

# OUR APPROACH TO ESG - GLOBAL EQUITY TEAM

August 2018

## Our Goal

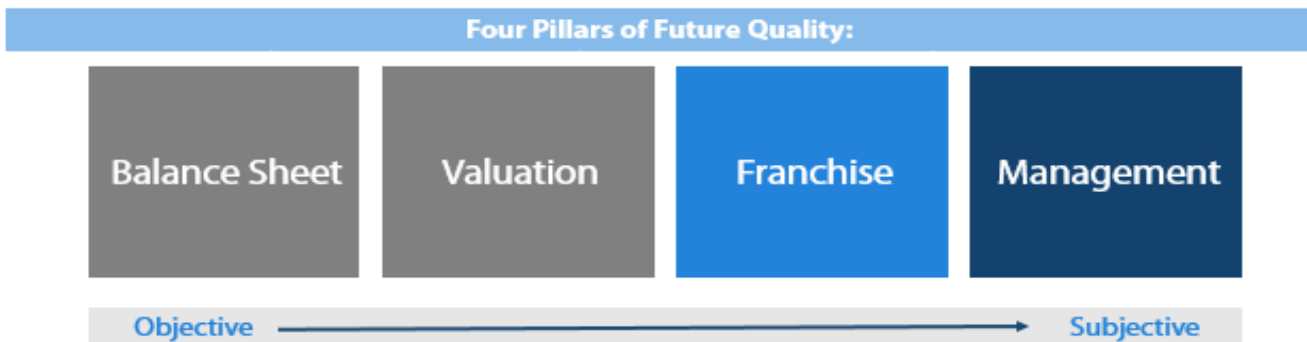
Our primary objective is to grow our clients' wealth by investing in global equities while being responsible stewards of their capital.

As institutional investors, we have a duty to act in the best long-term interests of our beneficiaries. In this fiduciary role and given the increasing trend towards a multi stakeholder society, we believe that environmental, social, and corporate governance (ESG) issues can influence client returns.

Our investment philosophy, Future Quality, describes the type of company we invest in. ESG can have a profound impact on corporate value and is therefore an integral part of our investment process. Engagement, in the form of investigative discussion with management through to voting, provides us with an opportunity to determine which ESG factors may impact value.

## Future Quality:

There are four pillars to Future Quality investing, each contributing to the investment case. Some, such as the strength of a company's balance sheet, provide a picture of the health of a company's finances at a set date. However the majority of a company's worth is defined by its future – hence why we call it Future Quality. Most of our time is spent researching the franchise and management quality of a company, as these pillars will dominate the likely future returns a company generates.



Like the balance sheet data, we believe ESG scores add value by providing a snap shot of a company's status. However, ESG factors are contingent liabilities and are often difficult to measure. If material, they will impact future returns and consequently corporate value and hence it is the context behind why ESG might influence future returns that makes integrating ESG an essential part of being a fundamental investor.

There is increasing evidence of a strong correlation between companies with high ESG scores & high financial performance. However, there are limitations to ESG data and the data doesn't explain why ESG matters. ESG factors influence value in many ways. The sustainability of a company's future returns can be influenced by **E**nvironmental & **S**ocial factors while **G**overnance acts as the mechanism for establishing how a management team is likely to allocate capital in the future.

We use company engagement and independent third party ESG specialists to help us understand the importance of ESG factors for each investment decision we make.

## Experience:

Experience through a variety of market cycles across global investment markets enables the team to ‘join the dots’ and find the best available investment opportunities. How we interpret the materiality of each ESG factor is down to the experience and skill of the team.



Academic Background

Experience as at August 2018. Not to scale

- **Long-term and fundamentally driven:**  
We only invest in companies that the team has thoroughly researched and debated
- **Debate and Insight:**  
We believe diverse experience leads to better investment decisions and outcomes for our clients
- **Future quality:**  
We believe that sustainable and superior returns on capital over the long run will deliver better compounded returns

Each member of our Global Equities team has two roles: **specialist** and **generalist**. The specialist sector role provides the necessary depth of knowledge and coverage of global markets. The generalist role means that each member has oversight and responsibility as a portfolio manager of all client portfolios.

Given we are long term investors, each team member needs to understand how industry & company ESG factors may impact investments and ultimately client portfolios. ESG factors cannot be managed in isolation. The quality of a management team, the ESG risks faced by a company or indeed the opportunity to create value from ‘sustainable’ investments may influence investment decisions and ultimately impact our clients’ wealth.

However, the impact of ESG factors altering investment decisions is subjective. We use our extensive experience and joint roles as specialists & generalists to help us understand and evaluate the **materiality** of ESG factors.

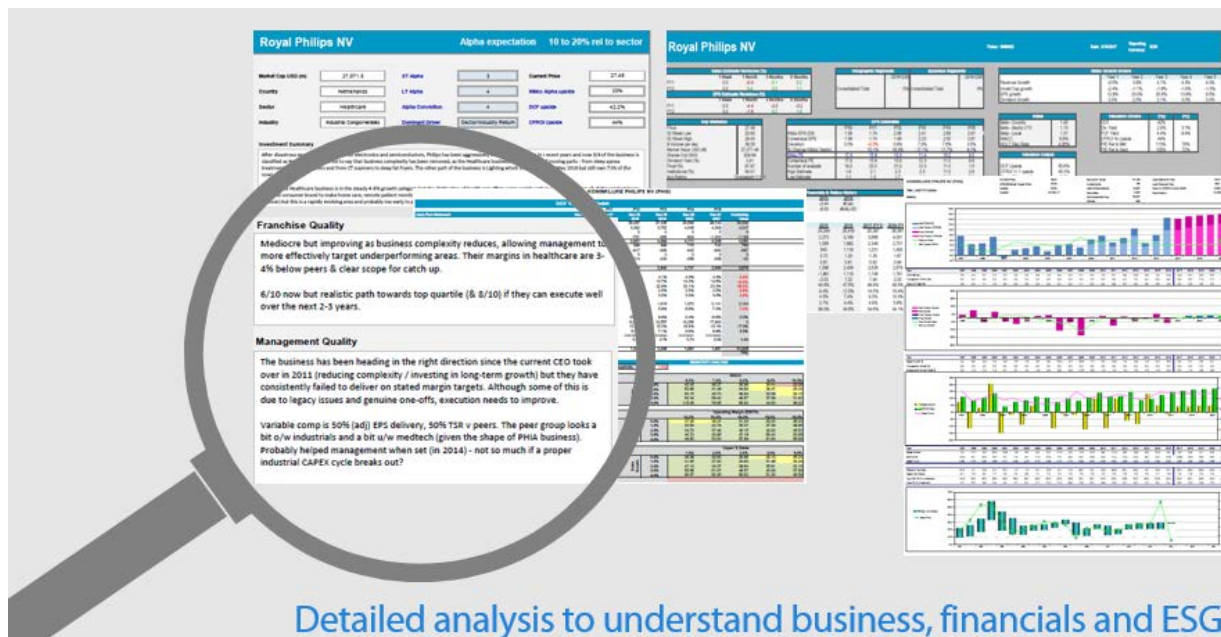
On many occasions ESG factors are not material enough to alter our conclusions, however, a general understanding of ESG analysis can help us build a picture of the risks and opportunities faced by a company.

There is no set formula for quantifying the materiality of each ESG factor or how this might impact a company’s value. We rely on the experience of each team member to articulate the impact in their research reports and investment conclusions.

The combination of each team member’s experience, philosophy & process allow all material ESG factors to be discussed before investment cases are presented prior to inclusion in a client portfolio.

## Execution:

Multi stakeholder analysis such as ESG research is valuable as it provides a more complete view of what might impact the long term value of an investment. Evidence of how we integrate ESG is shown in the example research report below:



For illustrative purposes only

## Voting & Engagement:

The Global Equities team regards voting as an integral part of being a responsible steward of capital. Analysis of a company's corporate governance structure will likely help form our view on the quality of a management team.

The Global Equities team exercises proxy voting rights independently and solely in the interests of our clients and beneficiaries standpoint. Our clients' interests come before our own.

The team does not use standing instructions for voting; all voting decisions are made by the portfolio manager on an individual basis and votes cast via a third party vendor Institutional Shareholders Services (ISS). ISS provides research for all proxy votes but the final decision rests with the Global Equities team.

This process enables the team to control its voting policy and final vote decisions, whilst outsourcing the processing of the proxy voting process.

## Nikko AM's Commitments:

Nikko AM has been a **signatory of United Nations Principles for Responsible Investing (UN PRI)** since 2007. Nikko AM has also launched Japan's first SRI fund and has a history of innovation across all asset classes. Our adoption of the Japan Stewardship Code is set out on our website.

Nikko AM is a member/signatory of the following organisations and initiatives:

- **Principles for Financial Action for the 21st Century:** Nikko AM actively engaged in initiatives from Japan's Ministry of Environment as one of the members of the drafting committee, and we are a steering committee member of Principles for Financial Action for the 21st Century
- **CDP (formerly Carbon Disclosure Project)** – Nikko AM is a signatory since 2006, a global disclosure system that enables companies to measure and manage their environmental impacts.

*It is important to note that we do not exclude particular asset types, industry sectors or securities wholly on moral or ethical grounds, unless this is expressly built into the product's investment strategy or client agreement.*

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