ENVIRONMENTAL, SOCIAL
AND GOVERNANCE
INDICATORS AND KEY ISSUES
REFERENCE DOCUMENT

Threadneedle Asset Management Ltd
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RATIONALE

1.1. BACKGROUND

Environmental, social and governance (ESG) research is a core part of the equities investment process and developing in scope for fixed income.

1.2. PURPOSE

The purpose of this document is to define the ESG key performance indicators (KPIs) which we consider particularly relevant.

1.3. OBJECTIVE

The objectives of the document is to set out both global and thematic views as well as individual company KPIs in the area of environmental, social and governance research.

1.4. SCOPE

The scope of this document is as a supporting document to the main Governance and Responsible Investment policy. Applicable to the Governance and Responsible Investment team.

1.5. KEY POINTS

The policy sets out details of the following sections

- Global ESG sectors and themes:
  - Global sector meetings and other internal inputs
  - External inputs
  - Global guidelines
  - Table of key themes

- Corporate ESG KPIs
  - Human rights
  - Environment
  - Labour relations
  - Governance
  - Innovation

1.6. INTERNATIONAL GUIDELINES

<table>
<thead>
<tr>
<th>Memberships and Governing Bodies</th>
<th>Comments and Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>UN backed Principles of Responsible Investment</td>
<td>Signatories and members to the principles</td>
</tr>
<tr>
<td>UN Global Compact</td>
<td>Guidelines for analysis</td>
</tr>
<tr>
<td>OECD Guide for multi-national Enterprises</td>
<td>Guidelines for analysis</td>
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POLICY STATEMENT

2.1. GENERAL

Environmental, social and governance research forms a core part of Columbia Threadneedle Investments’ stewardship approach. The analysis of ESG factors is incorporated into our investment process to identify material associated risks and opportunities. The Columbia Threadneedle Investments’ investment process follows a model of idea generation, research and debate towards implementation. ESG research plays a part at different points in this model but is a key element of research and debate. Specifically, the ESG research is a part of the stock review process and the macro and themes review process feeding into the investment themes meeting. Other key areas of input include company meetings; broker meetings; weekly and ad-hoc updates and daily morning meetings.

The ESG research and engagement adds value to the overall understanding of ESG related risks and opportunities for a company, sector or theme. The ESG view can influence the level of conviction in the investment idea but we do not have a non-investment policy for higher risk companies. Sustainability growth trends such as energy efficiency, access to food as well as safety and security have been important inputs to our discussions around global sector reviews and macro themes providing investment opportunities.

Given the nature of our ESG approach, third parties should not assume any assurance as to the ESG risks inherent in any investment made by Columbia Threadneedle Investments. Rather, the approach is a contributing factor to better informed investment decisions.

2.2. ROLES AND RESPONSIBILITIES

<table>
<thead>
<tr>
<th>Role</th>
<th>Responsibility</th>
</tr>
</thead>
<tbody>
<tr>
<td>Chief Investment Officer</td>
<td>Mark Burgess</td>
</tr>
<tr>
<td>Head of Equities</td>
<td>Leigh Harrison</td>
</tr>
<tr>
<td>Head of Responsible Investment</td>
<td>Iain Richards</td>
</tr>
<tr>
<td>Sustainable and Responsible</td>
<td>Cathrine de Coninck-Lopez</td>
</tr>
<tr>
<td>Investment Officer</td>
<td></td>
</tr>
<tr>
<td>Responsible Investment Analyst</td>
<td>Michael Hamblett</td>
</tr>
<tr>
<td>Responsible Investment Analyst</td>
<td>Rose Beale</td>
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</table>
ESG VALUE PROPOSITION

The ESG research focuses on all three aspects of ESG and we believe a holistic understanding of these indicators provides a sound overview of management quality and can contribute to shareholder value. We reference in this respect an initiative lead by the UN Global Compact LEAD group and the PRI on “The ESG value proposition”. This neatly summarizes the link between growth, return on capital and risk management to ESG issues which impact business operations such as innovation, reputation, cost reduction and market power.

<table>
<thead>
<tr>
<th>Growth</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>New Markets &amp; Geographies</td>
<td>Gain access to new markets and geographies through exposure from ESG programs</td>
</tr>
<tr>
<td>New Customers &amp; Market Share</td>
<td>Use ESG programs to engage customers and build knowledge of expectations and behaviour</td>
</tr>
<tr>
<td>Product &amp; Services Innovation</td>
<td>Develop cutting-edge technology and innovative products and services for unmet social or environmental needs</td>
</tr>
<tr>
<td>Long-term strategy</td>
<td>Develop long-term strategy encompassing all ESG issues and shape material ESG communication based on value driver framework</td>
</tr>
</tbody>
</table>

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<thead>
<tr>
<th>Return on Capital</th>
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</thead>
<tbody>
<tr>
<td>Operational Efficiency</td>
<td>Enable bottom line cost savings through environmental operations and practices (e.g. energy, water, waste efficiency, less raw materials used)</td>
</tr>
<tr>
<td>Human Capital Management</td>
<td>Attract &amp; retain better and highly motivated employees by positioning company and management as ESG leaders</td>
</tr>
<tr>
<td>Reputation Pricing Power</td>
<td>Develop brand loyalty and reputation through ESG efforts that garners customers’ willingness to pay price increase or premium</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Risk Management</th>
<th></th>
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</thead>
<tbody>
<tr>
<td>Operational &amp; Regulatory Risk</td>
<td>Mitigate risks by complying with regulatory requirements and industry standards and ensure uninterrupted operations by addressing ESG issues in policies, systems and standards and engaging with employees</td>
</tr>
<tr>
<td>Reputational Risk</td>
<td>Facilitate uninterrupted operations and entry in new markets using local ESG efforts and community dialogue to engage citizens and reduce local resistance; avoid negative media publicity and NGO boycotts by addressing ESG issues</td>
</tr>
<tr>
<td>Supply Chain Risk</td>
<td>Secure consistent and long-term access to high-quality raw materials and products by engaging in supply chain community welfare and development</td>
</tr>
<tr>
<td>Leadership &amp; Adaptability</td>
<td>Develop leadership skills and culture to adapt to fast changing political, social and environmental situations</td>
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</tbody>
</table>

Source: The ESG Value Proposition – PRI and UN Global Compact LEAD (Cary Krosinsky and David Lubin 2013)
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GLOBAL ESG SECTORS AND THEME

The environmental, social and governance themes and sector specific issues that we have identified as our focus is based on a process of three key inputs and consists of a comprehensive list of global ESG themes.

GLOBAL SECTOR MEETINGS AND OTHER INTERNAL INPUTS

The global sector meetings, stock reviews and other discussions, ensure that ESG themes are rooted in investment relevance to a particular sector. The initiation of thematic or sector research often comes from discussions in our global sector meetings which bring together a range of individuals from across the investment department with representatives from both equities, fixed income, commodities and GRI. These discussions also bring out new ideas for research.

EXTERNAL INPUTS

Sustainability related mega-trends have been highlighted by several external sources as bringing significant opportunity and risk for corporations and investors. Brokers from investment banks, government agencies, consultants and NGOs all have ideas for what the big thematic drivers will be for the future. Unsurprisingly, many of the conclusions relate to environmental, social and governance ideas.

The list of mega trends related to ESG is long but the main concepts include issues such as: Climate change and energy; Water availability and management; Food and nutrition; Population Growth and urbanisation; Ageing populations; Education; Healthcare; Safety, Security and verification; Internal audit and control.

GLOBAL POLICY DRIVERS

Global and local policy drivers have been very important in influencing themes such as climate change and energy regulation; shareholder rights; supply chain oversight; and data protection in recent years. Supranational goals set at the UN level, such as the Sustainable Development Goals, are also important references and drivers for our themes. Global objectives post 2015 include: Peace and security; environmental sustainability; inclusive economic and social development.

Identifying Global ESG themes

**Internal inputs**
- Global sector meetings
- Stock reviews
- Other Investment teams

**External inputs**
- Research providers
- Industry associations and initiatives

**Global and Local Policy Drivers**
- UN Sustainable Development Goals
- Climate change policy

**Outputs of the research**
- Draw out key ESG sector issues
- Identify potential stock ideas that are related to the theme
## Themes of interest

<table>
<thead>
<tr>
<th>ESG theme</th>
<th>Investment considerations</th>
</tr>
</thead>
</table>
| Climate change and energy        | - Energy efficiency enabling technological providers  
- Renewable Energy Sources  
- Energy transition technologies and sources - eg Gas products, storage technology, smart grid  
- Electric vehicles |
| Water availability and management| - Water management strategies  
- Pollution control technologies  
- Distribution and access |
| Food and nutrition               | - Food producers  
- Agricultural companies  
- Chemical and seed providers |
| Population Growth                | - Employee relations and people management strategies  
- Supply chain oversight  
- Community opposition  
- Infrastructure development |
| Ageing populations               | - Pension reform  
- Infrastructure needs  
- New solutions and marketing approaches |
| Education                        | - Access to education  
- New forms of teaching |
| Healthcare                       | - Access to healthcare  
- Innovation for new diseases  
- Obesity  
- Global pandemics |
| Safety, Security and verification| - Data protection and consumer protection  
- Inspection and certification providers  
- Safety technology and processes  
- Greater enforcement of regulation and fines  
- Innovative IT solutions and information management |
| Internal control and audit       | - Litigation and fines across sectors  
- Tax management  
- Alignment of incentives |
**05 CORPORATE ESG KPIS**

The global ESG trends and themes translate into areas of interest on a company specific level that can influence stock specific opportunities or risks.

We pay particular attention to disclosure and transparency of reporting as well as focus on materiality and discussion of the ESG value proposition when highlighting sustainability initiatives to investors. We recognise that there are geographic, size and other differences to the level of disclosure and we consider these when setting our initial expectations. We look for an improvement in the performance and disclosure of ESG KPIs over time.

We identify relevant key performance indicators (KPI) for which to analyse companies beginning with consulting sector research from our research providers and above thematic research and then considering the company specific situation (such as geographic exposure, complexity, history, news flow).

In addition, we take into account the UN Global compact principles and the OECD guidelines for multinational enterprises as appropriate. The UN Global Compact centre on human rights, labour relations, sound environmental management and anti-bribery and corruption. We reference these as companies often take the UN Global Compact as their basis, and we recognise that the principles have become a global standard in the corporate world with more than 8500 signatories in 135 countries.

The process for selecting ESG indicators

<table>
<thead>
<tr>
<th>Global Guidelines</th>
<th>UN Global Compact</th>
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<tbody>
<tr>
<td></td>
<td>OECD Guidelines for Multinational Enterprises</td>
</tr>
<tr>
<td>Sector Issues</td>
<td>Internally defined thematic sector key issues as per above</td>
</tr>
<tr>
<td></td>
<td>MSCI ESG research</td>
</tr>
<tr>
<td></td>
<td>GRI Broker Sector indicators</td>
</tr>
<tr>
<td>Company specific situation</td>
<td>Geographic scope</td>
</tr>
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<td></td>
<td>“Age” and Size</td>
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<tr>
<td></td>
<td>Ownership structure</td>
</tr>
<tr>
<td>ESG Indicators</td>
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**HUMAN RIGHTS INDICATORS**

Human rights are particularly relevant in companies with large supply chains using a lot of human capital such as retailers and consumer product producers as well as in companies with significant footprint on the local community such as extractive companies.

Child labour, a fair living wage and appropriate regard to the community in which companies operate have been shown to be core to the licence to operate and protecting reputational risk. Most of the incidents we have seen have had shorter term impacts on the share price rather than a main driver of performance. However, they are indications of potential longer term risks and management ability to navigate specific business environments. Indicators we typically look for include:

- Audit of supply chain – both internal and external
- Gender equality and diversity programmes
- The extent of community involvement in the context of the business environment

**LABOUR RELATIONS**

Labour relations are particularly relevant in extractive industries, companies with history of governmental influence such as telecommunications, and for companies that have a focus on innovation, R&D and need highly skilled labour.

Good health and safety practices and strong employee training programmes improves productivity and employee retention for example companies have shown growth in sales per employee workforce hour following targeted training programmes. Poor health and safety practices can result in fines, production disruption and relatively long slumps in the shareprice. Similarly industrial action in extractives can lead to prolonged disruption to operations. Indicators we look for include:

- Lost time injury rate and fatalities declining or flat if already at a low level
- Training hours per employee
- Relationship with unions
ENVIRONMENTAL MANAGEMENT INDICATORS

Environmental management is particularly relevant for industrials and companies that use a lot of natural resources as input to their processes such as capital goods and extractives. Climate change regulation covers most industries.

Sound environmental management such as managing water, waste and energy have been shown to improve costs and for companies to be able to maintain margins despite slumps in revenue. For example innovative lean production methods, have contributed to better than expected results and stable margins despite relatively flat topline growth.

The types of indicators we typically look for include:

- The existence of an environmental management programme
- Certification against standards such as ISO 14001
- Publishing environmental consumption figures and trends (e.g., green-house-gases, waste, energy and water)

GOOD GOVERNANCE, ANTI-BRIBERY AND CORRUPTION

Good governance is relevant across sectors and we highlight what we consider as good corporate governance in our Corporate governance and proxy voting principles. Anti-bribery and corruption is a related area specifically highlighted as part of the UN Global Compact. In addition, the OECD guidelines for multi-national enterprises emphasise marketing practices and protection of consumer interests, involvement in anti-competitive practices, and how the company is generally accountable to external stakeholders. Increasingly this also encompasses concerns on taxation. The key indicators we look for include:

- The existence of appropriate internal controls through an audit system, with board level oversight
- Level of board independence, quality, diversity
- Remuneration incentives and its implication for risk taking/appropriate inclusion of ESG elements
- Litigation actions against the company
- Taxation scandals
- Data and IT security and systems
- Accounting Quality

INNOVATION

Innovation in companies is a core area of focus as we consider the opportunities that companies can achieve under the sustainable growth trends highlighted in the thematic and sector issues. Development of new science and technologies to adapt to climate change, enable greater food production, new methods of transportation are all relevant in a world of resource scarcity and changing operating contexts. The indicators we typically look for include:

- Percentage of sales devoted to research and development
- Method by which ESG factors are included in capital allocation
- Where appropriate, revenue derived from “sustainability” products
06
RELATED DOCUMENTS/REFERENCES

GOVERNANCE AND RESPONSIBLE INVESTMENT POLICY
CORPORATE GOVERNANCE AND PROXY VOTING PRINCIPLES