.

The UK submitted its NDC in December 2020, which can be found here **https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/943618/uk-2030-ndc.pdf**

The NDCs submitted for COP26 are expected to include targets for more ambitious reductions in emissions of greenhouse gas emissions with 2025 or 2030 targets.

As well as the negotiations, there will also be space for countries, international organisations and other delegates to showcase climate action, highlight diverse climate change issues and share knowledge.

The USA, under President Biden, rejoined the Paris Agreement on 19 February 2021. The President himself may be attending the summit in Glasgow.

This is also a defining moment for Boris Johnson, who has the opportunity this year to present himself as a world leader. The UK also assumes presidency of the G7 in 2021, which will be held in Cornwall. If Mr Johnson is able to extract further commitments from the other Parties, his stewardship may be considered a success. A significant area of interest is green finance, where the Bank of England is a notable leader in international finance, having launched the TCFDs in December 2015.

COP26 is being held after a year of global lockdowns and recovery from a global recession. This could alter the exact nature of targets set by different Parties, although many have increased their commitment to climate action through 2020. We expect companies to follow suit, releasing their own targets and commitments to highlight their green credentials.

Issues that will be discussed at COP26

- **Carbon market mechanisms,** notably an agreement on the rules to govern international carbon trading under the Paris Agreement. This will allow a country to purchase carbon credits (reductions) from another to offset their own emissions. (See our Carbon Pricing Primer here)
- **The funding for loss and damage.** This refers to the loss and damage experienced by developing countries from human induced climate change. These countries are particularly vulnerable to the adverse impacts of climate change.
  This is supported by the Warsaw International Mechanism (WIM), the international mechanism designed to help countries deal with the impacts of climate change when they occur.
  The 'Loss and Damage' pillar of the UNFCCC negotiations arose from the recognition that there are limits to how much it is possible to adapt to the impacts of climate change: when these limits are reached, losses and damages occur, because the actions needed to adapt are unaffordable, not physically or technically possible, socially difficult or simply not sufficient to prevent some harm to humans, the environment and assets.[1]
- The mobilisation of **$100bn a year in climate finance** to support climate action in developing countries. COP26 is also likely to set the next target for climate finance to be achieved by 2025.
- COP26 will begin to discuss how to integrate **nature-based solutions (NBSs)** into the Paris implementation strategy. NBSs can refer to a number of different things, with actions focused on the protection, restoration and sustainable management of the world's ecosystems – in order to increase climate mitigation and adaptation, as well as support sustainable development and protect and promote biodiversity.
  NBSs are more complicated than simply tree-planting. In fact, in some cases monoculture plantations or planting the wrong kinds of trees can undermine climate and biodiversity action.[2]

Areas of interest for investors

The acceleration of climate action globally will have ramifications across financial markets.

- There will be increased demand for companies that provide **effective efficiency or clean energy solutions and technologies.**
- There will be growing regulatory pressure on companies with higher carbon emissions, with the focus on carbon market mechanisms likely to affect operational costs with the **increasing cost of carbon.**
- Loss and damage should be an area of interest for investors, with companies that have operations in vulnerable geographies at **risk from sudden and extreme weather events.**
- There is likely to be some focus, and scrutiny, on the **use of carbon offsets.** Many experts agree that carbon offsetting is necessary for us to achieve the goals of the Paris Agreement and it is a tool many corporations are electing to use. The legitimacy and efficacy of these offset schemes are of the utmost importance.

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[1] www.lse.ac.uk/granthaminstitute/news/addressing-the-impacts-of-climate-change-through-an-effective-warsaw-international-mechanism-on-loss-and-damage/

[2] https://nature4climate.org/news/momentum-for-nature-based-solutions-continues-to-grow-despite-disappointing-un-climate-talks/

Changing the world with investments

How you can make a difference with your savings

(Originally published December 2020)

Over the past few years, many more people have been making changes in their day to day lives to try and make a small difference in the world. Maybe you take a reusable cup to the coffee shop, try to reduce your consumption of fast fashion or take fewer car journeys. Maybe your contribution is volunteering in the local community or donating to charity.

One effective change that should not be overlooked is the difference we can make with our savings and investments. Responsible investing is a more holistic approach to investment, which aims not simply to make a profit, but also to bring in an analysis of ESG factors to look at how these factors might impact the valuation of an investment, perhaps through the extra cost of dealing with high carbon emissions or lower revenue growth as people switch to more sustainable products. Different approaches can be tailored to your own set of values, whether you are more interested in decarbonisation or social impact.

There are some interesting benefits to aligning your investments with your values, on both an overall impact and a personal level.

Cumulative effect

According to a study by Morgan Stanley, 85% of the population are now interested in sustainable investing, up 10% from five years ago. This rose to 95% for 18 to 37-year olds[3]. It is clear there is an ever-growing pot of personal wealth earmarked for those companies with more sustainable practices: investors and companies are taking note. We are already seeing changes to what is considered good practice. Even the major oil companies are now committing to net carbon zero targets, which would have been unimaginable a decade ago.

With each pound of savings that goes towards responsible investment, the cumulative pressure on corporations to improve their environmental and social policies increases. Each additional share held by asset managers on behalf of clients gives them greater traction for voting and engagement. This is where investors can really communicate with companies on the changes they want to see.

Better returns

There is also growing evidence that incorporating ESG criteria may generate better risk-adjusted returns[4]. There are a number of reasons why this may be the case: the most widely accepted is that ESG analysis, which covers a number of elements including climate change, resource scarcity, labour relations, cyber security, shareholder rights and board transparency, recognises non-financial factors could have a significant impact on the long-term financial performance of a company. By considering these factors, investors are more likely to avoid controversy while also making sure that they are invested in companies with good governance, risk controls and that think about the future.

At Smith & Williamson we created, using a set of quantitative tools and qualitative assessments, a list of responsible companies. These companies have positive products or services, have good relations with all stakeholders and strong management. Perhaps surprisingly, this condensed list includes an airline, oil and gas companies and mining companies, reflecting improving business practices and sustainability. This list outperformed our wider monitored universe by over 40% in the year to 30 September 2020[5]. In this period, it really has paid to be responsible.

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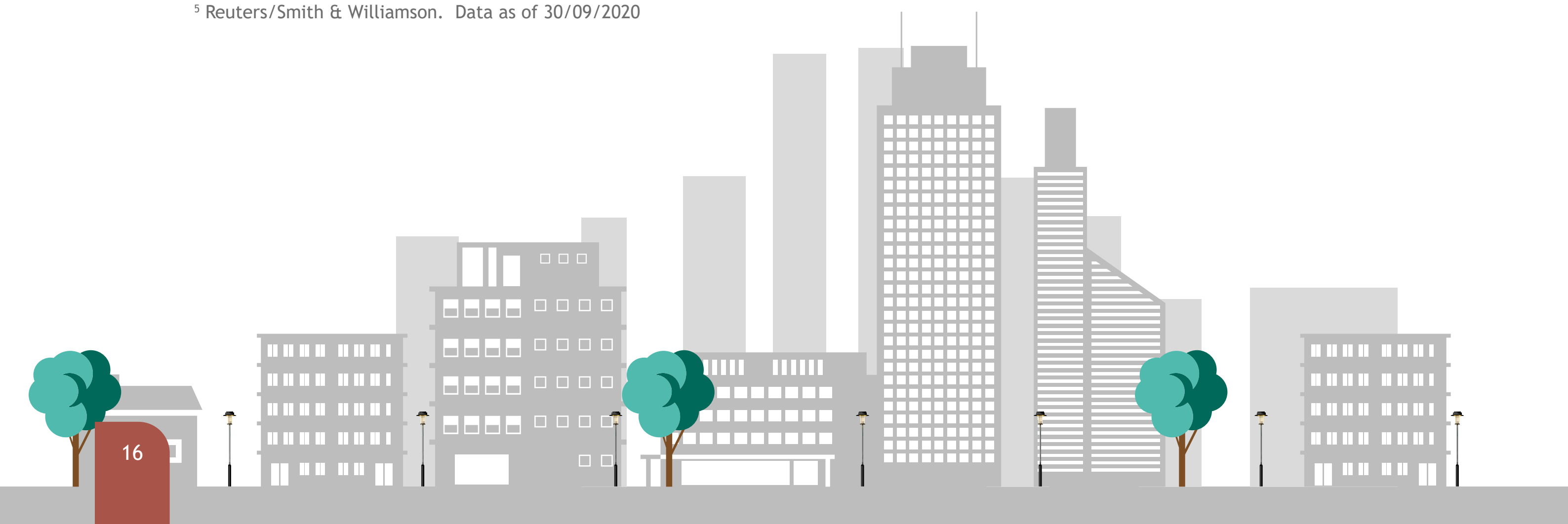
[3] Morgan Stanley Institute for Sustainable Investing: Sustainable Signals -- The Individual Investor Perspective (2019)

[4] Bassen, A., Busch, T. and Friede, G. (2015). “ESG and financial performance: aggregated evidence from more than 2,000 empirical studies”. Journal of Sustainable Finance & Investment, 5(4).

[5] Reuters/Smith & Williamson. Data as of 30/09/2020



What are the key issues that matter to you?

Responsible investment is varied in its styles and approaches. The broadest approach seeks to find companies that perform favourably using ESG metrics. Accordingly, no one issue or theme is targeted. More tailored and specific approaches can be adopted, and many clients have several specific topics in mind when thinking about sustainability.

Unfortunately, this is where an approach to responsible investment can become a little more complicated. Not all goals are compatible with one another, and many more cannot be viewed in black and white.

For example, many investors look at Alphabet (parent company of Google), which improves access to education. This has come into greater view over the pandemic, with many schools using the free Google Classroom application to deliver online classes. Additionally, the classic Google Search goes a long way in the democratisation of information and education. Knowledge is no longer just a privilege for the wealthy and academic elite. With access to a device and Wi-Fi, you can read up on almost any subject.

However, with this comes the negatives of a mammoth US technology company with an unprecedented monopoly on internet usage, or in the words of the US Department for Justice: "Google is now the unchallenged gateway to the internet for billions of users worldwide"[6]. The key issues surrounding Alphabet are those of data collection and privacy, tax avoidance and antitrust – though there are undoubtedly many more.

All this is not to discourage would-be responsible investors, but to encourage them to explore the key issues that they would want to address and consider the best way this could be achieved. In many cases, companies that are positive in some areas are inadvertently negative in others. Sometimes avoiding negative areas in the market is not the best solution. See more here: **https://smithandwilliamson.com/en/insights/covid-19-low-carbon-portfolios-and-divestment/**

Find a wealth manager that votes

The best way to ensure that your money is being used well is to ensure your manager votes. Using active ownership to influence positive changes is one of the best ways to encourage change.

Given the short-term nature of stock markets, the time and money companies need to transition to a more responsible approach can impact the next set of quarterly results. Voting and engagement ensure management understand that investors want positive action and can highlight their shareholders' specific ESG expectations. It also allows investors to understand the challenges and opportunities a company faces and better shape their expectations. So, when you are considering what more you can do to make a difference in the world, maybe consider how your savings are invested. It could prove to be the biggest change of all.

[6] https://uk.reuters.com/article/us-tech-antitrust-google-quotebox/factbox-key-arguments-in-u-s-antitrust-suit-vs-google-idUSKBN2752BU

Low Carbon Portfolios and Divestment

Why investing in low carbon portfolios may not be the solution for climate change

(Originally published July 2020)

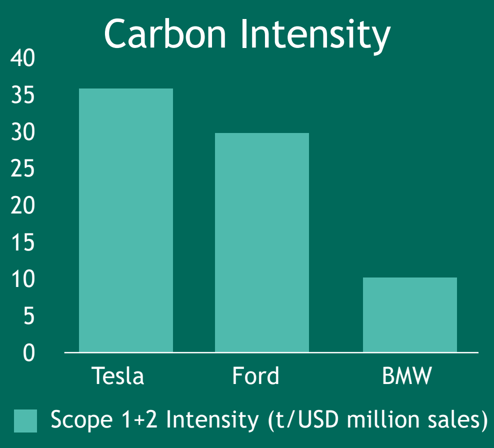
The Coronavirus may have proved a temporary distraction, but climate change remains public enemy number one in 2020. We are nearing the limits of our ability to mitigate the impact of climate change and keep to global targets of a 1.5 degree increase in temperature. The International Energy Agency has predicted that we need to invest $3.5tn in energy-sector investments each year until 2050, to be in with a chance of limiting global warming to 2 degrees.[7]

More and more of our clients are now anxious to see how they can use their own investments to help close this funding gap and encourage the transition to a low carbon economy. This objective is reasonable and understandable, but simply reinvesting into low carbon portfolios may not be the most effective approach. Investors need to take a considered view on the best options to support the transition to a low carbon economy.

Sustainable Technology Can Be More Carbon Intensive

Tesla is well-known for its investment in sustainable solutions, including battery storage and, of course, electric vehicles. However, Tesla is more carbon intensive than, for example, Ford or BMW.

To be fair to Tesla, the figures used here are only Scope 1 and 2, or - in layman's terms - the emissions generated by the company's own operations and the energy used to power these operations.



Source: MSCI ESG Manager

The data ignores Scope 3, where the emissions of the products once sold are included.

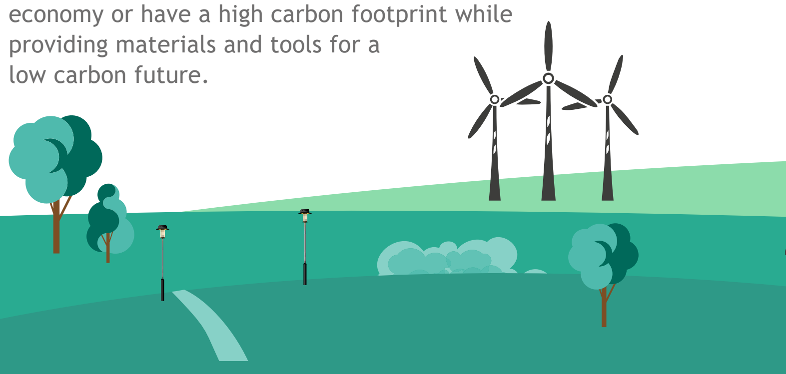
Scope 3 is often excluded because the data is hard to calculate, and most companies cannot or will not disclose. Low Carbon indices and ETFs exclude companies on the basis of Scope 1 and 2. This means low carbon tilts in portfolios can prove a crude measure.

Electric vehicles are currently more carbon intensive to produce, particularly the battery. It is only through the life of the vehicle that it becomes more efficient (and only in countries that don't regularly use coal-powered energy generation).

This means low carbon indices based on Scope 1 and 2 emissions or intensity don't necessarily exclude car manufacturers, even if they are doing nothing to facilitate the transition to a low carbon economy. They do not rule out those companies where emissions are primarily generated by their products once sold rather than in the manufacturing process.

In contrast, a low carbon approach would naturally exclude fossil fuel extractors, homebuilders and miners. Focusing on this last sector, mining is vitally important for many sustainable technologies. Copper, cobalt, platinum, manganese, nickel, lithium (to name just a few) are vital for clean technology. Miners may be dirty, but they are also essential. Some of these companies are mindful of their environmental and social impacts and strive to be as clean and careful as possible. As such, they are a valid and necessary part of the transition: is it right that it should be excluded from a portfolio hoping to encourage a low carbon economy?

While using carbon footprints can generate insights and flag areas of concern, it is a crude tool. It is possible to have a low carbon footprint while doing little to promote the transition to a lower carbon economy or have a high carbon footprint while providing materials and tools for a low carbon future.



The unintended consequences of divesting

Divestment from high carbon intensive companies remains widely used. Global divestments from fossil fuel companies have reached $11trn according to 350.org. The primary targets are largely thought to be the international public companies. However, oil remains a necessary component of our energy requirements and divestment can have some unintended consequences.

International public companies have high disclosure requirements and are subject to considerable scrutiny from the general public. The alternatives are state-owned companies (Saudi Aramco, National Iranian Oil Company, Gazprom, etc.) or private companies. The oversight of these businesses, especially from the public, can be non-existent.

There is a risk with mass-scale divestment that in order to appear cleaner, or to maintain profit for remaining shareholders, big international companies will sell their more problematic assets to the smaller, state-owned or private companies.

This means that instead of well-governed companies, with strong environmental policies and shareholders and the public to answer to, these assets will be managed by those companies who do not face the same oversight and scrutiny.

Though a simplistic view, there is a chance that by choosing divestment the investor is not preventing assets being managed, just changing who is managing them. This could end up being more damaging for the environment.

Who can add the most to the transition?

Looking at overall benefit, bypassing the energy giants in favour of smaller, low carbon alternatives may seem sensible. However, many of these smaller companies also have the resources of smaller companies. Their capital for further green projects or research and development may be fairly limited.

If a titan such as Royal Dutch Shell chooses to commit its considerable resources, experience and connections to energy transition, green research and development, it could have a huge impact. In fact, Shell committed to spending up to $2bn a year on green energy from 2016, with plans to increase this level in 2020. While Shell is currently struggling to hit those targets, the point still stands: if these international oil behemoths were to become greener overall, they have the power to make a far more profound and enduring difference.

Engagement can add the most value

Engagement is a key pillar of the UN supported Principles for Responsible Investment and the UK Stewardship Code. Engagement allows investors with a stake in a company to encourage real change and allows the active investor to generate an impact.

Most companies do not deny the reality of climate change or the risks it imposes on their businesses. However, given the short-term nature of stock markets, putting in the time and money to transition and research can have an impact on the next set of quarterly results. Engagement can ensure management understands that investors want positive action, plus their specific ESG expectations. It also allows investors to understand the challenges and opportunities a company faces and better shape their expectations.

Consistent data across companies and sectors remains a problem. Engagement can help give investors the information they need to analyse carbon related risks and opportunities properly, as well as ensuring they start reporting along established guidelines (this is the main goal of the Taskforce for Climate-related Financial Disclosures – TCFD).

Not all companies will be open to transparent communication or are ready to begin their transition to a low-carbon economy. This is where an investor must take this information and assess if they are comfortable to continue holding the company, both from an environmental and financial risk point of view. Divestment does have a place, but it should be reserved for businesses that can't or won't change.

Sometimes to make a real difference, pragmatism should triumph over idealism. Human beings naturally try to find the simplest solution. Removing association with highly polluting companies is a superficially simple way to reduce the portfolio carbon footprint, but real change can only be created by more thoughtful investment and engagement.

[7] IEA (2017), Investment Needs for a Low-Carbon Energy System, IEA, Paris https://www.iea.org/reports/investment-needs-for-a-low-carbon-energy-system

Is COVID-19 the end of Responsible Investing?

(Originally published April 2020)

Over the past few years Responsible Investing, often known as ESG, has surged in popularity, with more investors wishing to influence positive change with their money. The wider investment industry came to understand that more responsible companies are likely to still be trading in the long-term. However, for every trend there are critics. Their most common refrain is that people only want to invest responsibly during bull markets. So now we've entered into our first bear market in over a decade, is the rise in responsible investment over?

Responsible investing has grown, not only from a desire to keep investments in line with one's values, but also from investors trying to future-proof portfolios in a rapidly changing world. There is growing awareness of the impact corporations can have on societies and the environment and how this needs to adapt in future. More sustainable companies tend to be more resilient with more conservative balance sheets, fewer controversies and good stakeholder relationships. They often play an active role in adapting and mitigating societal challenges, which is likely to be rewarded through future policy and legislation.

Responsible investment has gone from being 'nice to have' to a crucial element in a long-term investment portfolio.

Aside from the theoretical explanations behind the rise in responsible investments, the most recent drop in markets has shown that these kinds of investments tend to fare better during falling markets. As reported in the Financial Times, 62% of ESG-focused large-cap equity funds outperformed the MSCI World Tracker over March 2020.[8]

There is a significant caveat we should add here. While many of these ESG-focused funds may use a best-in-class non-exclusionary approach, many will naturally tend to screen out Oil & Gas, Airlines and Miners. Alongside the inevitable fall in demand for these companies from reduced economic activity, a concurrent oil-price war between Saudi Arabia and Russia began, sending oil future prices into the red.

However, that is not to say that responsibility-based outperformance was purely down to sectoral biases. At Smith & Williamson we have created, using a set of quantitative tools and qualitative assessments, a list of responsible companies. These companies have positive products or services, have good relations with all stakeholders and strong management.

Perhaps surprisingly, this condensed list also includes an airline, Oil & Gas companies and Mining companies.

This list outperformed our wider monitored universe by 15.1% over the first three months of 2020.[9] The future is also looking bright for ESG investors. During a recession, carbon emissions fall year on year due to reduced economic activity. Normally when we emerge from these recessions, governments inject liquidity into the economy to stimulate recovery. In many cases this means large infrastructure projects, factory production starting up again and people regaining employment, all of which push emissions back up[10]. So far in 2020, worldwide promised stimulus packages total over USD 8 trillion[11].

But the world has changed and limiting global carbon emissions has become essential, pandemic or no pandemic. Dr Fatih Birol, executive director of the International Energy Association has urged governments to put clean energy at the heart of their stimulus plans[12].

This has been echoed by the President of the European Commission, Ursula von der Leyen, who has said that "the money in our next budget must be invested in a smart and sustainable manner".

She added that "crucially we need to invest strategically in our future, for example for innovative research, for digital infrastructure, for clean energy, for a smart circular economy, for transport systems of the future. A Marshall Plan of this nature will help build a more modern, sustainable and resilient Europe."[13]

The possibility of even a portion of global stimulus packages going towards clean energy and sustainability could mean huge advances for the low carbon transition and for environmentally responsible investments. It could mean a shift in our corporate eco-system, with companies that have already been preparing for a leaner, greener world reaping the benefits.

Another key shift as a result of the COVID-19 pandemic could be the way governments and societies view the gig economy. Many workers on temporary or zero-hour contracts will have been most hit by the current lockdown. Many have a hand-to-mouth existence and have now found themselves without a job, relying on government benefits (where they exist). If they keep their job, they are more likely to work if they feel unwell because they cannot afford not to.

For these reasons, the gig economy may come under further scrutiny in future. Corporations will also be weighed and measured over their handling of the crisis. Many will have to furlough or let go of staff just to weather the stall in economic activity. But making your lowest paid staff redundant while still issuing full executive pay packages will not go down well with the public. For many companies, their reputation is on the line.

Responsible investors should also be taking note because more stable workplaces with strong labour management tend to have lower turnover and higher productivity. Employees who know that their job could fall out from beneath them at any moment will hardly be encouraged to do their best work.

COVID-19 has been an interesting test of the defensive nature of responsible companies and of responsible investments. They have proved resilient, outperforming the wider market throughout the economic downturn. There is evidence that this crisis is helping to focus minds on investing in a more sustainable future.

So, in answer to the question “is the rise in responsible investment over?” No. It has only just begun.

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[8] https://www.ft.com/content/46bb05a9-23b2-4958-888a-c3e614d75199

[9] 31/12/2019 to 31/03/2020, equal-weighted, GBP. Data sourced from Thomson Reuters.

[10] https://www.washingtonpost.com/climate-environment/2020/03/06/coronavirus-could-halt-worlds-emissions-growth-not-that-we-should-feel-good-about-that/?arc404=true

[11] https://www.bloomberg.com/news/articles/2020-04-23/when-8-trillion-in-global-fiscal-stimulus-still-isn-t-enough

[12] https://www.iea.org/commentaries/put-clean-energy-at-the-heart-of-stimulus-plans-to-counter-the-coronavirus-crisis

[13] https://ec.europa.eu/commission/presscorner/detail/en/AC_20_602

Fast fashion and the legacy of a pandemic

(Originally published December 2020)

2020 proved devastating for countless communities, industries and nations. The fashion retail sector has been hit hard, facing store closures and a drop in customers as more and more people were plunged into economic uncertainty. Notable casualties have included Oasis, Warehouse, TM Lewin, Edinburgh Woollen Mill, M&Co, Peacocks, Jaeger and, of course, Arcadia, owner of the Topshop brand. The Centre for Retail Research has estimated that UK retail administrations this year will have affected over 95,000 employees.

Some of these brands may be saved in one form or another: Boohoo Group has already bought Oasis, Warehouse and Debenhams while Asos has bought a number of brands from Arcadia, including Topshop and Miss Selfridge. However, it is not just the pandemic that is hurting the sector. It is also facing a profound structural shift in the move to online, plus significant environmental and social challenges.

Environmental impact

In the short-term, policymakers' attention has been focused on the pandemic, but it is clear that climate action is likely to form a significant part of the recovery strategy. Governments around the world have already earmarked a significant proportion of their fiscal recovery packages to tackle carbon emissions and climate change.

The fashion industry is in the firing line. It is responsible for 10% of annual global carbon emissions, with global consumption of apparel at 62 million metric tons in 2019[14]. The UN Environment Programme (UNEP) has calculated that it takes an average of 3,781 litres of water to make one pair of jeans. Putting that in context, if the average person drinks 3 litres of water a day, one pair of jeans is equivalent to a person's water intake over nearly three and a half years. This is before we even begin to consider the environmental impacts from the eventual disposal of the apparel (whether from incineration or landfill) or the microplastics found in man-made fibres.

Though this area of retail has managed to escape public backlash for a lot longer than many other industries (energy companies and airlines for example), awareness of the negative impacts of fast fashion is starting to alter the way we consume. According to data from eBay, in June 2020 second-hand sales increased 1,211% from the same period in 2018[15] and more than half of 25-to-34-year-olds now buy second-hand clothes[16].

That said, it would be a step too far to conclude that the bankruptcies on the high-street are caused primarily by a consumer shift towards sustainability. One of the key drivers has been the shift to online shopping, a shift for which newer companies like ASOS and Boohoo have been perfectly positioned. Established brand names have divided into those who could navigate the change (Next) and those that could not (Debenhams).

To our mind, this illustrates the importance of being able to navigate shifts in our patterns of consumption. Although we are unlikely to do without new apparel entirely, we are likely to see a huge shift in the landscape of the industry. Retailers may be forced to rethink their mass production of poor-quality items before long.

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[14] https://www.worldbank.org/en/news/feature/2019/09/23/costo-moda-medio-ambiente

[15] https://fashionunited.uk/news/fashion/uk-s-secondhand-market-skyrocket-in-2020/

[16] https://www.drapersonline.com/news/more-than-half-of-young-shoppers-buy-second-hand-clothes

Social impact

Let's not forget that the fashion industry has a social cost as well. In the UK there have been scandals from Boohoo and Sports Direct on worker exploitation, with dangerous work conditions and low pay. This is more shocking because it happened in one of the world's wealthiest countries though tales of exploitation are replicated across the world.

This is illustrated by the Rana Plaza incident in Bangladesh in 2013. Rana Plaza was an eight-storey commercial building that included five garment factories producing clothing for large brands such as Primark, Matalan and Benetton. On 23 April 2013 structural cracks appeared on the lower floors of the building, leading businesses on the ground floor (shops and a bank) to be evacuated. The next day, garment workers were told to return to their posts in the factories. Within hours, the building collapsed[17] and 1,134 people lost their lives.

These garment workers were paid the minimum wage, only the third of the estimated living wage. Judy Gearhart, the executive director of the International Labour Rights Forum has since added "Managers hit workers with sticks to force them into the factory that day."[18]

In the years following there has been hard campaigning to improve working conditions, health & safety requirements, and the minimum wage. Progress has unquestionably been made, but there is now another potential controversy threatening fashion retail brands: Uighur forced labour.

There is growing global condemnation of the human rights abuses taking place in Western China, where it is thought that more than a million people from Chinese minority groups (most notably, Uighur Muslims) are detained for "re-education". There have been numerous alleged abuses and most recently, there has been new evidence that more than half a million of these detainees are being forced to work in seasonal cotton picking[19]. 20% of the world's cotton is sourced from Xinjiang.

As such, it is plausible that many mainstream brands will have used cotton in their products harvested from forced labour. The complexity of supply chains means that it is unlikely that many fashion retail companies would know that they are complicit in the practice. This brings serious reputational and litigation risks.

It should be said, neither the price or 'quality' of a brand, nor the quantity of items manufactured and sold is able to indicate if the materials were sourced responsibly or if the factory workers have been well treated and properly paid. Fast fashion and luxury retailers alike have been found wanting.

Investment

From an investment point of view, this makes retail a tricky sector. Long-term structural changes are underway and the ways we buy clothes are beginning to change. While there are structural tailwinds for online retailers, these same companies are facing enormous sustainability headwinds. Apparel remains one of the most carbon intensive industries in the world and has a poor reputation when it comes to the treatment of their workforce through the entire supply-chain.

Companies need to be on the right side of the move to ecommerce and to be running their businesses sustainably. There will be winners, but in the meantime, it is a sector that needs to be approached with caution.

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[17] https://cleanclothes.org/campaigns/past/rana-plaza

[18] https://www.opensocietyfoundations.org/voices/what-s-changed-and-what-hasn-t-rana-plaza-nightmare

[19] https://www.bbc.co.uk/news/extra/nz0g306v8c/china-tainted-cotton

The UN Sustainable Development Goals

(Originally published November 2020)

What are the UN SDGs?

The UN Sustainable Development Goals ('SDGs') were developed as an ambitious blueprint for achieving peace and prosperity for all nations while also protecting the planet. At the heart of the framework is addressing global environmental and social challenges to achieve a more sustainable future for everyone.

How did they come about?

The SDGs are the key focus of the UN's 2030 Agenda for Sustainable Development, which was adopted by members in 2015. The SDGs are deliberately interconnected – ending poverty, protecting the environment, and spurring economic growth must go hand-in-hand to future proof the Earth. Each goal has a number of sub-targets that need to be achieved by 2030. There is a total of 174 targets.

The United Nations Development Programme ('UNDP'), an agency of the UN, works in 170 countries focusing on the complex systems and root causes of issues to build high-level solutions on a national and international level. The SDGs, however, were designed to be used by anyone - companies and investors alike - as guidance for a more sustainable future. Businesses can align themselves by identifying those goals most relevant to their operations, as well as improving their reporting and monitoring of their contribution. Investors can use them as guides to identify and evaluate companies that are future-proofing and contributing meaningfully to that future, thus putting them in a position of competitive strength. Finally, policymakers can use them as an overarching goal when drafting and implementing policies and regulation.

What are the SDGs?

The SDGs are a mix of environmental, social and governance goals. They are:

Investor Landscape

ESG (Environmental, Social & Governance) is a familiar acronym to those working in finance and investment. Since 2006, the growth of assets managed by PRI signatories (Those agreeing to invest under the UN's Principles for Responsible Investment) has gone from $6.5trn to $103.4trn in 2020. What was once a niche investment style is now widespread practice, sparking many new ESG-focused funds coming to market. Existing funds now commonly integrate ESG scoring and monitoring into their investment process, regardless of their mandate.

Part of this incredible growth is due to a shift in responsibility. What was once perceived as exclusively a governmental or supranational duty now has a large and varied base of stakeholders. The SDG framework includes asset owners, businesses and all kinds of investors as part of those stakeholders who now have an increased role in advancing sustainable economic development.

Below are some of the ways that investors can use the SDGs as a tool when evaluating funds, companies, and portfolios.

Company Analysis

It's unlikely a company can tackle all 17 SDGs as part of its business model. However, there are almost certainly multiple goals that a company can address either by:

a) actively contributing to a goal as part of its operations – for example, an electricity utility company can make shifting entirely to renewable energy sources part of its long term strategy (SDG 7), or a drinks manufacturer can commit to using recycled plastic (SDG 12).

b) shifting its business away from detrimental activities. Equally important to the above is businesses and economies becoming less reliant on socially harmful or environmentally damaging practices. An example is oil and gas companies reducing their reliance on fossil fuels by investing more in their renewable energy portfolios.

Some companies, such as French food manufacturer

Danone, already have active and engaged policies and reporting in place to monitor their SDG contributions and impact. This includes monitoring environmental and social performance alongside financial performance in annual reports, using measurable targets that allow investors to observe progress.

Not all companies currently provide such information, but the Taskforce for Climate-related Financial Disclosures (TCFDs) are being adopted as an international disclosure framework by many governments and it is still useful for an investor to evaluate companies within the context of the SDGs even where information is lacking. The SDGs are not just a nice thing to have for corporate responsibility, but also a template of what 150+ nations are intending the future to look like – a trend that is likely to be accelerated by the COVID-19 pandemic. Are a Company's operations resilient within the SDG framework? Can this company continue or improve its growth projections in a sustainable way? Will this company still have, gain, or lose a competitive edge versus its peers?

As 2030 grows closer, policymakers will accelerate the implementation of regulation and policies that support the UN SDGs, so it's important for companies to at least address futureproofing, if not actively contribute to the UN SDGs.

Engagement

As stakeholders, investors can use the SDGs as a basis for engagement with companies. Where investors are trying to engage on a specific issue, the 17 SDGs can provide:

a) an easily communicated overarching goal e.g. how a company's internal policies incorporate SDG 5, Gender Equality, and SDG 10, Reduced Inequalities

b) specifically tailored and targeted suggestions and goals for a company to address. An example could be asking how food producers that rely on beef and cattle rearing address target SDG 15.2, under 'Life on Land', in promoting the sustainable management of all types of forests, and halt deforestation. Do they engage with suppliers that use deforested land for cattle rearing? Do they only do business with suppliers who have sustainable cattle practices? Do they have supply chain auditors in place to regularly monitor suppliers?

The ambition of the SDGs and their sub-targets can be overwhelming to both companies and investors, especially with increasing amounts of data being both made available and demanded. However, they can be useful in identifying a particular cause of concern or weakness in a company's operations and positively engaging with the company over it. There are also a number of investor initiatives that allow investors to collaborate with each other, raise awareness or learn about potential issues that merit engagement – e.g. Climate Action 100+.

A company's response to this kind of engagement is significant in itself. Some may have very good reasons why they have been unable to measure a particular impact, or implement a particular strategy. This may be indicative of problems that need attention from policymakers or governments. However, some companies may resist engagement and change without sufficient reason, or any reason at all. Investors in these cases must monitor the situation carefully and evaluate their investment case in a scenario where engagement has no impact.

How effective are the SDGs?

Measuring the global impact the SDGs have had since their adoption in 2015 is difficult. It has to be based on more than just a company's own disclosure to be robust. However, in the five years they have existed they have provided a common language for businesses, investors and policymakers, as well as unifying goals to achieve. They stress the importance of all stakeholders working together to a 2030 sustainable future. They highlight the significance of the challenges that need to be actively addressed. Most importantly, they provide clear guidance on where we need to go from here and thus where to look for new investment opportunities.

For investors, evaluating companies within an SDG framework helps affirm whether a company is operationally and financially aligned to specific SDG targets and achieving a positive impact. It is also useful to use the SDGs alongside scientifically based and measurable goals to ensure progress is actually made (x% reduction in water usage in an audited annual report is more material progress than 'we plan to consume less water in the future' in a press statement). Policymakers will continue to implement rules and regulation around a sustainable future, so the SDGs provide metrics by which investors can evaluate whether companies can adapt and thrive, or get left behind.

Including impact investing within your charity investment strategy

(Originally published February 2020)

This is written for charities, but the principles can be applied to most client types.

For many investors impact investing is a logical extension to responsible and sustainable investment as they strive to have greater purpose in the way they invest. Rather than excluding certain investment areas or including more of favoured areas, impact investing provides capital to companies that directly match a charity's social or environmental goals. Of course, charities will need to be mindful of the statutory and case law guidance relating to their investment policy.

The chief difference between impact investing and a grant, donation or philanthropy is that impact investments are made with the intention of generating a financial return as well as positive, measurable social and environmental impact.

Current estimates from the Global Impact Investing Network (GIIN) put the size of the impact market at US$502bn* having grown by around 80% in the past four years. Impact investment provides capital to address some of the world's most pressing challenges in sectors ranging from renewable energy, conservation and microfinance to affordable basic services such as housing, healthcare and education.

However, in embracing impact investing, it is important that charities don't risk their reserves in a way that imperils their main activity – after all, charities are the original impact investors.

First steps

For charities contemplating incorporating impact investment, the first priority should be to define their values. This is key to finding those impact investments that chime with the goals of the charity, be that equality, health, nutrition or social justice. As we see it, there are five key questions trustees need to ask before they start:

- What will you invest?
- What problems will you address?
- What steps will you take?
- How will you measure success?
- How can you measure impact?

In our experience, the most common explanation for weakness in an impact programme is not being clear about what success means at the outset. Only when a charity is clear about the change it hopes to bring about can it plan effectively.

Definitions

Definition is perhaps the most complex aspect for all types of investing with purpose. A 'good' social impact will ultimately be determined by our individual values, culture and belief system.

The Investment Association uses the GIIN (Global Impact Investing Network) definition, which sees impact investments as having four key elements: intentionality, financial returns, investing through any asset class and impact measurement.

Intentionality

The intentionality requirement means that companies that just happen to have a business with good environmental or social impacts are likely to be excluded. This makes 'true' impact investment more difficult in public markets and is why most impact investment is in non-public enterprises and vehicles.

Measurement

Deciding how impact is going to be measured can often give greater clarity to a charity's values and beliefs. It will open up ideas about impact to scrutiny, often giving a better result in the longer term. Any measurement tool will need to reflect a charity's priorities, as well as answer the question of whether the impact programme is really making a difference.

More opportunities are likely to emerge as the sector matures. Public market investors can start to measure their exposure to sustainable impact solutions and they can measure their portfolio exposures against the UN's Sustainable Development Goals. This establishes a baseline, so impact improvement can be measured over time. This is not 'true' impact investing perhaps, but a step in the right direction.

It is worth charities considering how they can incorporate impact investing into their investment strategy.

Environmental, social and governance (ESG) considerations

(Originally published January 2020)

ESG considerations are changing the investment landscape. Institutions are consequently under increasing pressure from stakeholders to draw these considerations into their investment process, a big step up from previous 'best practice' of merely adhering to various ethical exclusions. It is vitally important for investors to get this right, or they risk impacting their long term goals. However, we would argue that incorporating this into an investment process is more nuanced than many believe.

There have been significant and increasing flows into ESG mandates in recent years and this area is becoming a greater priority for institutional and other investors. Companies with ESG solutions are trading at a premium and in the past five years the MSCI World ESG Index has outperformed the MSCI World index by over 10% on a cumulative basis*.

It is also possible to see the phenomenon at work in individual sectors. For example, following the attacks on Saudi oil production, the oil price spiked higher on anticipation of supply shortages. The oil majors such as BP and Shell would normally follow suit, but the share prices remained stubbornly low. There seem to be fewer buyers for this type of company today.

Regulation has played an important role. From the Shareholder Rights Directive (SRD) II and Institutions for Occupational Retirement Provision (IORP) II introduced in 2019 to the new UK 2020 Stewardship Code, we have seen ESG regulation expand considerably - with more to come. The Paris Climate Accord targets on carbon emissions can only be achieved with what has been coined as 'the inevitable policy response'. Responsible investing has established itself as a mega-trend and will become a bigger part of all our lives. It will affect all the companies in which we invest and their customers. Changes to MIFID II will mean that investment managers need to ask each client for their specific ESG preferences and consider them alongside the traditional considerations which make up the suitability assessment.

Many firms are already signatories to the UN supported Principles for Responsible Investment (PRI) and the UK Stewardship Code which has just been revised. Signatories are required to do things like take account of ESG factors when investing, actively engage with companies and publicly disclose voting and engagement. This requires significant commitment of time and resource – for example we have voted** on over 10,000 resolutions at AGMs in the past year.

We believe experience matters in this part of the market because incorporating ESG considerations into a portfolio isn't straightforward and can have unintended consequences. Investors need to be really clear about the impact of their investment choices and restrictions through the market cycle. This is an immature sector, overloaded with jargon and few widely agreed definitions. For example, one 2017 study (GPIF) of Japanese equities found the correlation in the ESG scores between the different screening services to be only 0.3. Interested parties, such as the European Commission, are working on a taxonomy of environmental factors, but it will take time before there is agreement across all regions and sectors. The ESG scores generated by the screening companies are a starting point for further fundamental analysis, not an end in themselves.

Most investors are part way along a journey that moves from a standard investment process, focused solely on maximising returns, through to a responsible and sustainable investment approach (which includes portfolio screening and ESG criteria), to – ultimately - impact investment. Impact investment is still difficult, not least because of limitations over measurement. Mapping outcomes against the UN Sustainable Development Goals is gaining traction for listed equity funds. Imagine trying to measure different interpretations of impact across hundreds of companies and sectors in every region of the world.

There are choices to be made at each stage of this journey. If fossil fuel companies are excluded entirely, should you also exclude the main users of fossil fuels such as power companies? The transition to net zero carbon emission requires as a first step a switch from thermal coal to natural gas, because other technologies simply don't exist at this stage. Also coal/gas burning utility companies are often the biggest investors in wind and solar energy. Equally, ESG criteria can see a lot of larger companies with high dividends excluded: they tend to have diverse revenue streams and it can be more difficult to be entirely 'green'. This bias can be managed, but investors need to be aware that incorporating ESG criteria can skew their investment portfolios.

Equally, investors will need to choose between different 'shades' of green. This is considerably more nuanced than many believe. For example, companies that score highly on ESG criteria have often already seen a wall of money moving towards them, leaving their share prices high. Investors may have greater impact directing capital to and engaging with businesses in the process of improvement.

A good engagement programme can help push companies forward. Today, BP is the largest provider of electric car points, Scottish and Southern creates wind power, while RWE in Germany has a huge alternative energy business. Divestment often feels like the easiest option, but it is important to look at where management teams are heading and try to support their journey. To our mind, stewardship is key – without it, responsible investing is hollow.

This article was originally published in STEP Journal - 'Shades of Green', (Vol28 Iss1), p, 59

Sources:

**MSCI/Smith & Williamson (5 Aug 2019)*
***Smith & Williamson Q3 voting report (30 Sept 2019)*

Human capital is indeed capital

(Originally published December 2020)

One of the side effects of the Covid-19 crisis has been to bring human capital into the spotlight as one of the few variables capable of playing a key role, first in protecting the economy and society and second, in maximising the chances of a rapid output recovery when the pandemic ends. But, before briefly discussing recent events, it may be appropriate to look at the concept of human capital in some detail.

What is human capital?

There is no rigorous definition of human capital. It is a loose term that is generally considered to be the sum of several factors, notably the knowledge, skills, and abilities of employees.[1] Human capital is thus to be regarded as one of the essential assets a business needs to produce the goods and services it sells. Unlike most other assets which are physical in nature (such as land, plant and equipment) human capital is intangible, and hence particularly difficult to value. Nonetheless, it often represents a large share of the overall value of a company and can play a significant role in the determination of its long-term success or failure. Patents, copyrights, intellectual property, goodwill, brands, trademarks and research & development are other examples of intangible assets, but they all rely on human capital in one way or another. In short, human capital is indeed a form of capital, both for companies and for the economy as a whole: with physical capital, technology and institutions[2], human capital is one of the basic forces driving the economy and providing better standards of living.[3]

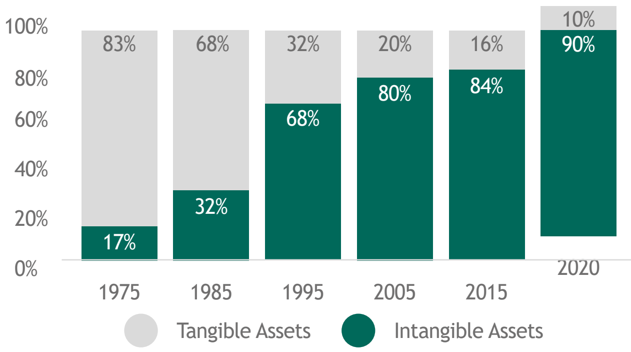
Why human capital matters for investors?

Since the late twentieth century, there has been a transition from an industrial economy to a knowledge economy – a transition largely fuelled by rapid technological progress. The knowledge economy has been defined as «a system of consumption and production that is based on technology and the knowledge acquired by the workers»[4]. It relies increasingly on human capital and other intangible assets, rather than on physical capital and natural resources as in the industrial economy. While precise figures are still not available, for developed countries the knowledge economy is generally believed to generate a large, if not the largest, share of gross domestic product (GDP). The long-term growth of intangible assets relative to tangible assets in the US economy is clearly shown in the chart. Over the last 45 years, the percentage of the market value of the S&P 500 firms represented by intangible assets has surged by more than fivefold, from around 17% in 1975 to around 90% in 2020, according to estimates of the investment advisory firm Ocean Tomo[5].

Equivalent data for European markets cover a much shorter period. The proportion of intangible assets in the market capitalisation of the S&P Europe 350 companies has also increased, although at a slower pace, from 71% in 2005 to 74% in 2020, according again to Ocean Tomo[6]. These figures largely reflect the importance of big tech firms "FAAMGs"[7] in the US economy relative to Europe.

The bottom line is that investors assessing the value of firms must pay close attention to the human capital of these firms, which is likely to be an important determinant of the value of their intangible assets and hence of their overall value.

Components of S&P 500 market value



Source: Ocean Tomo, LLC intangible asset market value study, 2020

How can the value of human capital be increased?

Given the rapid pace of technological progress mentioned above, to preserve and improve their human capital it is essential that companies provide more and better training and retraining to their employees. This is likely to set off a positive chain reaction boosting employees' commitment and productivity, product and service quality, customer satisfaction, sales volume, profitability, and ultimately stock market valuation. While empirical evidence has confirmed such a correlation, more research is needed to establish the direction of causality.[8] This may be a classic chicken and egg dilemma: did superior financial performance arise because of better trained employees, or did the company have more funds to invest in training because of a good financial performance due to other factors?

How can valuable employees be prevented from leaving?

The skills that make up human capital belong to the individual employees, not to the company. When employees leave the company, they take their knowledge, skills, and abilities - clearly a damaging outcome for the company. To prevent it, companies have to adopt a holistic approach that covers all aspects of the work environment and that will enable them to retain their employees. This includes a long list of measures, such as competitive remuneration packages and attractive career opportunities, applying best practices in health and safety, and having strong equal opportunity and workplace diversity programmes, as well as provisions for health and wellbeing, and flexible working hours. Companies that use employee engagement surveys (especially where there is a large workforce) are better able to identify and react to areas of concern among workers, while also giving employees a sense that management is committed to their welfare. A wider use of such policies would be beneficial to most companies.

How is human capital treated in the investment process at Smith & Williamson?

Human capital comprises an integral part of the investment process. For many sectors, including technology, healthcare, financial services and media, human capital is one of the most important ESG factors. It is likely to play a major role in the assessment of the value and prospect of companies in these areas since these companies tend to require a large workforce of highly skilled individuals. But human capital is systematically monitored for all companies and is focused on how companies attract, develop, and retain employees while providing working conditions favouring greater employee engagement. For that, Smith & Williamson notably looks at staff share programmes and remuneration, equal opportunity and workplace diversity programmes, training programmes, knowledge-sharing processes, employee satisfaction on Glassdoor (a website where current and former employees anonymously review companies), overall employee turnover, as well as health and safety policies and performance. Also considered is whether companies are performing employee engagement surveys or similar processes. As already noted, companies that perform well in this respect are likely to be more resilient and able to attract talented employees, and hence to remain competitive and thrive. On the other hand, poor human capital management is likely to lead to higher employee turnover, lower employee productivity, higher costs and a loss of competitiveness which may threaten the very existence of the company.

The Covid-19 crisis and human capital

As noted in the introduction, the Covid-19 pandemic has greatly increased the interest in human capital. A vivid example of this was the initiative in March 2020 of a group of more than 280 large investors with $8.2 tn assets under management (AUM) to call on companies to protect their workforce and their communities, as countries all over the world were imposing the first lockdowns[9]. At first sight, this call may appear contrary to normal practice, as the majority of investors are said to focus on short-term results and expect shareholder primacy – a principle divesting corporate directors of any responsibility other than to maximise profits for their shareholders. In fact, the investors behind the call, while recognising the considerable challenges posed by Covid-19, urged companies to do their best to prioritise safety, the use of paid leave and the maintenance of employment relationships. These measures were aimed at protecting society at large and the companies in which the investors have invested from potentially very harmful outcomes. These investors acknowledged the importance of human capital as an asset, and that by protecting it companies stood to be well rewarded when the economy recovered, as they would be able to increase output swiftly and smoothly. Companies that noticeably failed to protect their workforces were quickly identified in the media. Hence, Covid-19 may have played the role of a catalyst and accelerated the pre-crisis trend of investors taking human capital management increasingly into account when assessing the value of a company.

[1] Chartered Institute of Personnel and Development (CIPD), "Human capital theory, assessing the evidence for the value and importance of people to organisational success", 2017. https://www.cipd.co.uk/Images/human-capital-theory-assessing-the-evidence_tcm18-22292.pdf

[2] Institutions have been defined as: "rules, regulations, laws and policies that affect economic incentives and thus the incentives to invest in technology, physical capital and human capital." Daron Acemoglu, "Introduction to Modern Economic Growth", Department of Economics, Massachusetts Institute of Technology, 2007. https://www.theigc.org/wp-content/uploads/2016/06/acemoglu-2007.pdf

[3] Ibid.

[4] Patrick Ngulube, "Handbook of Research on Theoretical Perspectives on Indigenous Knowledge Systems in Developing Countries", University of South Africa, 2016. https://www.igi-global.com/dictionary/indigenous-knowledges-and-knowledge-codification-in-the-knowledge-economy/16327

[5] Ocean Tomo, "LLC intangible asset market value study", 2020.

[6] Ibid.

[7] Facebook, Apple, Amazon, Microsoft, and Google.

[8] Investor Responsibility Research Centre Institute (IRRCi), "The Materiality of Human Capital to Corporate Financial Performance", 2015. https://lwp.law.harvard.edu/files/lwp/files/final_human_capital_materiality_april_23_2015.pdf

[9] Interfaith Centre for Corporate Responsibility (ICCR), "Investor statement on coronavirus response", 2020. https://www.iccr.org/sites/default/files/page_attachments/investor_statement_on_coronavirus_response_04.02.2020.pdf

Our providers & memberships

Providers

MSCI | MSCI ESG RESEARCH INC.

MSCI ESG Manager is an online ESG research and analytics platform designed to provide asset managers and owners with an integrated suite of tools to efficiently manage research, analysis and compliance tasks across the spectrum of environmental, social and governance (ESG) factors.

GLASS LEWIS

As the leading independent provider of global governance services, Glass Lewis helps institutional investors understand and connect with the companies in which they invest.

Broadridge

Broadridge provides advanced technology and operations, communications, data and analytics solutions for the financial services industry and businesses.

SUSTAINALYTICS

A leading independent global provider of ESG and corporate governance research and ratings to investors.

Memberships

These logos are property of the relevant company

THE UK STEWARDSHIP CODE 2020

PRI Principles for Responsible Investment

THE INVESTOR FORUM

Climate Action 100+

Trade associations

THE INVESTMENT ASSOCIATION

TISA

PIMFA

Corporate Social Responsibility Data

Skills & Training

Looking at Tilney & Smith & Williamson combined, within financial practitioners we have 225 practitioners (i.e. those authorised to give financial advice) all of whom hold a level 4 qualification as a minimum, predominantly with the Chartered Insurance Institute (CII).

Within Investment Management we have 289 practitioners of which 124 are qualified to a minimum of level 4 and 165 to a minimum of level 6, predominantly with the Chartered Institute for Securities and Investment (CISI). In addition, 259 of the investment management practitioners hold Chartered status with the CISI. All graduate trainees within Investment Management are required to pass the Chartered Wealth Manager qualification, which is level 7, before they are able to progress to the Practitioner role.

Within Professional Services we have approximately 218 chartered accountants, predominantly with the Institute of Chartered Accountants in England and Wales (ICAEW).

Client engagement skills have been a particular area of focus in 2020 with us developing new programmes to enhance our practitioners and advisors networking, relationship building and influence skills, underpinned by the principles of behavioural science.

We set clear expectations through our performance management, with objective setting, coaching, and formal and informal feedback central to our approach.

We have leadership programmes for developing new leaders as well as more sophisticated programmes for more experienced leaders. Given the business growth and change agenda, we have particularly focused on strengthening leader's change management, adaptability and resilience skills.

Diversity and Inclusion

We are committed to having a diverse and inclusive organisation. We wish to ensure that individuals of all backgrounds, life experiences, preferences and beliefs are recognised and respected as individuals and valued for the different perspectives they bring and that all people are given equal opportunity to contribute to business success and be their true selves, regardless of background.

We have established a Group Diversity and Inclusion Committee, which has responsibility for ensuring the development and delivery of the Group's Diversity and Inclusion agenda. Our diversity and inclusion strategy focuses on ensuring that our recruitment, development and promotion processes fully support our diversity aims, removing sub-conscious bias, while continuing to ensure we select the best individual for the role. We promote a culture where all colleagues feel valued and able to contribute, through activities like diversity network support groups and celebrating diversity.

The Group will sign up to the Women in Finance Charter pledge for gender balance in financial services. The board will review Smith & Williamson's previous targets and re-commit to future targets for the Group in 2021.

In the formation of the board and the Executive Committee we have sought to improve gender diversity and are committed to doing this within all levels of the organisation. The following table shows the gender mix with the Group as at 31 December 2020.

	Female		Male		Total
Organisational level	Number	Percentage	Number	Percentage	Number
Board of Directors	2	18%	9	82%	11
Group Executive Committee	4	31%	9	69%	13
Senior Management	31	24%	100	76%	131
All colleagues (including Group Executive Committee and Senior Management)	1,474	47%	1,658	53%	3,132

The 2019 Gender Pay Gap Report for Tilney and Smith & Williamson is available on our websites. The first Gender Pay Gap Report for the combined group will be for 2021. For 2020 we will continue to report as separate legal entities. As an employer, we are committed to reducing our gender pay gap and we continue to focus on ways to encourage and support the progression of women into senior roles through recruitment, promotions and mentoring.

Remuneration

Our remuneration strategy aims to deliver outstanding client outcomes and experiences, aid high performing colleague attraction and retention, and support profitable business growth. The principles underpinning our remuneration strategy are to:

- ensure that colleagues are all able to benefit from a competitive base salary, bonus, pensions and benefits, while protecting colleagues' historical terms;
- consider total compensation against competitor and market benchmarks;
- ensure that we can recruit and retain key talent; and
- take care that our approach is compliant with regulations and aligned with sound risk management
- allocate equity to key senior staff.
- We will continue to monitor and evolve our remuneration strategy to ensure it delivers against our remuneration principles and business objectives.

Anti-bribery policy

Tilney Smith & Williamson values its reputation and is committed to maintaining the highest level of ethical standards in the conduct of its business affairs. The actions and conduct of the firm's staff as well as others acting on the firm's behalf are key to maintaining these standards. The Group does not tolerate bribery or corruption in any form.

The firm prohibits the offering, giving, solicitation or the acceptance of any bribe or corrupt inducement, whether in cash or in any other form:

- to or from any person or company wherever located, whether a public official or public body, or a private person or company;
- by any individual employee, director, agent, consultant, contractor or other person or body acting on the firm's behalf;
- in order to gain any commercial, contractual or regulatory advantage for the firm in any way which is unethical or to gain any personal advantage, pecuniary or otherwise, for the individual or anyone connected to the individual.

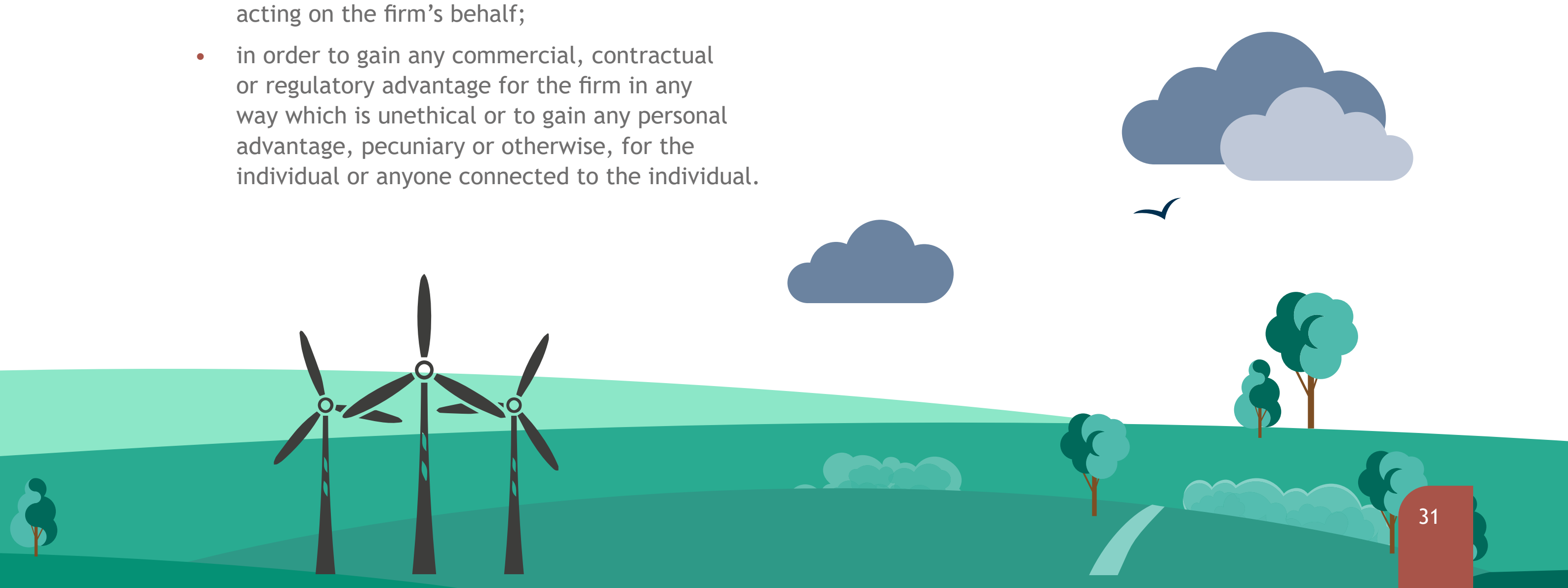
Our policies cover reporting requirements, restrictions on gifts and hospitality and facilitation payments, our approach to politically exposed persons, information security, our procurement approach and charitable gifts/donations.

The firm will investigate thoroughly any actual or suspected breach of our anti-bribery policies.

Modern slavery

We are committed to ensuring our business and supply chain are free from any slavery or human trafficking. As we operate in the financial services sector, many of the service providers we encounter are UK-based entities and they are often regulated by governing bodies. Our material supplier contracts (such as IT providers, audit services and property services) have been reviewed to assess whether the terms in the agreements are satisfactory to provide us with confidence that our suppliers have sufficient procedures in place to protect against slavery or human trafficking occurring within their business and supply chain.

The other main types of service provider relate to essential office services, such as security, catering and cleaning. Our office services are outsourced to organisations with their own due diligence procedures for employees and contractors. Our tender process for these contracts includes confirmation of the steps the potential suppliers take to ensure their businesses are free from modern slavery and human trafficking. The due diligence process includes verifying that they have sufficient policies and procedures in place to ensure fair treatment and pay of workers, adequate whistleblowing procedures and confirming that all those employed in the provision of services have the necessary documentation to work legally in the UK.



Communities

As a Group we enable our clients to invest responsibly and we take the same approach by investing in our local communities as a good corporate citizen. We have a wealth of talent and experience within our business and we are keen to share this with the community and enable our employees to gain further personal and professional development by getting involved in community projects and activities.

Our community investment programme is delivered through our Giving Back programme and funded by the Tilney Charitable Trust ('TCT'). The TCT was established in 1979 and since then has donated over £3 million to local and national charities. The Trust has a strong heritage in providing funding to the charitable causes which our employees support.

Our Giving Back programme is in place to:

- encourage and support volunteering participation from our employees, to contribute to employees' personal and professional development and enhance employee engagement;
- enhance our reputation as a responsible company with employees and external stakeholders at local, regional and national levels;
- encourage charitable giving and fundraising efforts for the benefit of our local communities; and
- embed good citizenship into all areas of the business.
- Giving back at Tilney Smith & Williamson focuses on supporting:
- Employee volunteering and personal development – We encourage and support our people to get involved in their local communities and at the same time develop their skills. We give all our employees paid time off to volunteer; and
- Giving to charity – We encourage our employees to give regularly to charity through our Payroll Giving scheme and match employee donations up to £20 per employee, per month. We also match our employees' fundraising efforts with donations of up to £250 for individuals and £1,000 for teams with additional matching available for national Tilney Smith & Williamson events through a donation from the Tilney Charitable Trust.

Since initiating our payroll giving scheme we have achieved both Gold and Platinum Payroll Giving Quality Mark Awards for our commitment to Payroll Giving.

We operate under an effective governance structure to protect our reputation, brand and our relationships with regulators and legislators, as well as our Partners. Our Giving Back Committee leads and governs our approach to volunteering and charitable giving, agreeing the focus and policy for the Giving Back Programme and ensuring the programme contributes to the overall business strategy.

The Committee comprises functional and regional employee representatives headed up by the Chair. The Committee is also supported by dedicated 'Giving Back Coordinators' in local offices. The Committee is responsible to the Tilney Charitable Trust Trustees.

In response to the COVID-19 pandemic, The Tilney Charitable Trust donated £10,000 to the Critical NHS which enabled the coordination and delivery of over 98,000 meals to front line staff across 15 London Hospitals.

Colleagues stepped up their fundraising efforts and we continued matching colleague fundraising throughout the pandemic to a sum of approximately £54,000. Colleagues raised approximately £33,500 through their payroll giving donations with circa £11,000 matched through the Giving Back Programme.

Following the merger in September 2020 the charitable activities of Smith & Williamson were amalgamated. In the last four months of the financial year the Charities Committee supported one particular event, encouraging staff to undertake a 5km run, jog or walk and for each participant £20 was donated to two foodbank charities – Fareshare and Foodcloud. In addition, the Committee agreed to match staff donations to the same charities. Over 400 members of staff from across the offices took part and over £11,000 was raised. The Charities Committee also made donations of approximately £40,000 to 20 charities at Christmas and continued to support members of staff who undertake personal charitable fundraising activities, donating £6,700 to 14 charities over the period.

Clients

We take a proactive approach to listening to and understanding our clients' needs and ambitions, operating a comprehensive and unified Client Care programme across the Group, led by our Group Head of Client Services. This provides an independent and objective platform to capture insights that will enable us to deliver a consistently exceptional client experience. We believe that by listening to our clients' experiences on how we are performing, and by understanding what they want and expect from Tilney Smith & Williamson – now and in the future - we can improve many aspects of our service that will bring real and tangible benefits. This is a client-centric programme that runs holistically across the Group, unifying all business areas nationally. It helps us to grow and deepen relationships, as well as understand more about our clients' needs so that together we can develop growth strategies, ensuring ongoing satisfaction and enabling us to better serve their interests.

Environment

The Company manages the majority of environmental, social and governance topics, policies and procedures through the Group Executive Committee. Although the Group has a relatively low environmental impact, we seek to minimise this impact through ongoing improvements. Examples include large-scale recycling and initiatives to promote environmentally-friendly offices and travel practices, such as 'follow me' printing and 'cycle to work' schemes. We have recently introduced a "paperless initiative" across our national business. Using digital tools, we are focused on reducing our paper consumption materially, with an initial focus on "digital valuations" through our online portal My Tilney. This project is led by our staff and supported by the Group Executive Committee.

We are also implementing other solutions to digitise how we communicate and share data between our advisors and our clients; for example, secure messaging through our client portal, and online suitability reviews, both of which remove paper from our processes.

Environmental Statement

We understand our responsibilities to the environment and the wellbeing of both our staff and the communities in which we work. The operation of our offices and business travel are the primary sources of our emissions.

As part of our focus to control / reduce our energy consumption, our key initiatives include:

- improving the scope for recycling of typical office waste (paper, plastics bottles, cardboard etc.) while encouraging the reduction of plastic bottles/ single use plastics;
- encouraging staff to place all waste paper in the confidential waste bins, which is then shredded and recycled securely;
- constantly working to improve the utilisation of our office space and reduce running costs per employee;
- work towards minimising our travel and our clients' travel while undertaking our business activities by using environmentally efficient technologies, including investment in video conference facilities; and
- enabling and supporting more clients to adopt paperless reporting, plus enhancing the content available via My Tilney, our secure online client portal.

Greenhouse Gas (GHG) Emissions

As a UK incorporated, large organisation, Tilney Smith & Williamson is required to report its UK energy & greenhouse gas (GHG) emissions information in line with the requirements of the Companies Act (Directors' Report) and Limited Liability Partnerships (Energy and Carbon Report) Regulations 2018.

The merger between Tilney and Smith & Williamson was completed in September 2020. In order to continue to report our greenhouse gas emissions in a consistent and like for like manner, we engaged EcoAct, an Atos company, to calculate the group 2020 emissions and to re-baseline both organisations' 2019 emissions to the calendar year reporting period. The re-baseline included the alignment of reporting scope and categories, a review and update of calculation methodologies, and alignment with the Annual Report and Financial Statements format.

The table below summaries the energy consumption and global greenhouse gas (GHG) emissions for the Tilney Smith & Williamson Group for the period 1 January to 31 December 2020, measured in metric tonnes of carbon dioxide equivalent (tCO2e), along with the combined and re-baselined data for the previous year.

	Tonnes of CO2e Current reporting year 2020	Tonnes of CO2e Comparison year 2019
Energy consumption used to calculate emissions, kWh	9,194,866	11,115,058
Emissions from combustion of gas, tCO2e (Scope 1)	523.10	517.46
Emissions from combustion of fuel for transport purposes, tCO2e (Scope 1)	4.68	14.79
Emissions from business travel in rental cars or employee-owned vehicles where company is responsible for purchasing the fuel, tCO2e (Scope 3)	114.58	539.84
Emissions from purchased electricity, tCO2e (Scope 2, location-based)	1,279.68	1,528.89
Total gross tCO2e based on above	1,922.04	2,600.98
Intensity ratio: tCO2e / FTE	0.60	0.81

Scope 1 emissions are direct emissions from fuel used in company owned vehicles and from gas used for heating in our offices. Scope 2 emissions are emissions released into the atmosphere associated with our consumption of purchased electricity, heat, steam and cooling. Scope 3 emissions relate to the consumption of fuel used for company transport.

We have not reported here on other emissions associated with inputs to our company (such as emissions from our supply chain) or emissions linked with outputs from our company, generally considered as Scope 3 emissions.

We have used the main requirements of the Greenhouse Gas Protocol to calculate our emissions. We have reported on all of the emission sources required under the regulations. These sources fall within our consolidated financial statement, with an operational control approach being followed when defining our organisational boundary. We do not have responsibility for any emission sources that are not included in our consolidated statement. Where necessary due to the unavailability of meter readings, some energy consumption has been estimated using direct comparisons and pro-rata extrapolation. We have used the HM Government Environmental Reporting Guidelines (March 2019) and emission factors from the UK Government's GHG Conversion Factors for Company Reporting 2019 and 2020 in calculating our emissions.

Energy Efficiency

In addition to our partnership with EcoAct, we changed our Mechanical Electrical Plumbing (MEP) service partner in September 2020 which has added a layer of energy use monitoring and reporting providing;

- A year-by-year comparison of our monthly energy consumption and cost against published benchmarks.
- Report on any significant variance from the commissioned performance of equipment or systems.
- Proposals for limiting energy loss and/or gain from the building fabric, pipes and ducts.
- Proposals for improving the efficiency of equipment and lamps
- Improvements to timing and temperature controls.
- Improvements to metering and switching strategies

Our electricity energy supplier, where we are responsible for the purchase of electricity, remains Green Network Energy. The energy we purchase is 100% from renewable sources backed by Renewable Energy Guarantees of Origin REGO certification via Ofgem.

Tax Strategy

The group's tax strategy has been made publicly available on our website www.tilney.co.uk, in accordance with the Finance Act 2016. Both the Risk and Audit Committee and the Board have reviewed and approved the Group's tax strategy. The strategy sets out the Group's governance in relation to tax compliance, risk management, attitude to arranging our tax affairs, and our relationship with the tax authorities. The Group's tax risk appetite is considered to be low.

Cautionary Statement

Where this document contains forward-looking statements, these are made by the Directors in good faith based on the information available to them at the time of their approval of this report. These statements should be treated with caution due to the inherent risks and uncertainties underlying any such forward-looking information. A number of factors, including those in this document, could cause actual results to differ materially from those contained in any forward-looking statement.

Looking forward

The pace of regulatory change has accelerated in 2020.

The TCFD (Taskforce for Climate-related Financial Disclosure) was set up in 2017 to 'encourage companies to provide high quality disclosure about how organisations and investments will be impacted by and impact the environment'. The idea has been that better transparency would allow better-informed pricing and capital allocation. In November the FCA announced that all Premium Listed companies would need to adopt the TCFDs by 1 Jan 2021 and that other institutions including asset managers would need to adopt by 2022. Rishi Sunak announced in December that TCFD disclosures would be mandatory across the whole UK economy by 2025.

The European Union Sustainable Finance Disclosure Regulations (SFDR) start to come into force from March 2021 in Europe, and will be adopted by the UK in 2022. The first part of this is making sure investment company services and products properly disclose the environmental risks of portfolios and any environmental damage done by the companies in which we invest.

To follow shortly is the requirement to ask and integrate clients' sustainability preferences into their portfolios. The European Union Environmental Taxonomy consultation at the end of 2020 resulted in an amazing 46,000 responses, but the timetable for implementation starts in 2022 and is likely to have a big impact on companies too.

The new US President, Joe Biden, has started the process for the USA to rejoin the Paris Agreement and has ambitious climate change investment plans. Many of his senior leadership picks have strong environmental and social credentials.

Significant progress is being made globally on moving to new sustainability reporting standards – in particular the IFRS consultation and setting up the new Sustainability Standards Board to operate alongside the International Financial Reporting Standards. The EU have published the Corporate Sustainability Reporting Directive to align EU reporting requirements to those of the SFDR. Linking these all together will take time but represents solid progress in the right direction.

In terms of our integration with the Tilney Group, considerable progress has been made integrating our investment processes, which of course includes the area of stewardship and responsible investing.

I hope this report provides a helpful snap shot of the many areas of significant progress. There is a huge amount still to do if we are to deal effectively with long term environmental threats, incorporate social considerations, build investment resilience and protect wealth now and for future generations. That said, after a uniquely challenging year, we still have much that we can be proud of and I'd like to stress that we see so much to be positive about in the years ahead.

Nick Murphy
Chair of the Stewardship and Responsible Investment Group (SRIG)

Contact

If you would like to find out more about our Stewardship and Responsible Investment activities please look at our website **https://smithandwilliamson.com/en/stewardship-responsible-investment/** or contact our Stewardship & Responsible Investment team

Stewardship and Responsible Investment
Smith & Williamson Investment management

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Please remember the value of investments and the income from them can fall as well as rise and investors may not receive back the original amount invested. Past performance is not a guide to future performance.

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