BROCK MILTON
CAPITAL

ESG: CHANGE IS TAKING PLACE

WE SUPPORT
UN GLOBAL COMPACT

Signatory of:
PRI Principles for Responsible Investment

SWESIF
SVERIGES FORUM FÖR HÅLLBARA INVESTERINGAR

Contents

IMPORTANT INFORMATION

Historical returns are no guarantee for future returns. The money invested in funds can both increase and decrease in value, and it is not certain that investors will get back all the invested capital. We recommend that investors read the fund's fact sheet and full information brochure before buying units in the fund.

Background

We only have this one planet with its limited resources, even though we humans are using the earth's assets as if they were inexhaustible. According to a study by the World Wildlife Fund (WWF), the human population lives today as if we had 1.6 planets to provide all our resources and absorb our emissions. This is clearly unsustainable. The consequences are becoming ever more apparent, affecting us all. The switch to a more sustainable future should be in everyone's interests, but it is, most of all, the responsibility of us all.

The way our society conducts business has changed. Sustainability is no longer just an alternative but a competitive necessity. It is a key driving force in operational efficiency and innovation. The fact is, companies that drive their business in a more sustainable fashion have also proven more profitable and resilient, have a stronger brand, and find it easier to attract capital, labor, and skills since they are also more responsive to their customers, employees, and to society.

WHAT DOES SUSTAINABLE DEVELOPMENT MEAN TO BROCK MILTON CAPITAL AB?

To consider sustainability and promote a sustainable development that satisfies today's needs, without compromising on the future generations' ability to satisfy their needs, is a matter of course for us at Brock Milton Capital AB.

Those of us who work with asset management have an important task: to support and allocate capital to companies that influence and drive development in the right way and that also have profitable businesses in the long term.

We take sustainability very seriously. This is not something new or forced upon us. It is part of our DNA and one of the most essential components in our analysis process, helping to ensure we have a more accurate picture of a company's future possibilities and risks. We integrate sustainability work fully into our investment process.

This begins with an ESG screening of every investment prospect to ascertain that the companies fulfil our minimum requirements. After that, our investment team—two managers and three analysts—conducts a more in-depth analysis of each company. It is the team that maintains and drives the entire sustainability work throughout the investment process, and it also takes discussions directly with the companies on ESG and its future development.

To be aware of and understand the impact a company has on its environment, the climate, and society is naturally important, but it is just as crucial to monitor and understand the ways and the extent to which these three factors can affect a company and its future. A company's operations being affected by climate risks (flooding, storms, rising temperatures) can have a considerable impact on its revenues and profitability.

Sustainability and sustainability development are therefore a natural and essential part of our business, forming the basis for our carefully selected investments, which we continuously evaluate through criteria such as the environment, human rights, equality, and other key sustainability measures.

By investing sustainably, we aim to achieve higher returns, avoid unnecessary risks, and do our part in making the world a better place.

RESPONSIBLE OWNERSHIP

We consider and include sustainability at all stages and apply strict procedures, so we can also meet our unitholders' high demands for both returns and sustainable development in the portfolio companies.

At Brock Milton Capital AB, we are convinced that we can contribute to increased awareness, allowing us to together work towards a better world and more sustainable societies. We must set a good example ourselves and live as we learn, sharing our unique skills and experience. To consistently be a conscious owner that closely follows, analyzes, supports, and influences the sustainability work in the companies we own is thus central to our analysis and investment processes.

We are convinced that when those with differing skills and areas of responsibility meet and communicate, the resulting exchange of competences can often lead to increased understanding, contributing to stronger sustainability development, where our combined efforts and actions will make a difference.

To illustrate how we consider sustainability in our asset management and to substantiate how this affects us in our choice of investments, we have put together this report. We believe this will offer a glimpse into our work with sustainable investments and demonstrate the importance that we attach to ESG analysis.

Brock Milton Capital AB—our sustainability work

Since launching what is now known as the Brock Milton Capital Global Select fund in 2014, we have worked actively with sustainability analysis. ESG (Environment, Social and Governance) has always been an integral part of our asset management and is essential in identifying what we call our "Champions"—the world's finest companies.

As an active asset manager, Brock Milton Capital's raison d'être and goal is to deliver a good, sustainable, risk-adjusted return. A well thought-out investment philosophy offers not just the opportunity to deliver a competitive return, but it also limits the risk, including from a sustainability perspective.

The asset managers seek attractively valued companies that act long-term enough that they consider ESG mega-trends such as population growth, urbanization, and new technologies that streamline and improve business models. The fund's investments thus contribute to reducing the negative effects on society in terms of both people and the environment.

INNOVATIONS, TRENDS, AND NEW TECHNOLOGY IN ACTIVE SUSTAINABLE MANAGEMENT

Sustainability factors are crucial to any decision by the investment team on investing in a company. Our analysis is based on understanding a company, its industry, and how external circumstances and trends affect them, while also reviewing how a company's own operations and actions can have a long-term impact on the outside world.

Our ESG process is extremely hands-on. We have no separate ESG function; all ESG analysis is done by the analysts themselves and is integrated into our daily work, alongside our investment process at Brock Milton Capital.

We can cite several examples of companies where our investment team's knowledge, commitment, and its collective experience have allowed the early identification of high risks that could also affect the future valuation of the company. This may include corruption but also other ESG-related risks that could, in turn, mean not only avoiding investing in these companies but also, in some cases, engaging in discussions with them to raise their awareness of the issues and risks.

Through strict and thorough analysis, the asset managers have also been able to identify many positive ESG opportunities among the companies they have invested in, such as products that help the environment through reduced CO_2 emissions and positive trends like the move towards e-commerce and specific consumer goods as people were at home more during the pandemic.

Sustainable investments are very much about new technologies springing from trends and environmental analysis, with a particular focus on minimizing negative climate risks and promoting environmental-related improvements.

Thus, sustainable investments also function as a catalyst that can drive innovation in a company to adapt and transform their business towards a healthier, more efficient, and more sustainable development.

In the end, sustainability (all aspects of ESG) is about consuming, eating, working, traveling, and living harmoniously without destroying the future for coming generations and using up the resources they will rely on.

At the EU level, the finance industry has been singled out as a particularly important actor in the actual implementation of change and the reallocation of society's capital to companies that promote a sustainable development.

Within actively managed funds, asset managers have the possibility to integrate and take into account different sustainability factors in their investment decisions, so that unitholders and investors have the greatest opportunity to receive significantly more than just financial returns on their capital.

HOW IS THE FUND AFFECTED BY EU TAXONOMY?

To help investors easily identify and compare environmentally sustainable investments and to offer clarity and impose higher requirements on companies' sustainability work and reporting, the EU announced a new taxonomy.[1] It is a common classification system or framework that also serves the purpose of facilitating and helping investors to easily identify and compare sustainable investments.

Brock Milton Capital classifies itself as a so-called ”light green product”, according to article 8 of the new EU directive, and the fund's asset managers have, as part of their existing analysis process, committed first to conducting a comprehensive sustainability analysis of several stages.

What the Brock Milton Capital funds may not invest in has been decided in their guidelines.[2] A light green fund is, according to the EU taxonomy, one that has committed to carry out a thorough sustainability analysis in addition to its usual financial analysis and to integrate sustainability risks and environmental impact into all investment decisions.

According to the EU directive,[3] during 2021, the fund must be able to show how its corporate investments are associated or not associated with the first two objectives of the EU taxonomy, as designated by the EU: ”climate change mitigation” and ”climate change adaptation.”

(More about BMC Global Select's classification according to the EU's regulation[4])

HOW WE WORK WITH ESG

- Eligibility for investment: The starting point for our ESG analysis and a key part of our bottom-up stock-picking approach. See WE EXCLUDE, page 6.
- ESG disclosure: We consider it our duty to work actively to encourage our companies in this crucial area. See WE ANALYZE, page 7.
- UN Global Compact: Something we believe every company should sign and work with. Our ESG Impact Letters to our companies encourage them to sign the compact. See WE ANALYZE, page 7.
- Environment: We question our Champions as to their ESG work, CO_2 emissions targets and reductions, and science-based targets and taxonomy-eligible activities, highlighting UN Sustainable Development Goal #13 (*Take urgent action to combat climate change and its impacts*).
- Social: We focus on employee wellbeing and engagement, employee turnover, the gender balance of executive management and the board of directors, and whether this has improved over the past three years, with particular reference to goal #5 (*Achieve gender equality and empower all women and girls*).
- Governance: We look at code of conduct, internal audit functions, and the separation of the CEO and chair of the board roles.
- ESG risks and opportunities: We seek to identify all the ESG risks we can for each company, using ISS ESG to assess whether we have identified all possible risks an investment in a company might bring exposure to.

1. http://www.regeringen.se/regeringens-politik/finansmarknad/taxonomi-ska-gora-det-enklare-att-identifiera-och-jamfora-miljomassigt-hallbara-investeringar/
2. https://www.bmcapital.se/fonder/bmc-global-select and https://www.bmcapital.se/fonder/bmc-small-cap-global-select
3. https://www.fi.se/sv/publicerat/nyheter/2020/nya-regler-om-hallbarhetsrapportering/
4. https://www.bmcapital.se/hallbarhet

How the asset managers at Brock Milton Capital work with sustainability in an integrated manner in their asset management

- A proprietary ESG scoring model results in a premium or discount in the asset managers' valuation model
- On-site meetings at companies' premises over time provide deeper fundamental insights
- Communication with portfolio companies—an ESG letter outlining our expectations sent to all companies we classify as Champions
- A concentrated portfolio allows the asset managers to have deeper ESG conversations with each holding
- ISS ESG is used to support the company analysis—with overall analysis from Coeli's sustainability team
- Company analysis comprises an evaluation of the business model and products, accounts, management, sustainability, and environmental impact, etc. We take a holistic view of the analysis and include all these aspects.

Sustainability analysis—step by step

Sustainability factors are crucial to us when investing in a company. The fund's managers are responsible for ESG analysis with support from a partner company, the Coeli organization.

ESG not only forms the first stage of our analysis process, but also feeds into all aspects of our investment approach. This is because we see an unequivocal correlation between shareholder returns and being a good corporate citizen.

We use independent data provider ISS ESG as a working partner to complement our own analysis in this field. ISS ESG has around 200 ESG analysts globally and generates research on more than 20,000 companies across the globe. ESG is integrated throughout the process of analysis and decision-making on what investments are made. In practical terms, our ESG analysis involves the following steps.

WE EXCLUDE

Eligibility for investment is the starting point for our ESG analysis and is a key part of our bottom-up stock-picking approach. It begins with the application of our exclusion criteria.

Before we make an investment, we always conduct ESG exclusion screening and analysis, allowing us to exclude companies with more than 5% of their revenues from the production of fossil fuels, tobacco, alcohol, pornography, weapons, or gambling. Note: gambling (betting) rather than gaming (computer gaming). We exclude any Russian companies. We also exclude companies that fail to respect the international agreements and norms on human rights, working conditions, environmental issues, and anti-corruption. We use the analysis tools from ISS ESG at this stage.

Why the 5% cut-off? This cut-off is often used when fund management firms talk about which investments they will exclude, and it is also in accordance with the Swedish Investment Fund Association's "Guidelines for marketing and information by fund management companies."

Situations could occur such as a global industrial corporation with a small proportion of its business in some countries that sell military defence equipment, for example, or with a by-product from its industrial process that can be considered a fossil fuel. Our intention is to not invest in companies involved in the areas stated above, but it can also be challenging to anticipate exactly which of these scenarios could occur, and so we have also decided to use the 5% cut-off.

As companies might fall into a gray area when considering these exclusion areas, we choose to take a broad approach to this. If we consider that a company might fall into the gray zone, we err on the side of caution and exclude it. This means our exclusion list is wide-ranging at more than 2,000 companies around the globe. This helps protect us from any negative ESG consequences when deciding upon the companies in which to invest.

In addition to using ISS's ESG database for exclusion criteria, Brock Milton Capital has also signed the UN Global Compact and complies with the ten principles of the initiative. We also take responsibility for our investments, following the six principles and guidelines of the UN PRI investment initiative. Coeli, our partner company, is also a member of Swesif—Sweden's Sustainable Investment Forum. All this helps to ensure the companies we invest in meet the highest sustainability requirements and that we actively work to take our own sustainability responsibilities as asset owners.

WE INCLUDE

All else being equal, we prefer to invest in companies that take ESG seriously and whose businesses have a positive environmental and social impact. In our experience, such companies are often not just well run but also prove to be investments that offer high returns to our unitholders.

Our own analysis ”out in the field” forms part of our work to find these companies. This field work can be anything from company visits and participation at capital markets days and trade fairs to gathering insights from the asset managers' personal networks and monitoring watch lists, such as Barron's Top 100 and Sustainability Corporate Knights Global 100 (the world's 100 most sustainable corporations).

Excludes:

- Fossil fuel producers (>5% of revenues)
- Alcohol manufacturers/distributors (>5% of revenues)
- Weapons manufacturers (>5% of revenues)
- Tobacco producers and retailers (>5% of revenues)
- Gambling (>5% of revenues)
- Companies that breach international norms on human rights, working conditions, the environment, and anti-corruption
- Russian companies

Includes:

- Own analysis – brakes for electric vehicles (Brembo), environmentally friendly gas (Beijer Ref, Carel), energy (Vestas)
- Idea generation from Barron's Top 100 Sustainability (Thermo Fisher, American Water Works, Ecolab)
- Idea generation from Corporate Knights 100 most sustainable corporations (Neste)

Impacts:

- ESG impact letter to the companies we define as Champions, outlining our expectations as a shareholder
- Discussion with portfolio companies regarding ESG – for example, with Carel on the importance of signing the UN Global Compact and with Beijer Ref on the internal audit function.
- Voting at AGM

Quantifies:

- Own developed model that quantifies ESG risks and opportunities.

Another part is desk-bound work, looking at company after company highlighted as good ESG performers by other institutions, so as to establish contact with them and undertake our own analysis.

WE ANALYZE

When we have found an interesting company, we begin our own analysis. Before investing, we undertake the exclusion process outlined above. After that, we scrutinize the company's ESG profile, investigating its ESG reporting, climate initiatives, social impact, and corporate governance, focusing on its internal accounting and shareholder program. Through this analysis, we make an assessment of how large the company's environmental impact is versus the size of its business. We also evaluate the company's ESG risks and opportunities.

A key factor we look for (beyond signing of the UN Global Compact) is whether a company produces an ESG report, how often, whether it has a dedicated ESG person or team within its organization, and if it has set any ESG targets.

The asset managers quantify the company's ESG profile and include this in their valuation of the company. For companies that we judge as taking ESG seriously, that conduct measurable climate initiatives, and that are well run, we assign a valuation premium to comparable companies that fall short on these attributes.

We anticipate higher upside in equities with such a premium and so we are more likely not only to invest in them, but also to keep them in the portfolio for a long time.

ESG also forms part of our evaluation of a company's business model and our ongoing risk analysis.

WE INFLUENCE

We influence the companies that we define as Champions through an ESG Impact Letter, in which we outline our expectations as a shareholder. For example, we urge them to sign the UN Global Compact—the UN's international principles regarding human rights, working conditions, environmental issues, and anti-corruption directed at companies. In our discussions with companies, we promote #5 of the UN's Sustainable Development Goals (Gender Equality) and #13 (Climate Action) by encouraging the companies to work actively with these vital issues.

In addition to this letter, ESG issues form a recurrent theme in our meetings with company representatives, regardless of whether we own shares in the company or not. In addition, we aim to vote at any AGMs where we have a holding in the company. In the future, our activity in this field will accelerate rapidly and our intention is to take part in as many as possible.

WE SUPPORT

5 GENDER EQUALITY

13 CLIMATE ACTION

Company visits and active advocacy work

To provide an accurate picture of the companies we invest in—and the sustainability work they do—we find it particularly important to have physical meetings with the companies and their representatives. We consider these an essential part of our active advocacy work to convince the companies to improve their sustainability work further.

Since the fund's establishment, the managers of BMC Global Select have carried out more than 1,200 direct company interactions, 319 of which were in 2023. Most of these have been physical company visits. In a typical year, we conduct more than one hundred interactions with different companies around the globe, with 2023 seeing an almost doubling versus the previous year. During the pandemic, we replaced physical visits with digital meetings.

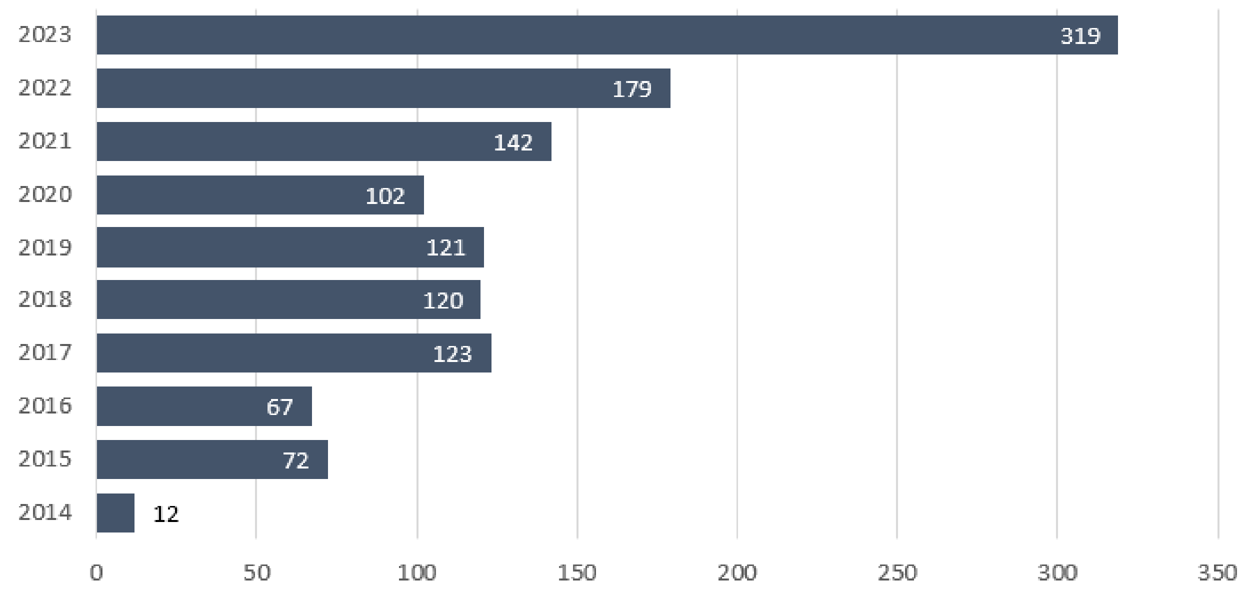
We view physical meetings as extremely important in providing a fair picture of a company. By meeting with company representatives, we have the opportunity to ask questions related to sustainability. This is especially valuable when we have identified deficiencies in this work and communicated these by letter to the company.

ANALYSIS TRIPS

Our asset managers undertake regular major analysis trips as an opportunity to form an opinion of companies' work on-site. These trips offer a chance to verify that companies we find interesting following our analysis actually show this same positive picture in reality at physical meetings.

Most of the trips are to the US and Europe, where a majority of the fund's holdings are based. But the asset managers have also carried out more extensive trips to Brazil and India. We then make detailed trip summaries to collate our impressions of the companies and their markets so as to follow up on them.

Chart 1. The number of direct company interactions per year since BMC Global Select was established



Photos from company visits. Top left: In Paris to meet L'Oréal's Global Head of Corporate Finance and Financial Communication. Top right: At the CMD of Sweden's Axfood. Bottom left: In Silicon Valley to meet semiconductor system designer Cadence. Bottom right: Meeting Jaimin Bhatt, President & Group CFO at Kotak Mahindra Bank.

ADVOCACY WORK

Brock Milton Capital is a relatively small fund manager in a global context, but we believe the companies we invest in take our ESG feedback seriously. We are often given access to those at the top echelons of an organization and can have ongoing discussions with the companies about how they are strengthening their work in this area.

One example of impactful dialogue was when the fund took a discussion with US financial services firm Fiserv in June 2020.

The asset managers set out a requirement in their ESG letters for the company to introduce science-based targets in its climate change work to show more clearly the results of its sustainability endeavors and to link them to the Paris Agreement climate goals.

In addition, we urged the company to introduce "inclusion policies" in its recruitment process. In terms of corporate governance, we suggested that the roles of CEO and chair of the board should be separated and an internal accounting function be established, reporting directly to the board of directors. This is because the company had many geographically dispersed reporting units.

Other examples of active advocacy are our discussions with Beijer Ref, Martin Marietta, NVIDIA, Sterling Infrastructure, SIKA, and Vonovia.

We have, for example, urged some of these companies to appoint a person responsible for ESG and to support and comply with the UN Global Compact's principles/guidelines, take scientifically proven initiatives to fight global climate warming, respect and not interfere in employees' union affiliations, to have an internal accounting function that reports directly to the board of directors, and to improve the gender balance in their management.

The fund's managers have also had ongoing discussions with previous and current portfolio companies, including SIKA, Vonovia, and WDP, to discuss their opinion that more equality is needed in these companies' management groups.

ESG scoring model—the wheat from the chaff

Brock Milton Capital's proprietary ESG scoring model is a unique tool for distinguishing which companies might finally end up in the portfolio. It considers both qualitative and quantitative factors and directly incorporates ESG opportunities and risks into company valuations.

Brock Milton Capital has developed its own ESG scoring model to objectively and quantitatively evaluate a company's ESG work. The purpose of the model is also to allow an objective comparison of companies, regardless of which country they are based in, and to directly include ESG opportunities and risks in a company's valuation.

The model considers factors such as:

- Has the company signed the UN Global Compact?
- Does the company provide detailed ESG accounting?
- How is the gender balance on the board and in general among management in the company?
- Do the company's products support the climate change initiatives needed in the world?

SUPPORTING THE ASSET MANAGEMENT PROCESS AND QUANTIFYING THE ESG PROFILES

The model provides the asset managers with a structured method to evaluate a company's ESG profile and create briefing material that can be used in discussions with a company's management and other representatives.

The model's quantitative results are applied directly to the valuation and have a significant effect on the asset managers' investment decisions since the model can generate a valuation premium of around 15%, rising to 20–30% in exceptional circumstances.

This work goes hand in hand with the view that those companies taking ESG seriously are better run than others, and this creates both higher return possibilities for unitholders and minimizes investment risks. The ESG model allows these views to be integrated, becoming one and the same.

As active investors, it is our job to find incorrectly priced companies. Experience tells us that the stock market is often relatively skilled at setting the price of a company, and many shares trade within 20% of the value that one can objectively estimate the company should be valued at under normal circumstances.

A company judged by the ESG model to be doing particularly good work can receive a valuation premium of 30% or more—a level that is considerably higher than the 20% upside potential that typically makes an investment in a share look attractive.

Chart 2. The impact of Brock Milton Capital's ESG model on valuation

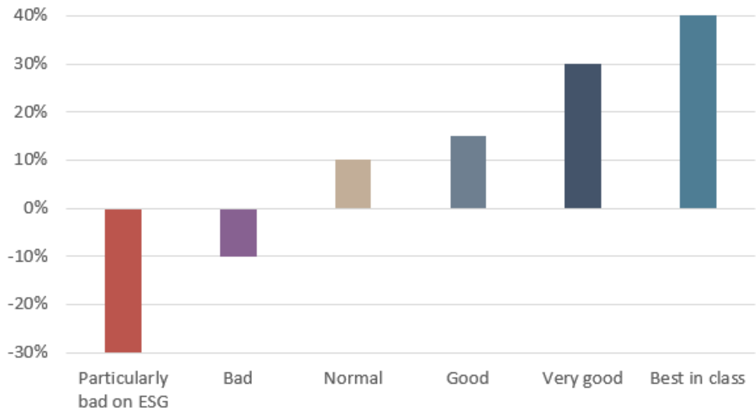
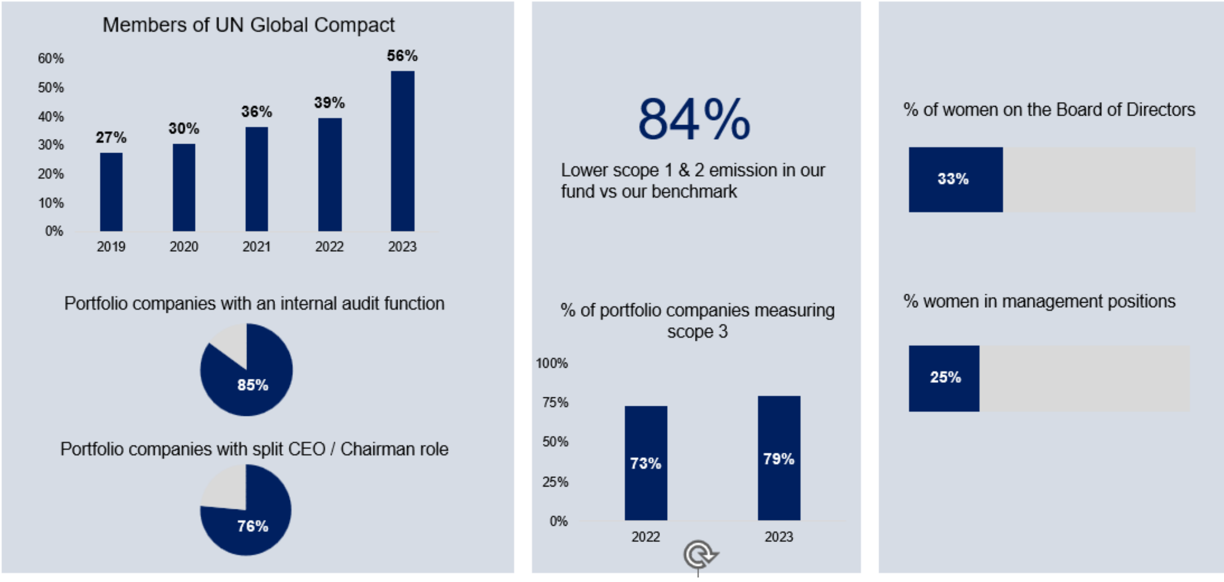


Chart 3. BMC Global Select key ESG performance factors, as of October 31, 2023



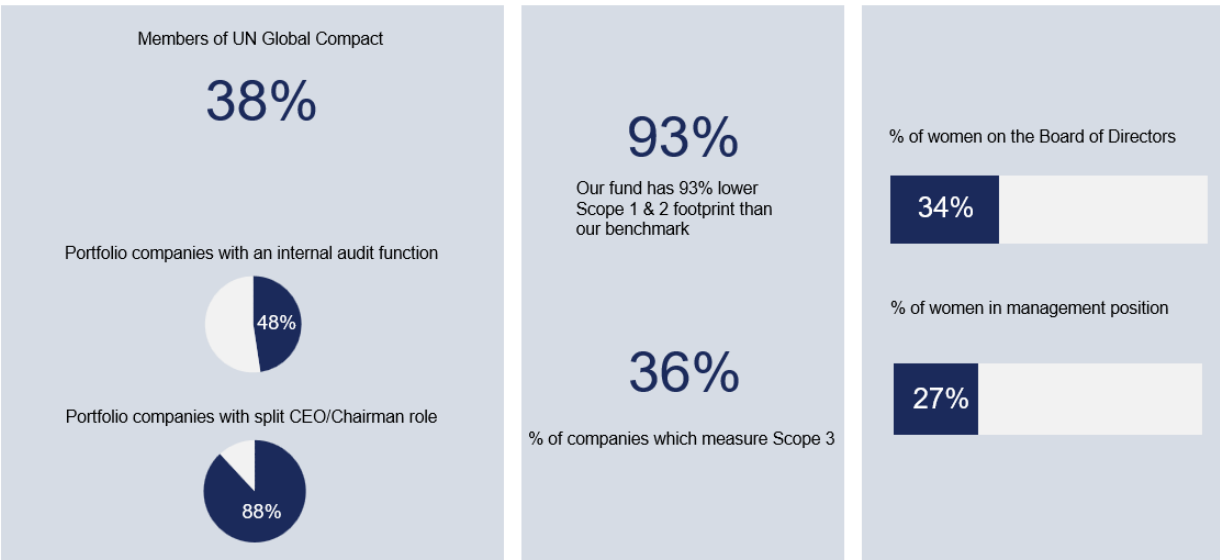
That ESG factors can have such an impact on valuation mean that the asset managers are much more likely to invest in companies with a good ESG profile and also to hold such shares at a greater weight in the fund and for longer.

On the other hand, the model can also assign an ESG discount of -30% or more, making it near impossible in practice to own a company with a low focus on the environment, gender equality, and/or corporate governance.

We can see from the chart for BMC Global Select above that, encouragingly, a growing proportion of our portfolio companies have now signed the UN Global Compact and a majority of them are performing well with measuring Scope 3.

On the governance side, a majority also operate an internal audit function and have split the CEO and chair of the board functions. However, female representation is still lacking on both boards and management teams—something we are encouraging them to improve.

Chart 4. BMC Global Small Cap Select key ESG performance factors, as of November 30, 2023



Location and size matter

Two aspects that can impact the extent of a company's work on ESG—and that also are key factors for our funds—are size (large caps versus small caps) and location (regional differences in sustainability goals).

LARGE CAPS VERSUS SMALL CAPS

As you might imagine, the larger a company, the more resources it has to spend on improving its sustainability and ESG status. Many of the larger companies in our portfolio have these resources and are using them to great advantage. That is not to say that there are no ESG stars in our small cap portfolio; simply that these smaller companies have other priorities that they need to spend their resources on before they can target ESG improvements.

The average ESG score in our proprietary scoring model is 16% for the BMC Global Select fund, while the BMC Global Small Cap Select fund has a more than respectable score of 10%. The difference between these two is not that substantial, and we hope to see it narrowing over time as we continue to work with our companies to identify and progress towards their ESG goals.

We can also see the difference between the large caps in our Global Select fund and the smaller companies in our Global Small Cap Select fund in the number of these that have signed the UN Global Compact. Among the large cap companies in our portfolio, 56% had signed as of the end of October 2023, compared with 38% among our small cap companies.

Moreover, 79% of our large cap holdings currently measure Scope 3 emissions versus just 36% among our small cap companies. Rather than seeing this as a drawback, we view this as an amazing opportunity for us to work with our companies—both large and small—and thus encourage them to make improvements to their emissions reporting and sustainability endeavors.

Interestingly, on the governance front, the results between our large caps and small caps vary. Our small caps score

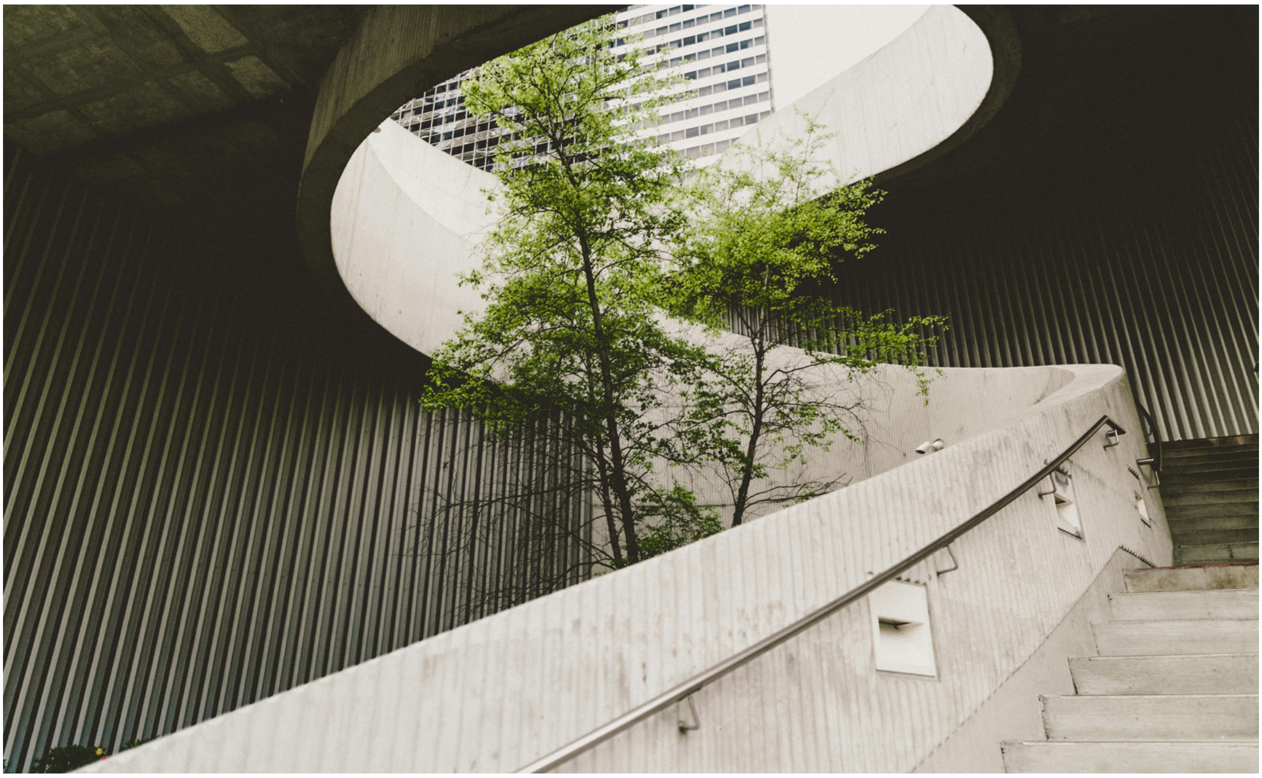


Image by Alexander Abero


Image by Vlad Hilitanu

marginally better than our large cap holdings on having women on the board (34% for our small caps versus 33% for the large cap holdings) and on women in management (27% versus 25%).

They also surpass the large caps on having separate CEO and chair of the board roles (88% versus 76%). On having established an internal audit function, however, the small caps have some room for improvement, with them coming in at 48% compared with 85% for the large cap holdings.

We are grateful for this chance to maintain close contact with our companies and help them to identify areas for ESG improvement they might themselves not have considered—including beyond these areas highlighted here.

REGIONAL DIFFERENCES ARE CLEAR

Not all companies tackle sustainability and ESG in the same way across the globe. In fact, we can identify clear regional differences when looking at the companies in our global funds. Our experience from investigating and assessing our companies' progress on ESG provides us with a number of examples of this.

Our US-based companies, for instance, tend to take social aspects—the S in ESG—particularly seriously, focusing on that more, and going beyond simply ensuring a good gender balance. However, this can sometimes seem at the expense of environmental (E) and governance (G) concerns.

In fact, on the governance front, we find that many more US companies have a CEO who also holds the role of the chair of the board—AMD and MSCI among them—while this is far less common among our European holdings.

Thanks to the EU's taxonomy for sustainable activities, many European companies focus on ways to improve their environmental footprint and on reducing CO_2 emissions, which is something they can typically score more highly on than their US counterparts.

Interestingly, when it comes to our Asian companies, we see a greater focus on governance—who owns a company and how their corporate governance has been set up—along with an increased interest in environmental issues, and more so than in the US.

As with the differences between large and small caps, the regional variations offer us the chance to see which of our companies are doing better on certain areas of ESG and to identify where others can improve, using these insights in our Impact Letters to encourage them to make meaningful changes.

How our portfolio companies work with sustainability

Working actively to maintain the highest possible sustainability standards is an important piece of the puzzle in creating and maintaining competitive advantages and attracting both capital and competence in the longer term, we argue. On the following pages, we showcase a handful of our companies and their sustainability work—some excelling and others needing to improve.

ASML—SIGNED UN GLOBAL COMPACT, BUT MORE WOMEN NEEDED IN TOP MANAGEMENT OVER TIME

As is common among semiconductor equipment firms, ASML reports low on emissions thanks to its low-impact business since it does not manufacture the chips itself.

We have previously highlighted the company as having room for improvement on the sustainability front; however, we have been pleased to see recent improvements, although Scope 3 remains its largest source of emissions—something that is typical of its industry.

ASML signed the UN Global Compact in 2023 as part of its ongoing ESG work and has committed to contributing to the UN's Sustainable Development Goals and the 2030 ambitions included in these. The company has set Scope 1–3 targets for CO_2 emissions comprising being net zero on Scope 1 and 2 by 2025, net zero emissions from its supply chain by 2030, and net zero from use of its products by 2040.

In 2021, the group appointed a Head of ESG Sustainability to strengthen its focus on this area, and it had expanded its ESG team from three people to 16 within a year of this. It takes ESG seriously as a key part of its operations, sharing its sustainability strategies and programs with its stakeholders and providing sustainability training to employees.

One area where further improvements could be made is the gender balance of its senior management team. Unlike the board (almost 45% women), senior management is made up entirely of men.

FERRARI—BECOMING CARBON NEUTRAL BY 2030

One of our ESG performers that might raise some eyebrows is Ferrari.

Who would expect a car manufacturer to be among those performing well on sustainability? However, Ferrari has recently joined the UN Global Compact and has long been transitioning towards electric vehicles in its fleet. In 2022, it started its work towards carbon neutrality by 2030, and it is transparent in its targets for Scope 1–3 emissions.

A surprise from a company known for its fast cars and participation in Formula One motor racing.

YOUGOV—AN ESG TOP PERFORMER WITH A GREAT GENDER BALANCE

YouGov says ESG is at the core of all it does, with the group employing a top-down approach that flows through its business. And we believe this is validated by it having won its second MSCI ESG rating of AA in 2023.

YouGov®

The company formalizes its ESG work in what it calls its "ESG Roadmap," in tandem with its annual ESG reporting and a Task Force on Climate-Related Financial Disclosures (TCFD) report. To comply with UK procurement policy, the group has established a Carbon Reduction Plan.

It evaluates its ESG approach regularly, understanding that regulations can change rapidly, and is proud of its work on this front. YouGov is transparent in documenting its Scope 1–3 emissions as part of its annual financial reports, breaking down the figures for easy comparison.

YouGov is committed to engagement with both stakeholders and employees, having open communication channels, a diversity and inclusion policy, and making efforts to document its pay gap reporting—all factors that stand out.

It also attracts attention with a good gender balance on its board and within senior management, and as is common among many UK companies, the chair of the board and the CEO are separate roles.

EAGLE MATERIALS—CONSIDERABLE POTENTIAL TO IMPROVE ITS ENVIRONMENTAL IMPACT

Like Ferrari, cement company Eagle Materials is a surprising inclusion in the list of companies performing well on sustainability measures.

Operating in a traditionally polluting industry, Eagle has worked hard to lower its emissions (reporting a reduction in relative terms of CO_2 per ton of cement produced), and as a consolidator in this field, it has also improved the pollution profile of its acquired plants.

Initiatives include changing to Portland limestone cement (a 100% achievement of this implies a 20% reduction in CO_2/ton from the 2011 baseline) and investing in research and development of carbon capture and other emerging technologies.

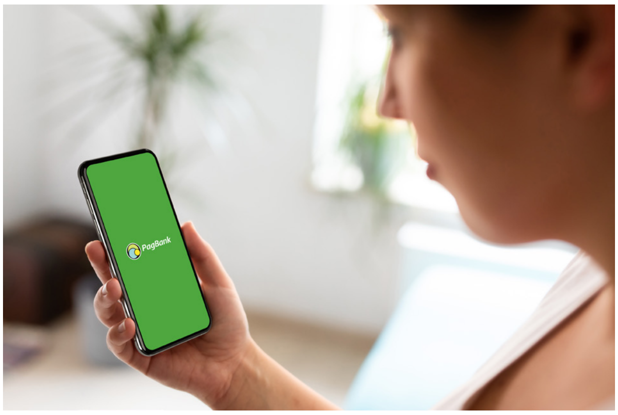
Energy usage is one of the key issues in the production of cement, as this is often coal-powered. Eagle has responded to this by conducting pilot studies into the use of alternative fuels.

The company has established an ambitious Net Zero target by 2050, which is all the better to see from an organization working in an industry that has typically been among the worst polluters across the globe.

On the governance side, more than 50% of the CEO's annual bonus is linked to ESG targets, which is encouraging to see, especially from a US company and one in this industry.

PAGSEGURO—LOW ENVIRONMENTAL IMPACT AND GREAT GENDER BALANCE

Among our ESG performers, digital financial solutions provider Pagseguro (PagBank) can be applauded for its excellent sustainability report, which it has been publishing since 2020.



The comprehensive report covers a wide range of ESG topics, including the group's work towards the UN's Sustainability Development Goals, its transparency on the corporate governance front, and its risk management—a factor essential to a financial services firm. Moreover, the company signed and has been committed to the UN Global Compact since 2021.

As a services provider, its environmental impact is lower than for companies operating in other industries, but it prides itself on its focus on maintaining its capital across a handful of key areas: financial capital (its financial results), intellectual capital (its digital business), human capital (its staff, with a focus on diversity, inclusion, and corporate culture), natural capital (climate strategy and targets, reporting of Scope 1–3 emissions, and aligning itself with the Task Force on Climate-Related Financial Disclosures (TFCD)), and finally social and relationship capital (relations with customers, investing in the community, and working towards better financial education in its domestic market of Brazil).

Although it has been awarded a Women on the Board seal, thanks to having a 50:50 split between men and women on its board, its senior management comprises solely men. However, Pagseguro is also a signatory of the WEPs (Women's Empowerment Principles) to promote gender equality and women in the labor market, which is a positive indicator.

EXCLUSIVE NETWORKS—TAKING ESG INCREASINGLY SERIOUSLY

Cybersecurity specialist Exclusive Networks responded positively to our Impact Letter and we've been heartened to see the company making a start on improving its sustainability monitoring and reporting.

It is considering adopting the UN Global Compact and has taken steps to enhance its reporting and sustainability, with a sustainability report that complies with GRI standards and discloses its climate change learnings to CDP.

Its appointment of a senior sustainability manager, who reports directly to the Group General Counsel and Compliance Officer, is a further positive note that we appreciate.

Exclusive Networks has aligned its Decarbonation Plan with the Science-Based Target initiative and is considering formally adopting the framework to document its accountability.

Our key governance concerns, namely the separation of the chair and CEO roles and the implementation of an independent internal audit function, have been addressed.

The company has also established an incentive program that ensures that senior management members hold personal financial stakes as part of their compensation packages. It is considering aligning these with ESG targets in the future, which we appreciate.

CAREL—INDUSTRY LEADER WITH GREAT POTENTIAL ON ENVIROMENTAL IMPACT

Carel's motto "Better control, better environment" also forms the basis of its sustainability strategy, as it continuously works to improve the importance of ESG within its business. The company's commitment to sustainability is robust, with its dedicated ESG team having produced a 2024 sustainability plan that encompasses the guidelines it has already employed over the past few years.

By their very nature, Carel's operations aid the HVAC industry in moving toward more environmentally friendly options, thanks to the company's focus on optimizing energy efficiency and the transition toward using the less polluting natural refrigerant gases and fluids. Carel's work in urging stakeholders to embrace these new cooling mediums is certainly encouraging, given the positive impact on greenhouse gas emissions.

CAREL

The company signed the UN Global Compact in 2022, committing to support the UN's Sustainable Development Goals and sowing the seeds of these ten principles throughout its organization and operations. It reports on its progress towards these in its annual ESG report.

These moves have borne fruit in recent years, with the company seeing its MSCI ESG rating moving to AA in 2022 and it being named in the ESG Leaders category of those companies best managing ESG risks and opportunities.

The governance aspect of ESG is an area in which Carel has room for improvement, however. Although the gender balance on its board is outstanding (more than 50% female), its management team comprises only men.

SIEGFRIED—OUR WORK HAS HOPEFULLY BEEN PAYING OFF

Swiss contract development and manufacturer Siegfried is a company with which we have particularly active engagement thanks to our portfolio's shareholding. Our Impact Letters have previously encouraged the company to link management compensation to ESG targets and to establish an internal audit department.

Whether or not Siegfried responded to these wishes from us, or from another source, we are particularly pleased to have seen them implemented.

The company is a recognized leader in sustainability, with an MSCI ESG rating of AA (promoted in 2022) and three years under its belt as a member of the Dow Jones Sustainability Index (DJSI) Europe. In 2022, it also joined the Science-Based Targets initiative and was awarded a "Committed" status.

Siegfried has set goals for lower energy and electricity consumption, as well as a smaller carbon footprint, and has a dedicated Sustainability board to ensure this is in focus daily, as well as producing a comprehensive annual sustainability report. Moreover, it has joined the Reuters-led Vision 2045 initiative to support the UN's Sustainable Development Goals, contributing a particular focus on green bioscience.

Positively, like many other European companies, Siegfried has separate roles for CEO and chair of the board, although its gender balance in both senior management and on the board could be improved.

We are also happy to see that a dedicated Strategy & Sustainability Committee works closely with the overall board to ensure the company's sustainability efforts.

QUALYS—A US COMPANY TAKING MAJOR STEPS ON ESG

Cloud security and compliance provider Qualys took a major step on the sustainability path with the publication of its first sustainability report for 2022. Although this initial report was slimmer than many other companies' similar documentation, we've been pleased to see such moves from the US company.

It has measured Scope 1 and 2 emissions since 2020. As a digital service provider, a majority of its location-based emissions stem from electricity usage—something that increased during 2020 and 2021 as working environments changed. Despite this measuring and monitoring of Scope 1 and 2 emissions, Qualys has not set definitive targets for either; instead, it has stated a desire to investigate alternative renewable energy sources and power purchase agreements.

The company has stated its support for the UN's 17 Sustainable Development Goals, with a particular focus on six: quality education; gender equality; decent work and economic growth; industry, innovation and infrastructure; responsible consumption and production; and climate action.

Its management team could have a better gender balance (currently, seven men and two women), likewise its board

(five men and two women). However, it is positive that, as a US firm, Qualys has taken the decision to keep its CEO and chair of the board positions separate.

We will encourage Qualys to dedicate itself further to setting emissions targets and compiling a more comprehensive sustainability strategy and report, but we are gratified to see it heading in the right direction.

BRØDRENE A&O JOHANSEN—A SMALL COMPANY MAKING THE RIGHT MOVES

Although one of our smaller companies, AO has shown that size and more limited resources don't have to be a hindrance in sustainability action and reporting.

It acknowledges its limited Scope 1 and 2 emissions, reporting these in its annual financial report, but has nonetheless set an ambitious target of making itself carbon-neutral in these two areas by 2030. Regarding Scope 3, it intends to define these emissions, allowing it a base from which to reduce them as part of its ongoing sustainability work, alongside its aim to implement Science-Based Targets.

One previous red flag that we identified in the group—the low female representation on its board—has been partly resolved with the inclusion of one female board member in 2023, and the group has set a target of 40% female board representation by 2025.

We would welcome the creation of an internal audit function in AO as part of its governance work, as well as the linking of executive remuneration to ESG targets, and we will be keeping an eye out for these in the future.

AO is moving in the right direction towards transparency in its sustainability activity, proving that size has little to do with taking responsibility.

MARTIN MARIETTA—WE FINALLY HAVE SCOPE 1, 2, AND 3 GOALS

Like Eagle Materials, US building materials supplier Martin Marietta is a somewhat surprising inclusion among companies with solid sustainability goals and progress.

In fact, it even goes beyond the work that Eagle is doing, having produced annual sustainability reports (that have grown in scale each year) since 2019.

Included in the reports are extensive comments on the company's Scope 1–3 emissions as well as its targets, which it aims to achieve via coal replacement and tire-derived fuel investments, use of alternative fuels, substituting natural gypsum with synthetic versions, modernizing plants to increase efficiency, and lowering equipment emissions.

Image by Luis Tosta

Image by Nick Page

Martin Marietta's foremost environmental target is its goal to achieve net zero in Scopes 1–2 across all its product lines by 2050—something of an impressive target for a company that operates in an industry known for its negative environmental impact. However, Martin Marietta believes these improvements and changes to its operations will secure this goal.

Moreover, the company focuses on improved water and waste management and minimizing its operations' impact on the local environment and biodiversity.

On the corporate governance side, Martin Marietta follows the pattern of many other US companies with its CEO also sitting as the chair of its board. This is a typical situation and something we highlight to our companies as a potential change they can make.

Martin Marietta's board's gender composition could also be improved (currently, seven men and three women); likewise, its management team skews more male (five men and two women).

COMPANIES WITH UPSIDE POTENTIAL

We are aware that approaches to ESG and sustainability vary substantially across the globe, but we relish the opportunity that our global investments give us to send our Impact Letters to companies in markets like the US where there is less focus on the environmental and governance aspects fo ESG.

These companies are largely starting out on their sustainability journey, and we will continue to encourage them to create goals and targets, to make progress in reducing their emissions, to contribute to their local environments and society as a whole, and to improve in their corporate governance.

Among our US companies, we can highlight some progress from **Asbury Automotive Group**, which has established an energy management program as part of its aim to reduce emissions, such as by introducing zero emissions vehicles at its dealerships. However, the company has no stated policy on reducing Scope 1 or 2 emissions and its sustainability report (its "Corporate Responsibility Report") is quite thin. We will continue to urge Asbury to measure its Scope 1–2 emissions and improve its sustainability reporting.

Although security solutions provider **Napco Security Technologies** offers no information on the sustainability front, we believe this lack of progress only leaves potential on the table for improvements—something we will keep working towards.

AutoPartner is another of our newer portfolio additions that we are urging towards greater responsibility on the ESG front via our Impact Letter and our discussions with management, highlighting potential areas for improvement. We would welcome seeing the company establishing an ESG reporting structure, starting to measure its CO_2 emissions, and improving the gender balance on its board and among senior management.

Likewise, we are encouraging **Sterling Infrastructure** to start measuring CO_2 emissions and to set targets for these, while we have also highlighted the gender imbalance in the company (an all-male management team and a board of five men and two women.

Another new portfolio addition, HVAC distributor **Watsco**, is among those with extensive potential to advance on the ESG front. Although it aims to be part of its industry's transition towards low-carbon products, Watsco does not measure CO_2 emissions and has not set definitive targets to achieve by a certain time. We encourage it to do so and to separate the chair of the board and CEO roles.

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