Rathbones Group Plc

Influence through dialogue

Rathbones Group engagement action plan for 2023

Rathbones

Our engagement approach

At Rathbones we believe that it's important to have an active dialogue with the companies in which we invest across a wide range of issues, including environmental, social and governance (ESG) questions. We're motivated by academic evidence that engagement with companies on material issues can lead to better investment outcomes by improving corporate behaviour.[1] In this report we outline an action plan for our engagement activity in 2023. We've selected eight planned priorities, which we assign to separate environmental, social and governance sections.

We expect many of these engagement themes to remain a focus over a number of years. For this reason it's important to track progress against objectives. In the interests of transparency, we provide an honest assessment of how much progress we made in advancing our engagement priorities for 2022. Our evaluation of that year is a brief summary, but more details can be found in our annual and interim responsible investment reports covering 2022.

Voting

Our engagement with companies would probably come to naught without the opportunity we have, as shareholders, to back up this engagement with votes at companies' annual general meetings (AGMs). In practice, we only feel the need to vote against the board on quite a small minority of occasions – about 7% of the time in 2022. However, the power of our engagement as investors rests on the board's knowledge that we will, if necessary, oppose them at the AGM.

Historically, AGM votes mainly covered the G in ESG: governance. They were also primarily about voting on resolutions tabled by management. These days, however, we see AGM and voting activity increasingly dealing with environmental and social concerns. We've contributed to this trend: Rathbones has adopted a more detailed voting policy on sustainability, which often triggers engagement with company boards on serious ESG issues and risks that we identify. Given the recent trend, we expect an increase in ESG-themed resolutions tabled by shareholders, rather than management, in our clients' holdings in 2023.

[1] arabesque.com/research/From_the_stockholder_to_the_stakeholder_web.pdf

Our ***responsible investment policy*** defines responsible investment as:

> The purposeful integration of environmental, social and corporate governance (ESG) considerations into investment management processes and ownership practices in the belief that these factors can have an impact on financial performance.

We engage on a wide range of ESG issues, including:

Environmental

- Climate change
- Biodiversity loss
- Energy efficiency
- Resource depletion
- Waste management
- Air and water quality

Social

- Equality and diversity
- Employment rights
- Human rights
- Supply chains
- Data protection and privacy
- Product safety and liability

Governance

- Management structure and compensation
- Accounting and auditing standards
- Board leadership, diversity and independence
- Succession management
- Shareholder rights

Engagement priorities

The world of ESG is fast-moving and dynamic. Many issues vie for our attention. It's important that we balance the long and short-term.

In deciding whether to engage, we consider:

1. **Exposure:** across our portfolios we may hold stakes in smaller companies that, while small in value, are significant because they account for a high proportion of total voting rights. We're more likely to engage directly where we hold a significant stake in the company, which we define as above 3% of its share capital, or where shares in the company are widely held across Rathbones.
2. **Severity:** we're more likely to engage on issues that present an immediate, systemic or severe threat to the best interests of our clients, or where the ESG issues in discussion are pressing and serious.
3. **Location:** we're more inclined to engage with companies when we have a deeper understanding of the local legal framework.
4. **Expertise:** we're more likely to engage where we have a deeper experience of a company or issue. We select certain issues for specific action each year and develop specific policies for the most important ESG engagement issues.

Environmental priorities

Climate change — net zero

Issue

In 2021, Rathbones Group Plc announced its own plans to achieve net zero emissions by 2050 or sooner. The majority of emissions we're responsible for are financed emissions: they're created by the companies that we invest in. We have established an engagement programme covering the highest-emitting companies within our holdings universe. We want to see at least 57% of our underlying holdings set climate targets validated by the Science-Based Targets initiative (SBTi), an arbiter of corporate climate change targets, by 2030.[2] Failing that, we want them to have committed to this. Over the past year we've made important changes to our net zero engagement strategy and voting policy to reflect the urgent need for escalation with companies not yet aiming for their own net zero future.

Objectives

- Gain credible net zero commitments from target companies.
- Improve the quality of transition plans for net zero so that they meet expected guidelines and standards.

Targets

Identify priority companies by taking into account:

- The amount of carbon companies are responsible for emitting.
- Companies' share of our financed emissions.
- The need to attain our own SBTi-approved net zero targets.

Nature and biodiversity

Issue

Natural ecosystems provide the foundations for economic growth, human health and prosperity. These benefits are sometimes known as 'ecosystem services'. As economic activity depends on ecosystem services, the degradation of nature and reduction in biodiversity - the variety of plant and animal life on Earth - are financially material. By this, we mean they could harm the financial performance of companies that rely on their preservation. Recognition of the importance of this issue, among policymakers and in the financial sector, is gaining powerful momentum. This has given increased authority to institutions and frameworks such as the Taskforce on Nature-related Financial Disclosures and the UN Biodiversity Conference, which held its most recent summit, COP15, in 2022 in Montreal.

Objective

Engage with priority companies to encourage them to identify, mitigate and reverse negative impacts on nature and biodiversity - and therefore on ecosystem services. Discuss with them effective targets and strategies, as well as appropriate measurements and good disclosure of negative impacts and progress in reducing them.

Targets

We've identified priority companies through our own model, which combines ESG data from different external providers with our own scoring system. The stewardship team has selected 28 top-priority companies - those with the most impact on land ecosystems - and 24 secondary-priority businesses. These are the companies that pose the greatest risk to nature, with a focus on those with the most impact on land ecosystems.

[2] The SBTi is an arbiter of corporate climate change targets. For more information, see sciencebasedtargets.org/

Hazardous chemicals

Issue

Hazardous chemicals find a use in many different consumer products, but their persistence in the environment poses risks to human health and the environment. Specifically, a class of chemicals known as PFAs do not degrade after use. Their durability increases the risk of cancer in humans and damages plant and animal life. Some applications for PFAs lack readily available alternatives. However, in many cases such substitutes exist. We believe that chemicals companies aren't doing enough to publicise to their customers the existence of these alternatives.

Objectives

- Advocate for increased efforts to phase out harmful persistent chemicals in favour of alternatives that are more sustainable because they're less harmful.
- Obtain greater transparency, including disclosure of all hazardous chemicals produced.
- Persuade companies to publish a timed phase-out plan for persistent chemicals.
- Encourage companies to work to improve their ranking in ChemScore, an industry benchmark that ranks the world's top chemical producers on their work to reduce their chemical footprint.

Targets

Working with the non-profit organisation ChemSec, we're engaging with 54 of the world's largest chemicals companies.

Social priorities

Modern slavery

Issue

Some 50 million people were in forced labour or forced marriages in 2021, according to a United Nations report.[3]

In a landmark piece of legislation to combat modern slavery, Section 54 (s54) of the UK Modern Slavery Act 2015 created a duty for companies with a turnover of £36 million or more to publish a statement annually and have it approved by the board, signed off by a director, and uploaded to a prominent place on the homepage of the UK website. The statement must set out the steps they've taken to ensure modern slavery isn't taking place in their business or supply chains.

However, the Act contains no mechanism for enforcing s54. With this in mind, we launched Votes Against Slavery in 2020, following a pilot scheme in 2019. The 'Votes' in 'Votes Against Slavery' refers to the commitment of investors taking part in the campaign to vote against a company's annual financial statement and statutory report if it failed to meet the demands of s54.

In 2022 the campaign targeted the 44 FTSE 350 companies that hadn't published a compliant s54 statement as the year began. By year-end, 41 of 44 companies had done so - and the remaining three had committed to complying before their financial year-end.

Votes Against Slavery won 'Stewardship Initiative of the Year' in the 2022 Principles for Responsible Investment (PRI) awards.

We will continue our engagement on this important issue in 2023.

Objectives

- Re-run Votes Against Slavery, aiming for a 100% success rate for proper disclosure for FTSE 350 companies (see Targets that follow).
- Hold a meeting with every FTSE 350 target company to address the content of their modern slavery statement. We will be assessing the quality of companies' action against modern slavery, even if they're complying with the letter of the law.
- Separately from the Votes Against Slavery collaborative engagement programme, Rathbones will also directly engage with the FTSE AIM companies with the highest revenue to press them to comply with s54.

Targets

- For Votes Against Slavery, the 29 FTSE 350 companies that don't comply with the s54 disclosure requirements.
- Separately, Rathbones will target 59 FTSE AIM companies.

Modern Slavery Bill

Issue

In 2019 the Home Office asked for views on how to improve the Modern Slavery Act. Rathbones and CCLA, another investment manager, responded with a joint submission. Rathbones is now co-ordinating the investor response to proposed changes by three non-governmental organisations, Anti-Slavery UK, Justice & Care and Unseen UK, to the UK Government's new Modern Slavery Bill. These proposals include the suggestions made by Rathbones and CCLA back in 2019. But they also go further, calling for a legal framework for the transparent imposition of controls to prevent the import of goods and services that rely on slave labour.

Objective

Ensure that the proposed demands, strengthening s54 (see modern slavery) and import controls, are included in the new Modern Slavery Bill.

Targets

Our ultimate target is the UK government, which is drafting the bill. However, to achieve our aim, we're also seeking engagement and collaboration from investors who subscribe to the Votes Against Slavery and PRI Advance (see section on human rights) initiatives, to persuade them to join us in putting the case for our demands to the government. We aim to secure the support of at least ten investors.

[3] ilo.org/global/about-the-ilo/newsroom/news/WCMS_855019/lang--en/index.htm

Human rights

Issue

Some issues are too wide-ranging and important to leave to the efforts of one investor. The need to advance human rights and fundamental freedoms is one such issue. We will pursue progress in this field within the framework of Advance, a collaborative stewardship initiative organised by the PRI.

Objectives

Press companies to:

- Fully implement the UNGPs, the United Nations' Guiding Principles on Business and Human Rights - a guardrail of corporate conduct on human rights.[4]
- Align their political engagement with their responsibility to respect human rights.
- Deepen progress on the most severe human rights issues across their value chains. This includes both their own operations and goods and services supplied from outside the company.

Targets

- Companies whose business could have an impact on human rights, and policymakers involved in this field.
- In particular, the multinational utility company Iberdrola, for which we will lead the engagement for Advance.

[4] ohchr.org/sites/default/files/documents/publications/guidingprinciplesbusinesshr_en.pdf

Governance priorities

Board diversity

Issue

We've engaged for many years on gender and racial diversity on boards. Academic evidence suggests that diverse groups of people may make better decisions.[5] Some studies reflect how diversity can also be beneficial in a business context. McKinsey, the management consulting firm, states that executive teams featuring strong gender and ethnic diversity are more likely to outperform their peers on a range of corporate performance measures such as profitability, compared with more uniform teams.[6]

In 2022 the Financial Conduct Authority (FCA), a UK regulator, raised its target for gender diversity on the boards of listed companies. These are on a 'comply-or-explain' basis: if companies don't meet the benchmark they must explain why not. Its new targets for boards include:

– At least four in ten to be women.
– At least one woman in a quartet of senior board positions - chair, senior independent director, chief executive officer or finance director.
– At least one member from an ethnic minority background - the target of the UK government's Parker Review.

Objectives

– Request compliance with the new targets.
– Request planning is put in place to create a pipeline of talent across all levels of the company, to position any company that hasn't done so to meet these targets.

Targets

FTSE 350 companies that are still falling short of the FCA's three benchmarks.

Governance at smaller companies

Issue

For companies both large and small, good corporate governance helps protect shareholders' best interests and makes management more aware of issues that matter to wider society. The Quoted Companies Alliance (QCA) operates a code of governance for companies not covered by the UK's main governance codes. We take alignment with the QCA code as a sign that smaller companies are taking the management of ESG risks seriously.

Objectives

– Make sure all targeted companies are aware of the demands of the QCA code and of investor support for its requirements.
– Undertake dialogue with these companies, aiming to secure a firm timetable for compliance, ideally by the end of 2024.

Targets

Smaller and mid-sized companies not yet compliant with the QCA code. We've identified 72.

[5] physicstoday.scitation.org/do/10.1063/pt.6.1.20201223a/full
[6] mckinsey.com/featured-insights/diversity-and-inclusion/diversity-wins-how-inclusion-matters

Reviewing 2022: how did we do?

Rathbones engagement priorities for 2022

Successful | Partially successful | Limited progress

Environmental

Net zero strategy: We contacted 25 priority companies, clearly setting out our expectations as investors. Ahead of the 2022 voting season, we engaged with high-emitting companies. However, there were fewer clear examples of actual change.

Nature and biodiversity: We didn't make any progress in engagement but did the essential preparatory work, including deepening our knowledge of the issue. We will ramp up our engagement in 2023.

Social

Votes Against Slavery: Every target company was compliant by the end of the year.

We increased the number of companies we held meetings with from 7 to 13. This allowed us to put our point of view across effectively and to learn more about how each company is tackling slavery within its supply chain.

Governance

ESG and pay: Over 90% of FTSE 100 companies have now included a measure linking pay to performance on ESG issues. However, we need to conduct further analysis of whether this improves ESG risk management. Companies were fairly responsive, though we didn't hear back from a small minority.

Gender and racial diversity on FTSE 350/100 boards: Almost all the FTSE 100 became compliant with the Parker Review target for ethnic diversity. There was still work to be done with the FTSE 350 but the vast majority are now compliant with the government's FTSE Women Leaders target of 33% female representation.

Collaborative engagements that included Rathbones

Successful | Partially successful | Limited progress

Environmental

IIGCC and physical climate risks and opportunities: Updates by the Institutional Investors Group on Climate Change (IIGCC) showed limited progress on objectives by target companies. However, some target companies are responding with changes that better align with what the IIGCC is asking for.

IIGCC and banks: As with the IIGCC engagement on physical climate risks and opportunities, IIGCC updates indicated limited progress on objectives by target companies. However, in this case too, some target companies are responding with changes that better align with what the IIGCC is asking for.

Climate Action 100+: We maintained our lead role in engagement with the UK energy company SSE and as a supporting investor for fellow UK energy company National Grid. A number of meetings were held in 2022. We developed stronger relationships with both companies and saw them make good progress in improving their net zero plans.

Social

Tailings dams: The engagement has come to its natural conclusion because of its success: a new Global Industry Standard on Tailings Management has been established and run by an independent body, with every major mining company signing up to this initiative. Tailings dams store mining waste.

Find it, Fix it, Prevent it (FIFIPI): We held a meeting with Mitchells & Butlers as part of this campaign for hospitality businesses to find victims of slavery within their supply chain and support their rehabilitation. We were very pleased with this engagement because we were one of the few investors involved in the campaign that held a physical meeting rather than a call. We believe this gave us better insight into what the company was doing than could have been achieved through a call.

Governance

Climate risk and corporate accounts: Investors held meetings with Rio Tinto and ThyssenKrupp to set out their expectations for Paris-aligned corporate accounts. The year saw good continuing engagement in a campaign to press the Big Four audit firms to conduct net zero-aligned audits.

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Head office: 8 Finsbury Circus, London EC2M 7AZ.

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